KPMG

KING COUNTY PUBLIC HOSPITAL DISTRICT NO. 2
(d/b/a EvergreenHealth)

Financial Statements

December 31, 2018 and 2017

(With Independent Auditors' Report Thereon)

KING COUNTY PUBLIC HOSPITAL DISTRICT NO. 2
(d/b/a EvergreenHealth)

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KPMG LLP
Suite 2900
1918 Eighth Avenue
Seattle, WA 98101

Independent Auditors' Report

The Board of Commissioners
King County Public Hospital District No. 2
d/b/a EvergreenHealth:

Report on the Financial Statements

We have audited the accompanying financial statements of King County Public Hospital District No. 2, d/b/a EvergreenHealth, which comprise the statements of net position as of December 31, 2018 and 2017, and the related statements of revenue, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We did not audit the financial statements of Public Hospital District No. 1, Snohomish County, Washington, d/b/a EvergreenHealth Monroe, a component unit, which statements reflect total assets constituting 100% of total assets at December 31, 2018 and 2017, respectively, and total revenue constituting 100% of total revenue of the discretely presented component unit for the years then ended. Those statements were audited by other auditors, whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for EvergreenHealth Monroe, is based solely on the report of the other auditors. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, based on our audits and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of King County Public Hospital District No. 2, d/b/a EvergreenHealth, as of December 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 17 be presented to supplement the financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the financial statements, and other knowledge we obtained during our audits of the 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.

KPMG LLP

Seattle, Washington
May 30, 2019

This discussion and analysis of King County Public Hospital District No. 2, d/b/a EvergreenHealth (the District) provides an overview of the District's financial activities for the years ended December 31, 2018 and 2017. Please read it in conjunction with the District's financial statements, which follow this analysis.

The District is a municipal corporation of the State of Washington formed under the provisions of Chapter 70.44 of the Revised Code of Washington. The District is considered a political subdivision of the State of Washington and is allowed by law to be its own Treasurer.

The District includes the incorporated cities of Kirkland, Redmond, Woodinville, Kenmore, and Duvall, portions of Bothell, Sammamish, and Carnation, as well as adjacent unincorporated areas.

The District's primary operations include Evergreen Hospital Medical Center (the Medical Center), an acute care hospital with 318 licensed beds and a 15-bed freestanding inpatient hospice care center, representing the ninth largest provider in the Puget Sound.

Type of beds	Number of beds	License category
Critical care	20	Acute
Family maternity	36	Acute
Acute rehabilitation	14	Acute rehab
Medical/surgical	205	Acute
Neonatal intensive care unit (Level II=29 beds; Level III=14 beds)	43	Acute/newborn
Total Beds for Hospital Acute License	318	
Hospice Care Center	15	Hospice

The Medical Center is accredited by the Joint Commission, a nonprofit organization that accredits more than 21,000 healthcare organizations and programs in the United States. The Medical Center provides clinical excellence in primary care and over 80 specialties, including, heart and vascular care, 24-hour level III trauma emergency care, cancer care, diabetes care, musculoskeletal and spine care, sleep services, oncology, surgical care, orthopedics, neurosciences, women's and children's services, and pulmonary care. Home care and hospice services cover both King and Snohomish counties as the largest provider in the Puget Sound.

The employed physician practices comprise 74 and 81 primary care providers in 2018 and 2017, respectively, and 241 and 237 specialty care providers in 2018 and 2017, respectively. Since 1972, the District's patient and family centered care philosophy, combined with its commitment to advancing medical solutions, has enabled the District to focus on providing excellent patient care.

The District is governed by a board of seven publicly elected commissioners, each elected by district residents to serve a six-year term in accordance with the laws of the State of Washington. The commissioners have delegated day-to-day operations of the District and the Medical Center to the chief executive officer/superintendent.

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Utilization Statistics

Historical patient utilization data of the District's facilities is shown in the following table:

Utilization statistics	2018	2017	2016
Hospital Acute Licensed Care Beds	318	318	318
Hospice Care Center Licensed Beds	15	15	15
Acute care admissions	15,068	15,281	15,672
Acute care adjusted admissions	35,997	34,539	33,125
Acute care patient days	57,848	61,154	62,133
Acute care adjusted patient days	146,113	137,937	131,248
Acute care average length of stay	4.1	4.0	4.0
Occupancy (based on acute care licensed beds)	49.8%	52.7%	53.5%
Observation Days	2,930	2,810	1,607
Inpatient surgeries	3,301	3,522	3,391
Outpatient surgeries	12,258	15,321	14,437
Home health episodes and admissions	10,465	9,954	9,878
Home Hospice program days	183,145	180,472	204,343
Emergency room visits	57,153	57,669	56,660
Primary care work relative value units (wRVUs)	309,543	297,695	199,443
Specialty care wRVUs	820,201	744,453	688,552

Economic Factors Affecting the Current Environment and Future Direction of the District

The future direction of EvergreenHealth is guided by its vision to "create an inclusive community health system that is the most trusted source for healthcare solutions." The District takes a long-term, strategic view on the future of healthcare in the community and responds with plans that consider that perspective. Challenges and opportunities that face the District are similar to those that face the healthcare industry across the country. Among those issues are:

- **Financial Performance**: The District continues to implement service enhancement and growth plans, discussed below, which require significant capital outlays. The investment in new and expanded facilities may put initial financial constraints on the organization; however, management believes the District is positioned to better serve the needs of the community.
- **Competition**: The Puget Sound has experienced increased market consolidation and collaboration between healthcare providers over the past several years. In addition, competitors have opened traditional and non-traditional healthcare facilities both within and around the District boundaries with the intention of drawing patients from the service area.
- **Operating Costs**: The volume indicators for acute care adjusted patient days increased while surgery counts decreased when compared to 2017. The District has continued working to manage its operating costs in line with volumes. Labor is the most significant operating cost for the District, representing over 66% of annual expenses. During 2018 and 2017, the District continued to implement various cost saving initiatives including supply chain standardization and improved labor productivity management.

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- **Regulatory Environment**: Continued focus by regulatory agencies on the healthcare industry may impact the District.
- **Labor Availability:** Throughout 2018, the District continued its Nurse Tech roles and RN Residency programs and increased its New-To-Specialty programs in order to decrease reliance on RN agency personnel and to address RN retirement. Labor shortages continued for various positions. Approximately 47% of the District's 4,533 employees are members of one of four labor unions. In May 2018, the District completed negotiations of its labor contract with the International Union of Operating Engineers (IUOE), which represents approximately 20 Plant Operations employees. In October 2018, the District began negotiations of its labor contract with the Washington State Nurses Association (WSNA), which represents approximately 1,080 Registered Nurses. Those negotiations are still ongoing. In April 2019, the District will begin negotiations of its labor contract with the United Food and Commercial Workers (UFCW), which represents approximately 190 professional/technical employees.
- **Contracting/Risk-Sharing Arrangements**: The District has three pay-for-performance contracts in effect with payors as of 2019. Via the Eastside Health Network, EvergreenHealth participates in an additional five value-based commercial contracts plus four Medicare Advantage contracts. All of these contracts are "layered" on top of existing fee-for-service arrangements between the District and those payors and provides for incentives based upon efficiency and quality performance. See additional discussion under alliances.
- **Payor Reimbursement**: Reimbursement for patient services from federal, state, and private insurance payors continues to be a concern as healthcare costs continue to rise. The District monitors reimbursement closely and works with payors in an effort to maintain payment levels and earn value-based reimbursement model revenue.
- **Partnerships**: During 2018 and 2017, the District continued to develop its strategic alliances with Seattle Cancer Care Alliance (SCCA), EvergreenHealth Monroe (EHM) and Overlake Medical Center.

  Overlake Medical Center – In 2016, the Boards of the District and Overlake Medical Center approved the exploration of a joint venture called *Eastside Health Alliance*. In November 2016, a letter of intent to form the joint venture was signed by the District and Overlake Medical Center. The joint venture, which is designed to advance the shared mission of improving the health of Puget Sound's Eastside community, was subsequently approved by both Boards in January 2017. Eastside Health Alliance has been focusing on three specific areas guided by a joint venture Board, comprising three board members and the CEO from each organization. The three areas include:

  – A coordinated quality and safety program
  – An Eastside-focused clinically integrated network, Eastside Health Network, that combined the Overlake Provider Network and EvergreenHealth Partners, LLC
  – Service line collaborations in cardiac services and neurosciences

  SCCA – The Halvorson Cancer Center, in collaboration with SCCA, has a shared vision to provide the highest quality, patient-centered, innovative and integrated care for cancer patients at EvergreenHealth. The partnership connects patients to promising new treatments with on-site access to the innovative research programs and breakthrough clinical trials of SCCA. There were over 1,200 cancer cases served by the partnership in 2018, signaling a 9% increase from the prior year.

EvergreenHealth Monroe (EHM) – The District's partnership with EHM continues to grow. EHM is governed by the Alliance Governance Board. Both organizations remain independently and separately governed, licensed, and accredited. The purpose of the affiliation is to provide EHM the ability to better serve its community through enhanced clinical services and to adopt the District's approaches to clinical outcomes, patient safety, and patient experience. Governmental Accounting Standards Board (GASB) No. 14 establishes that financial statements of the reporting entity generally should allow the users to distinguish between the primary government and its component units. EHM is reported within the District's financial statements as a discretely presented component unit in accordance with government accounting standards.

- Other substantial changes are anticipated in the U.S. healthcare system including numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, the Affordable Care Act and uncertainty surrounding the act, reimbursement of healthcare providers, and the legal obligations of health insurers, providers, and employers. Increasing patient obligations through high deductible plans and increased premiums has the potential for higher bad debt experience. Management will continue evaluating how it will respond to various healthcare reform components as they develop.
- The District recognizes that providing the community with high-quality healthcare goes beyond offering outstanding programs and services. As the community continues to grow and age, the District must keep pace with the need for more types of services. The 2018 population within the District's boundaries is estimated to be 321,170. Population is projected to grow 8.124% over the next five years and reach 347,262 in 2022 according to ESRI. The most recent version of the District's Master Campus Plan, filed with the City of Kirkland in February 2017, includes facility and service expansions based on projected needs.
- In 2018, the District initiated or completed the following related projects:
  - Welcomed a new Board of Commissioner, Todd Banks
  - Appointed a new Chief Executive Officer, Dr. Amy Beiter
  - Opened the new interventional biplane suite
  - Secured Eastside Health Network contract with Microsoft
  - Improved physician work flow through the Model Experience Project
  - Added new features to the online patient portal, making sign up easier and enhancing the user experience with online appointment scheduling and mobile access
  - Improved labor management through the Workforce Optimization Committee
  - Implemented Cerner at the Evergreen Surgical Center
  - Implemented tele-psych for the in-home mental health program
  - Opened Mill Creek Primary Care
  - Finalized the 2020–2023 Master Facility Plan

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- Launched a new internal communications platform called Treehouse
- Recognition:
  - Received four stars from CMS for Home Health quality and patient satisfaction (the only Home Health agency in King County to receive these ratings)
  - Recognized by Healthgrades as the Distinguished Hospital for Clinical Excellence for the ninth time
  - Recognized by Healthgrades as America's 100 Best Hospitals for the second consecutive year
  - Named a winner of the Healthgrades 2018 Outstanding Patient Experience Award (one of only six other hospitals in Washington State and among the top 15 percent of hospitals nationwide)
  - Recognized by the Washington Health Alliance for Remarkable Quality, Patient Experience, and Price in its 2018 Hospital Value Report, as one of the top four primary care groups in Washington state
  - Named by 425 Magazine as 'Best Hospital & Health System' for the second consecutive year

Overview of the Financial Statements

The District's financial statements consist of three components: statements of net position; statements of revenue, expenses, and changes in net position; and statements of cash flows. The activities of EvergreenHealth Foundation (the Foundation) are included with the District's financial statements as a blended component unit. These financial statements and related notes provide information about the activities of the District, including resources held by the District designated for specific purposes. The statements of net position includes all of the District's assets and liabilities, using the accrual basis of accounting, as well as an indication about which assets can be utilized for general purposes and which are restricted for a specific purpose. The statements of revenue, expenses, and changes in net position report all of the revenue, expenses, and changes in net position during the time periods indicated. The statements of cash flows report the cash provided by the District's operating activities, as well as other cash sources such as investment income and issuance of new debt, and use of cash such as cash payments for capital asset additions and improvements and repayment of debt.

On March 1, 2015, the District entered into a Strategic Alliance Agreement with EHM. GASB standards require that this entity be presented as a discrete component unit; therefore, its financial position at December 31, 2018 and 2017 and the results of its operations for the years ended December 31, 2018 and 2017 are included with the District in a separate column for financial statement presentation purposes (note 1 to the financial statements).

The analysis presented below represents the District and its blended component unit (the Foundation), but excludes the financial position and results of operations of its discrete component unit (EHM), unless otherwise noted.

Summary of Statements of Net Position

(In thousands)

		2018	2017	2016
Cash and cash equivalents	$	52,448	43,503	22,290
Patient accounts receivable, less allowance for uncollectible accounts		92,814	82,519	77,659
Other current assets		27,801	28,656	23,943
Total current assets		173,063	154,678	123,892
Assets limited as to use, less current portion of amounts required for current liabilities		156,631	147,130	183,495
Capital assets, net		319,041	327,097	310,926
Other assets		33,576	32,420	29,380
Total assets		682,311	661,325	647,693
Deferred outflows of resource:				
Deferred loss on refunding		3,070	3,645	4,278
Total assets and deferred outflows of resources	$	685,381	664,970	651,971
Current portion of long-term debt and capital lease obligations	$	13,752	13,101	12,440
Other current liabilities		84,469	73,348	80,095
Total current liabilities		98,221	86,449	92,535
Long-term liabilities		199,750	215,997	230,887
Total liabilities		297,971	302,446	323,422
Deferred inflows of resources:				
Deferred proceeds		—	19,139	—
Total deferred inflow of resources		—	19,139	—

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Summary of Statements of Net Position

(In thousands)

		2018	2017	2016
Net position:				
Invested in capital assets, net of related debt	$	113,169	105,899	74,838
Restricted		10,154	7,747	8,172
Unrestricted		264,087	229,739	245,539
Total net position		387,410	343,385	328,549
Total liabilities and net position	$	685,381	664,970	651,971

Current Assets

Current assets consist of cash and cash equivalents, current portion of board-designated and restricted assets, and other current assets that are expected to be converted to cash within one year. Current assets also include net patient accounts receivable valued at the estimated net realizable amount due from patients and insurers. Key ratios include:

- Current ratio: This is a liquidity ratio that measures the District's ability to pay short-term obligations or debts due within one year. The current ratio is calculated by dividing current assets by current liabilities.
- Days in accounts receivable: This is the number of days it takes the District to collect outstanding invoices. The ratio is calculated by dividing the ending accounts receivable by the total operating revenue for the period and multiplying it by 365 days or the number of days in the period.
- Days cash on hand: This demonstrates how long in days the District could meet operating expenses with the amount of cash currently available. This is calculated by adding cash and cash equivalents, board-designated cash and investments, less cash for EvergreenHealth Network, EvergreenHealth Partners and the Foundation, and multiplying by 365 days, then dividing the amount by total operating expenses less annual depreciation.

Key Ratios	2018	2017	2016
Current Ratio	1.8	1.8	1.3
Days in AR (Net)	48.0	44.7	44.0
Days Cash on Hand	109.8	98.3	91.5

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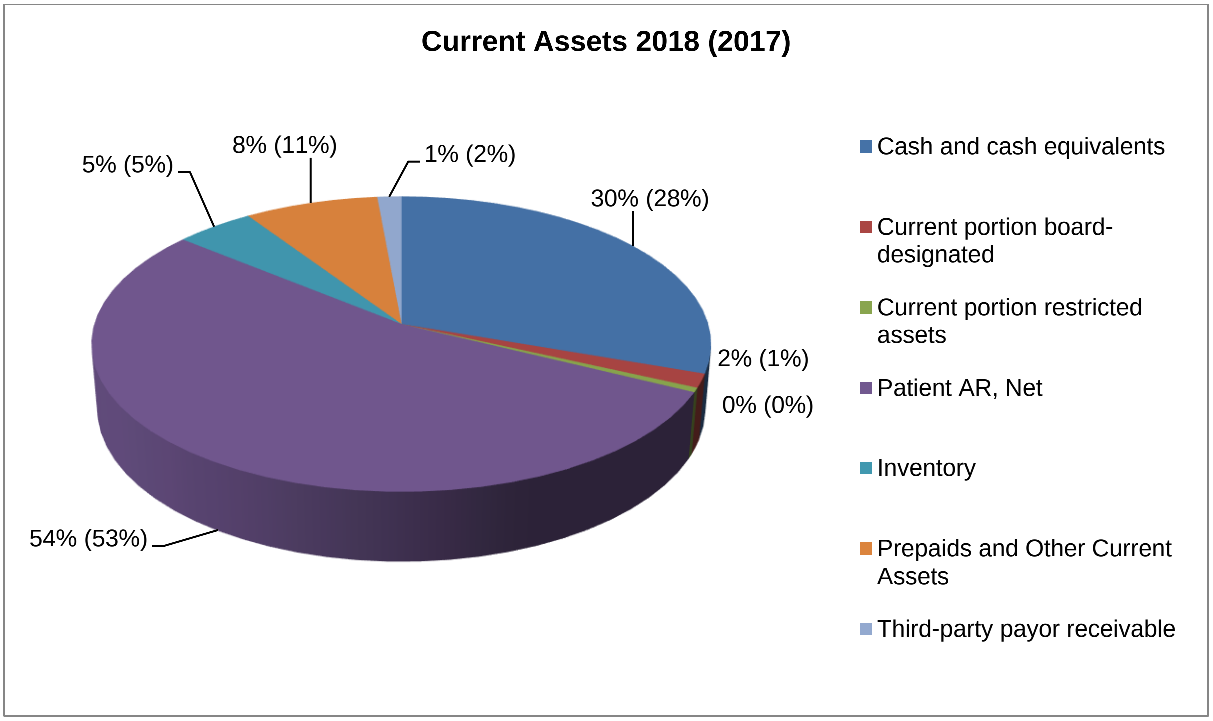
Total current assets were $173.1 million as of December 31, 2018, compared to $154.7 million as of December 31, 2017. The composition of 2018 current assets and comparison to prior year are illustrated below.

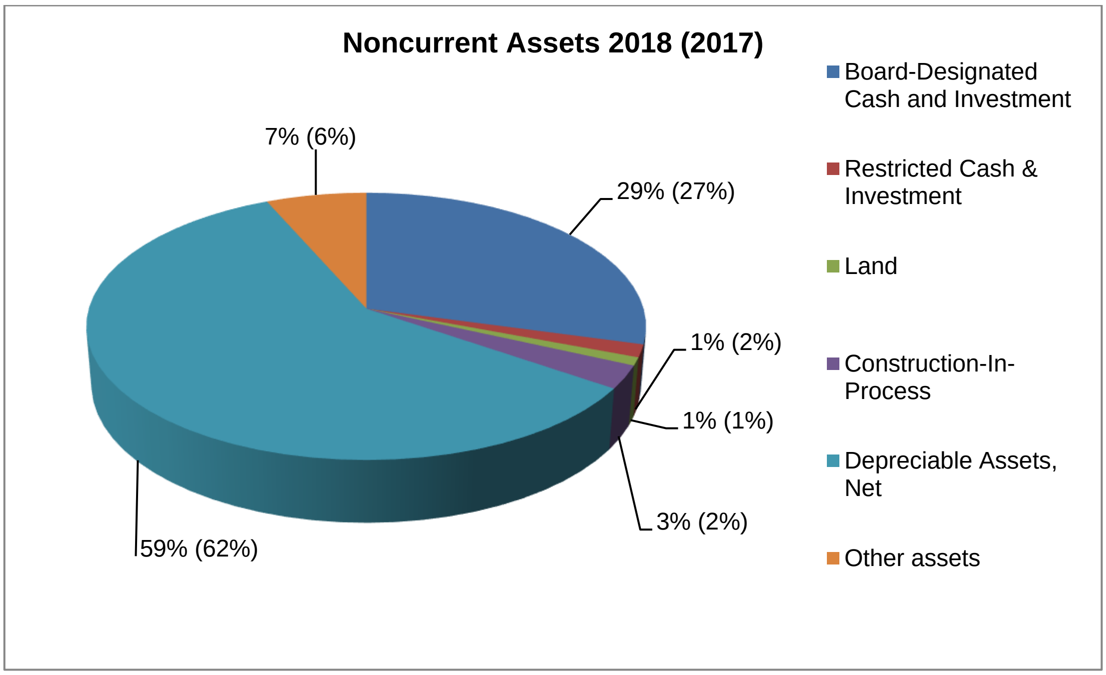


Current assets in 2018 increased by $18.4 million compared to 2017 primarily due to increases of $10.3 million in net patient accounts receivable related to price and volume increases, $8.9 million in cash and cash equivalents primarily due to improved operating performance as seen in the increase in the days cash on hand; 110 days in 2018 compared to 98 in 2017 and an increase in operating revenue; $701 million in 2018 compared to $669 million in 2017.

Current assets in 2017 increased by $30.8 million compared to 2016 primarily due to increases of $4.8 million in net patient accounts receivable related to price and volume increases, $21.2 million in cash and cash equivalents primarily related to an advanced payment related to the sale of the District's equity interests in its PacLab joint venture, and $2.8 million in prepaid expenses and other current assets.

Noncurrent Assets

Noncurrent assets consist of restricted and board-designated assets held for debt service, capital improvements, community service programs and other operations. Total noncurrent assets were $509.2 million as of December 31, 2018, compared to $506.6 million as of December 31, 2017. The composition of noncurrent assets in 2018 and comparison to prior year are illustrated below.

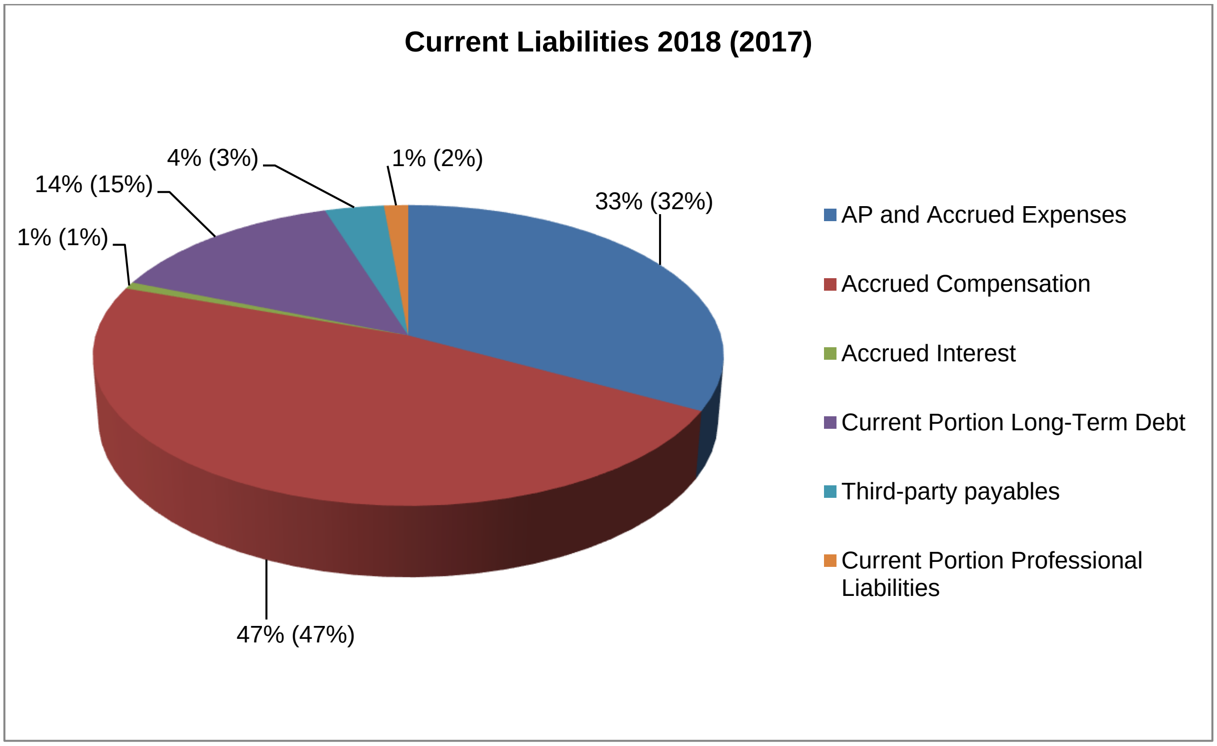


Capital assets, net of accumulated depreciation decreased approximately $8.1 million from 2017 to 2018 and increased $16.2 million from 2016 to 2017. The District continues to devote resources for capital projects and improvements, including significant components of the master facility plan. During 2018 and 2017, the District invested approximately $27.7 million and $50.2 million, respectively, in buildings, information technology, and equipment. This increase in capital assets was offset by $35.8 million and $34.4 million in depreciation expense in 2018 and 2017, respectively.

Restricted and board-designated cash and investments increased approximately $9.5 million from 2017 to 2018 and decreased approximately $36.4 million from 2016 to 2017. The increase in the current year is primarily due to funds transferred from the general fund account to the investment account to cover planned spending for the 2015 Limited Tax General Obligation (LTGO) Series B bond proceeds in accordance with the long-term master facility plan, as approved by the District's Board in July 2015.

Current Liabilities

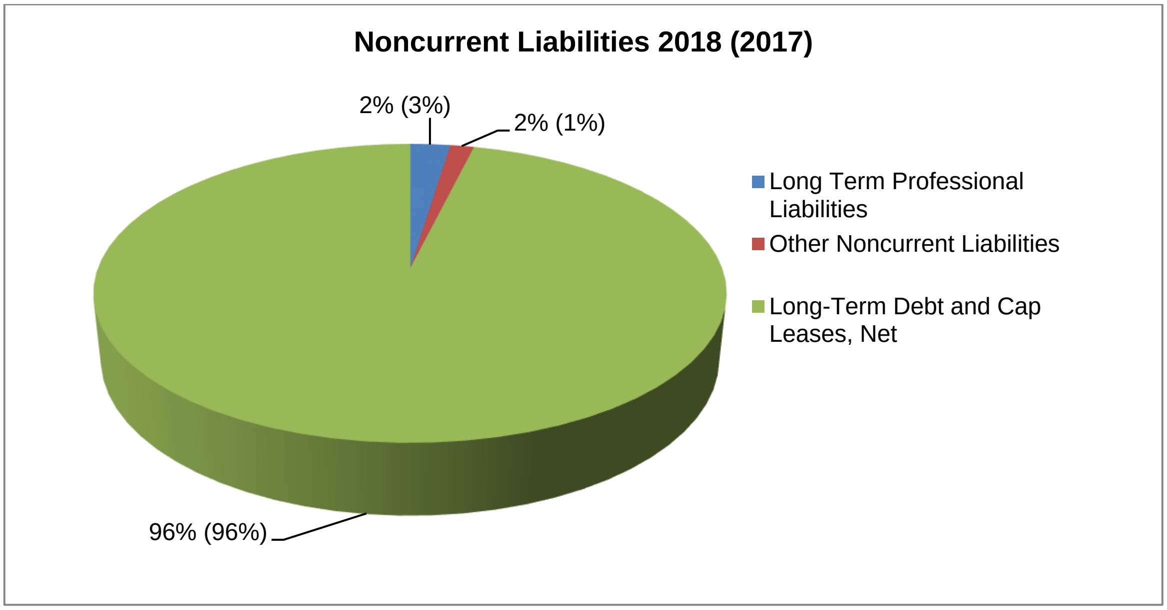
Current liabilities consist of accounts payable, accrued compensation and other liabilities that are expected to be paid within one year, including current portion of long-term debt and professional liabilities. Total current liabilities were $98.2 million as of December 31, 2018, compared to $86.4 million as of December 31, 2017. 2018 composition of current liabilities and comparison to prior year are illustrated below.



Current liabilities increased approximately $11.8 million from 2017 to 2018 and decreased approximately $6.1 million from 2016 to 2017, which is primarily attributable to an increase in both accounts payable and accrued expenses of $5.1 million and an increase in accrued compensation of $5.8 million. The change in accounts payable and accrued expenses is primarily due to the timing of regular accounts payable cycles. The change in accrued compensation is due a combination of a longer pay period to accrue for in 2018, management performance outcome payouts of $1.7 million and an increase in employee contribution to the retirement account of $1.6 million in the current year.

Noncurrent Liabilities

Noncurrent liabilities consist of long-term debt, capital lease obligations, and professional liability reserves. Total noncurrent liabilities were $199.8 million as of December 31, 2018, compared to $216.0 million as of December 31, 2017. The 2018 composition of noncurrent liabilities and comparison to prior year are illustrated below.



Noncurrent liabilities decreased approximately $16.2 million and $14.9 million from 2017 to 2018 and 2016 to 2017, respectively, primarily due to debt payments in accordance with the established debt service schedule.

Net Position

Investment in capital assets, net of related debt increased approximately $7.3 million, or 6.9%, from 2017 to 2018 and increased approximately $31.1 million, or 41.5%, from 2016 to 2017. The current year increase is attributable to a decrease in net capital assets of approximately $8.1 million offset by related debt obligations of approximately $15.3 million due to debt payments in accordance with amortization schedules.

Restricted net position (expendable and nonexpendable), representing resources with temporary or permanent donor restrictions, remained relatively consistent from 2017 to 2018 and 2016 to 2017.

Unrestricted net position, which includes other funds available to the District that do not meet the definition of restricted or net investment in capital assets, increased approximately $34.3 million, or 15%, from 2017 to 2018 and decreased approximately $15.8 million, or 6.4%, from 2016 to 2017. The current year increase is driven by net income and capital grants and contributions of approximately $44.0 million, offset by approximately $9.7 million to fund 2018 capital projects. The $15.8 million decrease from 2016 to 2017 was driven by 2017 net income and capital grants and contributions of approximately $14.8 million, offset by net increases of approximately $30.6 million, which are accounted for in the net investment in capital asset and restricted categories discussed above.

Summary of Revenue, Expenses, and Changes in Net Position
(In thousands)

	2018	2017	2016
Operating revenue:			
Net patient service revenue	$ 664,805	627,360	597,304
Other operating revenue	35,920	41,906	42,817
Total operating revenue	700,725	669,266	640,121
Operating expenses:			
Labor and employee benefits	459,932	443,499	417,823
Supplies, purchased services, and other	201,216	195,888	194,232
Depreciation and amortization	35,523	34,229	32,019
Total operating expenses	696,671	673,616	644,074
Excess (deficit) of revenue over expenses from operations	4,054	(4,350)	(3,953)
Nonoperating income, net of expenses:			
Property taxes	26,216	25,731	25,201
Interest and amortization expense	(8,027)	(8,490)	(8,914)
Investment income	2,661	1,404	1,882
Other, net	18,223	319	(163)
Net nonoperating income	39,073	18,964	18,006
Excess of revenue over expenses	43,127	14,614	14,053
Capital grants and contributions	898	222	1,227
Total change in net position	44,025	14,836	15,280
Net position, beginning of year	343,385	328,549	313,269
Net position, end of year	$ 387,410	343,385	328,549

Financial Highlights

Revenue

Sources of Patient Revenue

The District derives a substantial portion of its operating revenue from federal and state programs and insurance plans that pay for all or a portion of the healthcare services provided to its patients. As a consequence, the District's operating revenue depends to a great extent on the availability and level of reimbursement or payment under those programs and contracts.

In 2018, gross patient revenue increased by approximately $61.8 million or 3.4%. Gross patient revenue is the total fees charged to patients for services. Ancillary service outpatient revenue driven by surgery and pharmacy revenue increased $78.9 million, or 7.9%, which was offset by a decrease in ancillary service inpatient revenue and hospital inpatient revenue of $11.6 million and $6.1 million, respectively and an increase of $0.6 million in outpatient service revenue. Furthermore, total average length of stay (excluding NICU) was 4.1 days and 4.0 days in 2018 and 2017, respectively. Total surgery cases and home health volume increased 8.3% and 5.1%, respectively, while outpatient hospice volumes increased 1.5%.

In 2017, gross patient revenue increased by approximately $125.0 million or 7.4%. Gross patient revenue is the total fees charged to patients for services. Primary care and specialty care revenue increased $23.9 million, or 53.2%, and $22.5 million, or 15.2%, respectively. The significant increase in primary care is tied to the acquisition of Lakeshore Totem Lake and Lakeshore Bothell primary care clinics. Also contributing to the gross revenue growth was a targeted rate increase of 2.6% overall implemented on January 1, 2017. Total average length of stay (excluding NICU) remained constant at 4.0 days. Total surgery cases and home health volume increased 5.7% and 0.8%, respectively, while outpatient hospice volumes decreased 11.7%.

The following table sets forth the percentages of the District's hospital gross patient revenue applicable to various programs and plans for the fiscal years ended December 31, 2018, 2017, and 2016.

	2018	2017	2016
Non-Government third party payors	47.3%	47.9%	47.2%
Medicare	41.1	39.7	40.3
Medicaid	10.3	11.3	11.2
Patient self-pay	1.3	1.1	1.3

In 2018, net patient service revenue increased by approximately $37.4 million or 6.0%. Net patient revenue consists of gross patient revenue less contractual adjustments, bad debt, and charity. This increase was driven by growth in patients served, coupled with lower bad debt and charity adjustments in 2018. Other operating revenue decreased approximately $.6 million, or 14.3%, primarily due to the sale of PacLab and the elimination of related revenue streams.

In 2017, net patient service revenue increased by approximately $30.1 million or 5.0%. Net patient revenue consists of gross patient revenue less contractual adjustments, bad debt, and charity. This increase was driven by the top line growth mentioned above, partially offset by higher bad debt, charity care and administrative adjustment deductions in 2017. Other operating revenue decreased approximately $1.0 million, or 2.1%, tied to decreased federal grant dollars as a result of several programs that transitioned to the County and State. There is a corresponding decrease in operating expenses as a result of the transition.

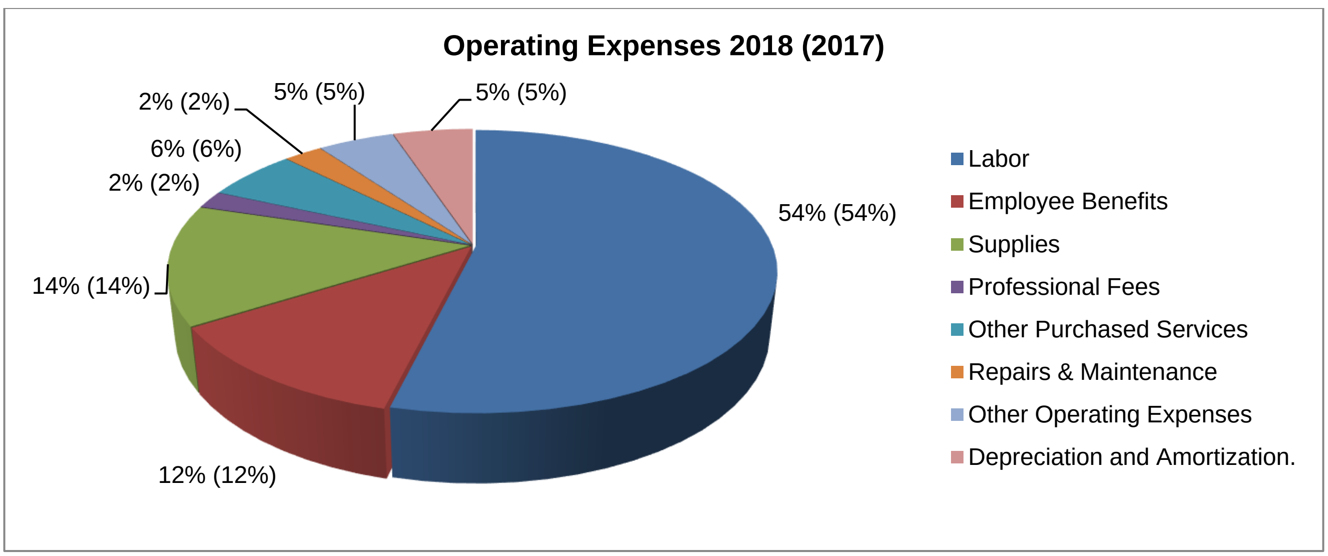
Operating Expenses

Labor, including contract labor, increased approximately $14.9 million, or 4.2%, and $19.9 million, or 5.8%, in 2018 and 2017, respectively. This increase is due to employee salary increases as well as premium pay related to contract labor and employee overtime due to labor shortages. The District's average employed and contracted full-time equivalents remained constant at 3,752 as of December 31, 2018 and 2017, respectively, compared to 3,629 in 2016.

Employee benefit expenses increased $1.5 million, or 1.8%, and $5.8 million, or 7.4%, in 2018 and 2017, respectively. This was primarily due to increased medical plan, social security and retirement plan costs.

Supplies, purchased services, repairs and maintenance services and other increased approximately $5.3 million, or 2.7%, and $1.7 million, or 0.9%, in 2018 and 2017, respectively. The increase is due to overall hospital growth, medical supply costs and professional fees relating to various legal matters.

Total operating expenses in 2018 and 2017 of $696.7 million and $673.6 million, respectively, include expenses related to tax-supported community programs for which the offsetting revenue is included in nonoperating income.



Nonoperating Income, Net of Expenses

In 2018, nonoperating income net of expenses increased $20.1 million, or 106%, from $19.0 million in 2017 to $39.1 million in 2018. The increase is due to the recognition of $19.1 million of proceeds from the sale of PacLab. The payment was received in 2017 but the closing and the associated sale were effective February 5, 2018, at which time the deferred inflow of resources was recognized as nonoperating income.

In 2017, nonoperating income net of expenses increased $1.0 million, or 5.6%, from $18.0 million in 2016 to $19.0 million in 2017. The increase is largely driven by an increase of $0.5 million in property tax revenue, which increased the amount of funding available for community programs over prior year.

Contacting the District's Financial Management

This financial report provides the reader with a general overview of the District's finances and operations. If you have questions about this report or need additional financial information, please contact the Chief Financial Officer or Director of Financial Reporting at EvergreenHealth, 12040 NE 128th Street, Kirkland, Washington 98034.

KING COUNTY PUBLIC HOSPITAL DISTRICT NO. 2
(d/b/a EvergreenHealth)

Statements of Net Position

December 31, 2018 and 2017

(In thousands)

Assets		2018 District	2018 Component Unit EHM	2017 District	2017 Component unit EHM (as restated)
Current assets:					
Cash and cash equivalents	$	52,448	4,942	43,503	733
Current portion board-designated assets		2,593	—	1,479	—
Current portion of assets restricted as to use		840	—	1,098	—
Patient accounts receivable, less allowance for uncollectible accounts of $21,274 and $1,026 in 2018 and $16,993 and $895 in 2017, respectively		92,814	6,378	82,519	5,989
Inventory		8,119	1,125	7,448	1,025
Prepaid expenses and other current assets		13,764	551	15,867	941
Third-party payor receivable		2,485	61	2,764	1,210
Total current assets		173,063	13,057	154,678	9,898
Assets limited as to use, less current portion of amounts required for current liabilities:					
Board-designated cash and investments		148,901	—	139,393	—
Restricted cash and investments		7,730	—	7,737	—
		156,631	—	147,130	—
Capital assets:					
Land		4,914	1,879	4,914	1,879
Construction in progress		14,280	414	9,699	880
Depreciable capital assets, net of accumulated depreciation		299,847	10,785	312,484	11,494
		319,041	13,078	327,097	14,253
Other assets		33,576	—	32,420	—
Total assets		682,311	26,135	661,325	24,151
Deferred outflows of resources:					
Deferred loss on refunding		3,070	—	3,645	39
Related to other postemployment benefits		—	365	—	—
Total assets and deferred outflows of resources	$	685,381	26,500	664,970	24,190

(Continued)

KING COUNTY PUBLIC HOSPITAL DISTRICT NO. 2
(d/b/a EvergreenHealth)

Statements of Net Position

December 31, 2018 and 2017

(In thousands)

Liabilities and Net Position		**2018** District	**2018** Component Unit EHM	**2017** District	**2017** Component unit EHM (as restated)
Current liabilities:					
Accounts payable and accrued expenses	$	32,373	3,465	27,311	5,037
Accrued compensation and related liabilities		46,591	2,457	40,753	2,491
Accrued interest payable		729	75	781	77
Current portion of long-term debt and capital lease obligations		13,752	675	13,101	761
Third-party payor payable		3,390	—	2,807	—
Estimated current portion of professional liability		1,386	—	1,696	—
Other accrued liabilities		—	243	—	213
Total current liabilities		98,221	6,915	86,449	8,579
Long-term estimated professional liability		4,785	—	5,178	—
Other noncurrent liabilities		2,845	3,258	2,723	1,988
Long-term debt and capital lease obligations, net of current portion		192,120	16,938	208,096	17,598
Net other postemployment benefits liability		—	6,083	—	5,099
Total liabilities		297,971	33,194	302,446	33,264
Deferred inflows of resources:					
Deferred proceeds		—	—	19,139	—
Related to other postemployment benefits		—	177	—	201
Net position:					
Investment in capital assets, net of related debt		113,169	(4,535)	105,899	(4,106)
Restricted:					
Expendable for specific activities		6,276	—	5,316	—
Expendable for debt service		806	253	715	250
Nonexpendable permanent endowments		3,072	—	1,716	—
Unrestricted		264,087	(2,589)	229,739	(5,419)
Total net position		387,410	(6,871)	343,385	(9,275)
Total liabilities, deferred inflows of resources and net position	$	685,381	26,500	664,970	24,190

See accompanying notes to financial statements.

KING COUNTY PUBLIC HOSPITAL DISTRICT NO. 2
(d/b/a EvergreenHealth)

Statements of Revenue, Expenses, and Changes in Net Position

Years ended December 31, 2018 and 2017

(In thousands)

	2018		2017	
	District	**Component Unit EHM**	**District**	**Component unit EHM (as restated)**
Net patient service revenue (net of provision for bad debts of $21,135 and $4,790 in 2018 and $23,449 and $4,797 in 2017, respectively)	$ 664,805	46,053	627,360	41,773
Other operating revenue	35,920	2,261	41,906	2,030
Total operating revenue	700,725	48,314	669,266	43,803
Expenses:				
Labor	375,148	19,331	360,209	19,333
Employee benefits	84,784	8,624	83,290	8,240
Supplies	95,623	6,031	94,837	5,763
Professional fees	13,770	5,631	10,787	4,399
Other purchased services	40,685	4,299	41,357	3,854
Repairs and maintenance	17,167	888	15,926	967
Other operating expenses	33,971	3,129	32,981	3,040
Depreciation and amortization	35,523	1,954	34,229	2,007
Total operating expenses	696,671	49,887	673,616	47,603
Excess (deficit) of revenue over expenses from operations	4,054	(1,573)	(4,350)	(3,800)
Nonoperating income, net of expenses:				
Property taxes	26,216	4,736	25,731	4,648
Interest and amortization expense	(8,027)	(1,008)	(8,490)	(1,070)
Investment income	2,661	—	1,404	—
Other, sale of assets	18,163	—	—	—
Other, net	60	—	319	—
Net nonoperating income	39,073	3,728	18,964	3,578
Excess (deficit) of revenue over expenses	43,127	2,155	14,614	(222)
Capital grants and contributions	898	249	222	209
Total change in net position	44,025	2,404	14,836	(13)
Net position, beginning of year	343,385	(9,275)	328,549	(9,581)
Change in accounting principle	—	—	—	319
Net position, end of year	$ 387,410	(6,871)	343,385	(9,275)

See accompanying notes to financial statements.

KING COUNTY PUBLIC HOSPITAL DISTRICT NO. 2
(d/b/a EvergreenHealth)

Statements of Cash Flows

Years ended December 31, 2018 and 2017

(In thousands)

	2018		2017	
	District	Component Unit EHM	District	Component unit EHM (as restated)
Cash flows from operating activities:				
Cash received from and on behalf of patients	$ 659,605	46,814	620,943	40,587
Payments to suppliers and contractors	(189,666)	(20,412)	(214,677)	(16,166)
Payments to employees	(454,094)	(27,955)	(440,449)	(27,254)
Distributions received from joint ventures	4,006	—	8,664	—
Other – cash payments	(976)	—	—	—
Other – cash receipts	27,682	3,326	31,306	2,093
Net payments provided by (used in) operating activities	46,557	1,773	5,787	(740)
Cash flows from noncapital financing activity:				
Property taxes received for community programs	4,868	4,736	4,343	4,648
Net cash provided by noncapital financing activity	4,868	4,736	4,343	4,648
Cash flows from capital and related financing activities:				
Purchases of capital assets	(33,261)	(778)	(44,346)	(2,717)
Proceeds from sale of capital assets	—	—	34	—
Principal payments on long-term debt and capital lease obligations	(13,096)	(761)	(12,442)	(891)
Payments for interest on long-term debt	(9,776)	(1,010)	(10,354)	(1,072)
Proceeds from issuance of long-term debt	—	—	—	387
Capital contributions	—	249	—	209
Proceeds from property taxes related to debt service	21,348	—	21,388	—
Net cash used in capital and related financing activities	(34,785)	(2,300)	(45,720)	(4,084)
Cash flows from investing activities:				
Purchases of board-designated assets and assets restricted as to use	(45,120)	—	1,678	—
Proceeds from sale of board-designated assets and assets restricted as to use	34,764	—	34,580	—
Investment income	2,661	—	1,406	—
Other	—	—	19,139	—
Net cash (used in) provided by investing activities	(7,695)	—	56,803	—
Net increase (decrease) in cash and cash equivalents	8,945	4,209	21,213	(176)
Cash and cash equivalents, beginning of year	43,503	733	22,290	909
Cash and cash equivalents, end of year	$ 52,448	4,942	43,503	733

(Continued)

KING COUNTY PUBLIC HOSPITAL DISTRICT NO. 2
(d/b/a EvergreenHealth)

Statements of Cash Flows

Years ended December 31, 2018 and 2017

(In thousands)

		2018		2017	
		District	**Component Unit EHM**	**District**	**Component unit EHM (as restated)**
Reconciliation of deficit of revenue over expenses from operations to net cash provided by (used in) operating activities:					
Excess (deficit) of revenue over expenses from operations	$	4,054	(1,573)	(4,350)	(3,800)
Adjustments to reconcile deficit of revenue over expenses from operations to net cash provided by (used in) operating activities:					
Depreciation and amortization		35,523	2,007	34,229	2,060
Provision for bad debts		21,135	4,790	23,449	4,797
Other		(1,426)	—	(90)	—
Other – PacLab transactions		(976)	—	—	—
Changes in operating assets and liabilities:					
Patient accounts receivable, less provision for bad debt		(31,430)	(5,179)	(28,309)	(4,736)
Inventory		(671)	(181)	(227)	(111)
Prepaid expenses and other assets		2,332	105	(5,650)	64
Accounts payable and accrued expenses, net of amounts related to construction in progress		11,498	(302)	(14,271)	2,135
Accrued compensation and related liabilities		5,838	957	3,050	98
Third-party payor settlements, net		862	1,149	(3,493)	(1,247)
Professional liability and other noncurrent liabilities		(182)	—	1,449	—
Net cash provided by (used in) operating activities	$	46,557	1,773	5,787	(740)
Supplemental disclosures of noncash investing, capital, and financing activities:					
Change in capital asset additions included in accounts payable and accrued expenses	$	6,436	—	(5,963)	—
Capital lease additions		—	—	—	387

See accompanying notes to financial statements.

(1) Organization and Summary of Significant Accounting Policies

(a) Organization

King County Public Hospital District No. 2, King County, Washington, d/b/a EvergreenHealth (the District) is a municipal corporation established under Chapter 70.44 of the Revised Code of the State of Washington (RCW). The purpose of the District is to own and operate hospitals and other healthcare facilities and provide healthcare services to area residents. The District's primary operations include Evergreen Hospital Medical Center (the Medical Center), an acute care hospital; Evergreen Home Health Services, a home health agency; Evergreen Hospice Services, a program serving the terminally ill; EvergreenHealth Medical Group, a multispecialty practice group consisting of family practice physicians, physician assistants, and certified nurse practitioners; and EvergreenHealth Foundation (the Foundation). Affiliated organizations are evaluated for inclusion in the reporting entity as component units based on the significance of their relationship with the District.

(i) Blended Component Unit

The Foundation is a separate nonprofit foundation. The purpose of the Foundation is to (a) receive grants, bequests, donations, and contributions on behalf of; (b) provide fund-raising and other support to; and (c) make contributions to the District. Consequently, the net financial position and the results of operations of the Foundation are included in the accompanying financial statements. For the years ended December 31, 2018 and 2017, the Foundation raised approximately $5.0 million and $2.2 million in contributions (included in other operating revenue) and its assets comprises of 1.8% and 1.4% of total assets of the District in 2018 and 2017, respectively.

(ii) Discrete Component Unit

The District and EHM, a 72-bed semirural community hospital (together with a 40-bed residential treatment facility license), entered into a Strategic Alliance Agreement effective March 1, 2015. EHM is located in Monroe, Washington and is a separate legal entity governed by the Alliance Governance Board (AGB). The AGB comprises five directors, consisting of two commissioners of the District, two commissioners of EHM, and the District CEO. The audited financial statements of EHM are available by contacting EHM at 14701 179th Avenue SE, Monroe, Washington 98272 or online at the following address:

www.evergreenhealthmonroe.com/governance-and-leadership-monroe

(b) Basis of Presentation

The financial statements have been prepared on the accrual basis of accounting. Under this method of accounting, revenue is recognized when earned and expenses are recorded when liabilities are incurred without regard to receipt or disbursement of cash.

The District prepares and presents its financial information in accordance with GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* (GASB 34), known as the "Reporting Model" statement. GASB 34 requires that financial statements be accompanied by a narrative introduction and analytical overview of the reporting entity in the form of “management’s discussion and analysis” (MD&A). This reporting model also requires the use of a direct method cash flow statement.

(c) Financial Reporting Entity

As required by accounting principles generally accepted in the United States of America (GAAP), these financial statements present the District, the primary government, and its component units, the Foundation and EHM.

Component units are legally separate organizations for which the District is financially accountable. These entities may be reported in the financial statements of the primary government in one of two ways: the component units’ amounts may be blended with the amounts reported by the primary government, or they may be shown in a separate column, depending on the application of the criteria of GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*. The Foundation meets the criteria of a blended component unit and has been included in the financial statements. EHM does not meet the criteria of a blended component unit and has been reported as a discretely presented component unit in a separate column of the financial statements.

(d) Use of Estimates

The preparation of financial statements in conformity with GAAP 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 revenue and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates in the District’s financial statements include patient accounts receivable allowances, third-party payor settlements, professional liabilities, and the fair value of investments.

(e) Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid financial instruments with original maturities of three months or less, excluding assets restricted as to use and board-designated assets. Deposits of up to $250 thousand are covered by the federal deposit insurance corporation and any deposits in excess of $250 thousand are covered by collateral held in a multifinancial institution collateral pool administered by the Washington Public Deposit Protection Commission.

(f) Patients Accounts Receivable

Receivables arising from revenue for services to patients are reduced by an allowance for contractuals and estimated uncollectible accounts based on recent collection experience and other circumstances, which may affect the ability of patients to meet their obligations. There are various factors that can impact the collection trends and the estimation process, such as changes in the economy, the increased burden of copays, and deductibles to be made by patients and business practices related to collection efforts. Accounts deemed uncollectible are charged against this allowance.

(g) Assets Limited as to Use

Assets limited as to use include assets designated by the Board of Commissioners (the Board) for capital improvements and community service programs. The Board retains control of the assets and may, at its discretion, subsequently change the use for other purposes. Assets limited as to use include

(Continued)

certain assets of the Foundation that are restricted by donor stipulations. Assets limited as to use also include unexpended proceeds and income generated from certain outstanding bond series restricted for the payment of principal, interest, and expenditures for construction and equipment costs. The assets of the Supplemental Executive Retirement Plan (SERP) are also recorded as assets limited as to use. The SERP is a postretirement plan covering the executive management team. Amounts required to meet related current liabilities have been classified as current assets in the accompanying statements of net position. These assets are carried at fair value with changes in fair value reported as investment income.

(h) Inventory

Inventory consists of pharmaceutical, medical-surgical, and other supplies used in the operation of the District. Inventory is stated at the lower of cost, determined on a first-in, first-out basis, or net realizable value.

(i) Capital Assets

Capital assets are recorded at cost. In accordance with governmental accounting standards, the District has established a capitalization threshold of $3 thousand and a life of three years or more above which asset acquisitions are added to the capital asset accounts. Donated items are recorded at fair value at the date of the contribution. Depreciation expense is computed using the straight-line method based on the following estimated useful lives of the assets:

Land improvements	10–20 Years
Buildings	25–40 Years
Equipment	3–20 Years

Maintenance and repairs are expensed as incurred. Expenditures that materially increase values, change capacities, or extend useful lives of plant and equipment are capitalized.

Equipment under capital lease is amortized on the straight-line method over the shorter of the lease term or estimated useful life of the equipment. Such amortization is included in depreciation and amortization in the accompanying statements of revenue, expenses, and changes in net position.

(j) Compensated Absences

The District’s employees earn vacation days at varying rates depending on years of service. Accrued vacation is reported as a current liability as employees utilize their vacation days within the following year.

(k) Net Position

Net position of the District is classified in five components. Investment in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the balances of any outstanding borrowings used to finance the purchase or construction of those assets. Restricted expendable net position includes expendable for specific activities and expendable for debt service and must be used for a particular purpose, as specified by grantors or contributors external to the District.

(Continued)

Restricted nonexpendable net position equals the principal portion of permanent endowments. Unrestricted net position does not meet the definition of investment in capital, net of related debt or restricted. The District will first apply restricted resources when an expense is incurred for purposes for which both unrestricted and restricted net position are available.

(l) Operating Revenue and Expenses

The District's statements of revenue, expenses, and changes in net position distinguish between operating and nonoperating revenue and expenses. Operating revenue results from exchange transactions associated with providing healthcare services — the District's principal activity. Nonoperating income includes property taxes received or grants and contributions received for purposes other than capital asset acquisition. Operating expenses are all expenses incurred to provide healthcare services.

Other operating revenue includes tenant lease receipts, distributions from joint ventures, outreach laboratory service revenue, retail revenue such as gift shop and pharmacy, educational offerings, grant funds to support specific programs, restricted donations, and other services.

(m) 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. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and per diem payments. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

(n) Charity Care

The District accepts all patients regardless of their ability to pay. A patient is classified as a charity patient by reference to an established policy of the District. The estimated cost of charity care is determined by calculating the ratio of operating costs to charges, and then applying this ratio to total charity care charges. The estimated costs of charity care provided by the District were $2.4 million and $3.2 million for 2018 and 2017, respectively. Because the District does not pursue collection of amounts determined to qualify as charity care, associated charges are not included in net patient service revenue.

(Continued)

(o) Nonoperating Income, Net of Expenses

The District received property taxes from regular levy proceeds and voter approved excess levies. These funds were used as follows:

		December 31	
		2018	**2017**
		(In thousands)	
Amount used for tax supported programs	$	4,868	4,343
Amounts used for debt service on general obligation bonds		21,348	21,388
	$	26,216	25,731

Of the amount used for debt service on general obligation bonds, $9.4 million and $9.9 million were used for interest payments for the years ended December 31, 2018 and 2017, respectively. The property taxes received are reflected in nonoperating income. Interest expense related to long-term debt is included in nonoperating expenses. All other expenses related to tax supported programs are included in operating expenses.

Investment income includes interest income and unrealized gains and losses on board-designated assets and earnings on cash deposits.

(p) Federal Income Taxes

No provision has been made for federal income taxes, as the District is a municipal corporation exempt from federal tax, under Section 115 of the Internal Revenue Code.

No provision has been made for federal income taxes related to EHM as it is a municipal corporation exempt from federal tax, under Section 115 of the Internal Revenue Code.

The Foundation is an organization exempt from taxation under Section 501(c)(3) of the Internal Revenue Code and is generally not subject to federal income taxes. However, the Foundation is subject to income taxes on any net income that is derived from a trade or business, regularly carried on, and not in furtherance of the purposes for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the financial statements taken as a whole.

(q) Recently Issued Accounting Standards

In January 2017, the GASB issued Statement No. 84, *Fiduciary Duties* (GASB No. 84). This Statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. This Statement describes four fiduciary funds that should be reported, if applicable: (1) pension (and other employee benefit) trust funds, (2) investment trust funds, (3) private-purpose trust funds, and (4) custodial funds. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2018. The District is currently analyzing the impact from implementation of this Statement.

In June 2017, the GASB issued Statement No. 87, *Leases* (GASB No. 87). This Statement requires the recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. Therefore it establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2019. Early adoption is permitted. The district has started implementation work but will adopt on the effective date, January 1, 2020. The qualitative effects on the District's future financial statements of these changes and related retrospective adjustments have not yet been determined.

In April 2018, the GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements* (GASB No. 88). This Statement clarifies which liabilities governments should include when disclosing information related to debt. It requires that additional essential information related to debt be disclosed in notes to financial statements, including unused lines of credit; assets pledged as collateral for the debt; and terms specified in debt agreements related to significant events of default with finance-related consequences, significant termination events with finance-related consequences, and significant subjective acceleration clauses. The requirements of this Statement are effective for financial statements for periods beginning after June 15, 2018. The District has considered the above GASB statement noting no financial statement implications or impact.

(2) Net Patient Service Revenue

The District has arrangements 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 is as follows:

(a) 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 diagnosis-related groups (DRGs). Each DRG has a payment weight assigned to it, based on the average resources used to treat Medicare patients in that DRG. Inpatient nonacute services and defined capital and medical education costs related to Medicare beneficiaries are paid based on a cost reimbursement methodology. The District is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of annual cost reports by the District and audits thereof by the Medicare fiscal intermediary. The District's cost reports have been reviewed and/or audited by the Medicare fiscal intermediary through 2015. The District recognized interim and final cost report settlements and a Net Payment Reconciliation Award payment from CMS resulting in increased net patient service revenue by $762 thousand and $596 thousand in 2018 and 2017, respectively. Most outpatient services to Medicare beneficiaries are paid prospectively based on ambulatory payment classifications (APCs). Centers for Medicare and Medicaid Service (CMS) assigns individual services (Healthcare Common Procedure Coding System codes) to APCs based on similar clinical characteristics and similar costs.

(b) Medicaid

In the spring of 2005, the Washington State Legislature and CMS approved a Medicaid Certified Public Expenditures (CPE) program for inpatient reimbursement. The CPE program uses public expenditures by certain public hospitals to earn federal matching funds. Certified public expenditures are qualifying expenditures made by the hospital to serve Medicaid eligible or uninsured patients. The program was designed to preserve a significant amount of federal match funding for the State of Washington (the State) and maintain the same level of reimbursement to the affected hospitals that they would have received prior to the implementation of the program.

The CPE program uses three payment mechanisms to reimburse hospitals for inpatient care: inpatient hospital claims payments, disproportionate share (DSH) payments, and state grants. Under the program, hospitals are paid an interim payment based on an estimate of the cost to provide services to Medicaid recipients. For each payment to a hospital in the program, only the federal matching portion of the payment is remitted to the hospital; the state portion is funded through DSH payments and state grants.

The intent of the legislature is that hospitals in the program receive no less in combined federal and state payments than the hospital would have received under the methodology that was in place during fiscal year 2005. Any differences between the federal matching and state DSH components on the CPE program payments and this baseline amount are to be paid to the hospitals with state grant funds. To the extent that state grant funds allocated at the start of the year are insufficient to meet the hold harmless provision of the program, additional legislative appropriations may be required.

Interim state payments based on prospectively estimated experience are retrospectively reconciled to “hold harmless” after actual claims are repriced using the applicable methods. This process takes place at least six months after the end of the fiscal year and results in either a payable to, or receivable from, the state Medicaid Program. State inpatient claim and DSH payments are subject to retrospective determination of actual costs once the District’s Medicare Cost Report is audited. CPE program payments are not considered final until retrospective cost reconciliation is complete. Final settlement of $0.8 million has been recognized in 2018 related to state fiscal year 2012. Final settlement of $0.07 million was paid back in 2018 related to state fiscal year 2011. The District recognized interim settlements resulting in an adjustment to decrease net patient service revenue by $0.8 million and $1.6 million in 2018 and 2017, respectively.

Inpatient Medicaid charges represented approximately 10.97% and 11.67% of total inpatient charges for the District in fiscal year 2018 and 2017, respectively.

The Medicaid CPE program continues through the State’s fiscal year 2018 and 2017. As of December 31, 2018 and 2017, the District has recorded a payable of $0.2 million and $0.3 million for estimated overpayments for state fiscal year 2018 and 2017, respectively, which is included in third-party payor payable in the statements of net position.

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.

In the July 2009 legislative session, the Washington State legislature enacted the Hospital Safety Net Assessment to help mitigate an estimated $400 million reduction in hospital Medicaid payments. Under this law, nongovernmental Washington hospitals are assessed a fee on all non-Medicare patient days. The fees are used to obtain new federal Medicaid matching funds.

The safety net assessment was subject to approval by CMS before it took effect. In 2010, CMS approved the two amendments required to fully enact the safety net assessment program. The initial safety net program expired in June 2013 and the State passed a new safety net assessment program that was approved by CMS in April 2014. The new law is retroactive to July 1, 2013 and will sunset on July 1, 2021. The latest legislative proposal will extend the expiration date to July 1, 2023. The District is not subject to the assessment but is a recipient of grant dollars through the program. The District received safety net payments totaling $0.9 million and $0.9 million for 2018 and 2017, respectively.

(c) Other Third-Party Reimbursement

The District has entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to the District under these agreements includes prospectively determined rates per discharge, discounts from established charges, and prospectively determined daily rates.

The following are the components of net patient service revenue for the years ended December 31, 2018 and 2017:

	2018	
	District	**Component unit**
	(In thousands)	
Gross patient service charges	$ 1,865,939	136,451
Adjustments to patient service charges:		
Contractual adjustments	1,170,186	85,023
Provision for bad debts	21,135	4,790
Charity care	6,527	585
Administrative adjustments	3,286	—
	1,201,134	90,398
Net patient service revenue	$ 664,805	46,053

		2017	
		District	Component unit
		(In thousands)	
Gross patient service charges	$	1,804,111	120,415
Adjustments to patient service charges:			
Contractual adjustments		1,128,527	73,247
Provision for bad debts		23,449	4,797
Charity care		8,635	587
Administrative adjustments		16,140	11
		1,176,751	78,642
Net patient service revenue	$	627,360	41,773

(3) Assets Limited as to Use

Assets limited as to use include board-designated cash and investments and restricted cash and investments.

Board-designated cash and investments represent unrestricted resources that have been designated by the Board for funded depreciation and community service programs. In addition, the Board has the authority to establish a regular property tax levy within statutory restrictions, with the proceeds being used for purposes designated by the Board.

Restricted cash and investments include certain assets of the Foundation that are restricted by donor stipulations, assets related to the postretirement plan covering the executive management team, and other restricted cash and investments.

Assets limited as to use are carried at fair value. Fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The three levels of the fair value hierarchy under GASB 72, *Fair Value Measurement and Application*, are described below:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities that a government can access at the measurement date
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for an asset or liability, either directly or indirectly
- Level 3 – Unobservable inputs for an asset or liability

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

(a) Cash and Cash Equivalents – The carrying value approximates fair value because of the short maturity of those instruments.

(b) Long-Term Debt – Long-term debt is carried at amortized cost; however, accounting standards require the District to disclose the fair value. The fair value of the District's long-term debt is based on market estimates. The fair value and carrying value of long-term debt are $202.2 million and $198.0 million, and $218.6 million and $212.3 million as of December 31, 2018 and 2017, respectively.

(c) Assets Limited as to Use – Fair values are estimated based on quoted market prices for those or similar investments. Maturities for securities are based on the weighted average maturity date, or reset date for adjustable rate mortgages.

The following tables present the composition, fair value, ratings and maturity of board-designated cash and investments for the District at December 31, 2018 and 2017:

Board-Designated Assets

December 31, 2018

Investment type		Fair value amount		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Ratings
				(In thousands)		
U.S. Treasuries	$	72,116		—	72,116	AAA
U.S. government agencies		26,775		—	26,775	AAA
Mutual fund – bonds		2,692		2,692	—	AAA
Credit		33,800		—	33,800	AAA
Taxable Muni		2,468		—	2,468	AAA
U.S. government agency – mortgage backed		4,606		—	4,606	AAA
Government Related		4,716		—	4,716	AAA
King County Investment Pool		659		659	—	Not rated
Total investments		147,832	$	3,351	144,481	
Cash and cash equivalents		219				
Total cash and investments		148,051				
Property tax, interest receivable, and other		3,443				
Total board-designated assets	$	151,494				

Board-Designated Assets

December 31, 2018

Investment type		Fair value amount	Investment maturities (in years) Less than 1	1–5
			(In thousands)	
U.S. Treasuries	$	72,116	498	71,618
U.S. government agencies		26,775	2,724	24,051
Mutual fund – bonds		2,692	2,692	—
Credit		33,800	—	33,800
Taxable Muni		2,468	—	2,468
U.S. government agency – mortgage backed		4,606	2,457	2,149
Government Related		4,716	—	4,716
King County Investment Pool		659	659	—
Total investments	$	147,832	9,030	138,802

Board-Designated Assets

December 31, 2017

Investment type		Fair value amount		Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Ratings
				(In thousands)		
U.S. Treasuries	$	54,717		—	54,717	AAA
U.S. government agencies		32,239		—	32,239	AAA
Mutual fund – bonds		1,598		1,598	—	AAA
Credit		30,165		—	30,165	AAA
Taxable Muni		3,665		—	3,665	AAA
U.S. government agency – mortgage backed		4,787		—	4,787	AAA
King County Investment Pool		1,035		1,035	—	Not rated
Total investments		128,206	$	2,633	125,573	
Cash and cash equivalents		9,722				
Total cash and investments		137,928				
Property tax, interest receivable, and other		2,944				
Total board-designated assets	$	140,872				

Board-Designated Assets

December 31, 2017

Investment type		Fair value amount	Investment maturities (in years) Less than 1	1–5
			(In thousands)	
U.S. Treasuries	$	54,717	3,295	51,422
U.S. government agencies		32,239	2,698	29,541
Mutual fund – bonds		1,598	1,598	—
Credit		30,165	—	30,165
Taxable Muni		3,665	180	3,485
U.S. government agency – mortgage backed		4,787	2,273	2,514
King County Investment Pool		1,035	1,035	—
Total investments	$	128,206	11,079	117,127

The following tables present the composition, fair value, ratings and maturity of restricted cash and investments of the District for the years ended December 31, 2018 and 2017.

Restricted Cash and Investments

December 31, 2018

Investment type		Fair value amount		Quoted prices in active markets for identical assets (Level 1)	Ratings		Investment maturities (in years) Less than 1
				(In thousands)			
King County Investment Pool	$	859		859	Not Rated		859
Mutual fund – bonds		1,776		1,776	AAA		—
Mutual fund – equity		2,282		2,282	AAA		—
Total investments		4,917	$	4,917		$	859
Cash and cash equivalents		104					
Total cash and investments		5,021					
Property tax, interest receivable, and other		3,549					
Total assets restricted as to use	$	8,570					

Restricted Cash and Investments

December 31, 2017

Investment type		Fair value amount		Quoted prices in active markets for identical assets (Level 1)	Ratings		Investment maturities (in years) Less than 1
				(In thousands)			
King County Investment Pool	$	775		775	Not Rated		775
Mutual fund – bonds		1,149		1,149	AAA		—
Mutual fund – equity		1,833		1,833	AAA		—
Total investments		3,757	$	3,757		$	775
Cash and cash equivalents		104					
Total cash and investments		3,861					
Property tax, interest receivable, and other		4,974					
Total assets restricted as to use	$	8,835					

Interest Rate Risk – The District's investment policy limits investment maturities as a means of managing its exposure to fair value losses arising from changing interest rates. Shares of mutual funds with portfolios consisting of only U.S. government bonds or U.S. government bonds issued by federal agencies must have average maturities of less than four years. Unless matched to a specific cash flow, the District does not invest in securities maturing more than five years from the date of purchase. However, assets whose use is limited may be invested in securities exceeding 10 years if the maturity of such investments is timed to coincide with the expected use of funds.

Credit Risk – Statutes authorize the District to invest in obligations of the U.S. Treasury, agencies, and instrumentalities, public funds investment accounts, state, or local government bonds with one of the three highest credit ratings of a nationally recognized agency, money markets with investments in authorized securities, and mutual funds of only U.S. government bonds and agencies. The U.S. Treasury, agency, and agency mortgage backed are considered to be of high quality; and the U.S. Treasury carry the long-term sovereign rating of the United States of America. The District's policy requires that all certificates of deposit be collateralized.

(Continued)

The District utilizes an investment adviser as well as the King County Investment Pool (the Pool), an external investment pool. The Pool is not registered with the Securities and Exchange Commission as an investment company. Oversight of the Pool is provided by the King County Executive Finance Committee pursuant to RCW 36.29.020. Participation in this pool is voluntary. The intent of this policy is to balance reasonable security with reasonable investment return, seeking to maximize both while meeting the daily cash flow requirements of the District and conforming to all applicable laws and regulations governing the investment of public funds.

Concentration of Credit Risk – In October 2017, the District's Board of Commissioners adopted a revised investment policy, which includes the ability to invest in Commercial Paper and Corporate Notes in accordance with RCW 39.59.040 and Washington State Investment Board policy number 2.05.500.

The following table sets forth the percentages by investment type of the District's total investment portfolio as of December 31, 2018 and 2017.

	2018	2017
U.S. Treasuries	49%	40%
Mutual fund/U.S. government securities	—	7
Federal National Mortgage Association	4	7
Federal Home Loan Bank	3	6
Federal Home Loan Mortgage Corporation	6	6
Federal Farm Credit Bank	6	7
Government National Mortgage Association	1	—
King County Investment Pool	1	1
Credit	23	22
Taxable Municipal Bonds	2	3
Agencies Other	2	1
Government Related	3	—

(4) Capital Assets (Tables in thousands)

The schedule of capital asset activity for the years ended December 31, 2018 and 2017 is as follows:

	January 1, 2018	Additions and adjustments	Sales and retirements	Account transfers	December 31, 2018
Assets at cost:					
Nondepreciable capital assets:	4,914	—	—	—	4,914
Land	$ 9,699	27,737	—	(23,156)	14,280
Construction in progress					
Total nondepreciable capital assets	14,613	27,737	—	(23,156)	19,194
Depreciable capital assets:					
Land improvements	14,664	—	(335)	—	14,329
Buildings	357,731	(379)	(2,479)	5,384	360,257
Equipment	403,671	379	(7,776)	17,772	414,046
Equipment and property under capital lease	15,131	—	—	—	15,131
Total depreciable capital assets	791,197	—	(10,590)	23,156	803,763
Less accumulated depreciation:					
Land improvements	11,706	403	(335)	—	11,774
Buildings	165,664	12,815	(2,479)	—	176,000
Equipment	292,845	21,216	(7,776)	—	306,285
Equipment under capital lease	8,498	1,359			9,857
Total accumulated depreciation	478,713	35,793	(10,590)	—	503,916
Depreciable capital assets, net	312,484	(35,793)	—	23,156	299,847
Capital assets, net	$ 327,097	(8,056)	—	—	319,041

	January 1, 2017	Additions and adjustments	Sales and retirements	Account transfers	December 31, 2017
Assets at cost:					
Nondepreciable capital assets:					
Land	$ 4,914	—	—	—	4,914
Construction in progress	30,152	50,163	—	(70,616)	9,699
Total nondepreciable capital assets	35,066	50,163	—	(70,616)	14,613
Depreciable capital assets:					
Land improvements	14,642	1	(82)	103	14,664
Buildings	325,908	312	(832)	32,343	357,731
Equipment	374,243	62	(8,804)	38,170	403,671
Equipment and property under capital lease	15,131	—	—	—	15,131
Total depreciable capital assets	729,924	375	(9,718)	70,616	791,197
Less accumulated depreciation:					
Land improvements	11,320	468	(82)	—	11,706
Buildings	154,152	12,344	(832)	—	165,664
Equipment	281,318	20,331	(8,804)	—	292,845
Equipment under capital lease	7,274	1,224	—	—	8,498
Total accumulated depreciation	454,064	34,367	(9,718)	—	478,713
Depreciable capital assets, net	275,860	(33,992)	—	70,616	312,484
Capital assets, net	$ 310,926	16,171	—	—	327,097

(Continued)

The schedule of capital asset activity for EHM for the years ended December 31, 2018 and 2017 is as follows:

		January 1, 2018	Additions and adjustments	Sales and retirements	Account transfers	December 31, 2018
Assets at cost:						
Nondepreciable capital assets:						
Land	$	1,879	—	—	—	1,879
Construction in progress		880	462	(928)	—	414
Total nondepreciable capital assets		2,759	462	(928)	—	2,293
Depreciable capital assets:						
Land improvements		1,146	—	—	—	1,146
Buildings		26,274	13	592	—	26,879
Equipment		18,090	300	213	—	18,603
Equipment and property under capital lease		2,475	4	123	— —	2,602
Total depreciable capital assets		47,985	317	928	—	49,230
Less accumulated depreciation:						
Land improvements		766	55	—	—	821
Buildings		18,904	862	—	—	19,766
Equipment		14,579	943	—	—	15,522
Equipment under capital lease		2,242	94	—	—	2,336
Total accumulated depreciation		36,491	1,954	—	—	38,445
Depreciable capital assets, net		11,494	(1,637)	928	—	10,785
Capital assets, net	$	14,253	(1,175)	—	—	13,078

	January 1, 2017	Additions and adjustments	Sales and retirements	Account transfers	December 31, 2017
Assets at cost:					
Nondepreciable capital assets:					
Land	$ 1,879	—	—	—	1,879
Construction in progress	905	1,293	—	(1,318)	880
Total nondepreciable capital assets	2,784	1,293	—	(1,318)	2,759
Depreciable capital assets:					
Land improvements	1,146	—	—	—	1,146
Buildings	25,072	3	—	1,199	26,274
Equipment	16,943	1,406	(366)	107	18,090
Equipment and property under capital lease	2,446	17	—	12	2,475
Total depreciable capital assets	45,607	1,426	(366)	1,318	47,985
Less accumulated depreciation:					
Land improvements	711	55	—	—	766
Buildings	17,879	1,025	—	—	18,904
Equipment	14,098	847	(366)	—	14,579
Equipment under capital lease	2,160	82	—	—	2,242
Total accumulated depreciation	34,848	2,009	(366)	—	36,491
Depreciable capital assets, net	10,759	(583)	—	1,318	11,494
Capital assets, net	$ 13,543	710	—	—	14,253

(5) Other Assets

Evergreen Radia, LLC

During 2003, the District formed a limited liability company with a local radiology group for the purpose of providing outpatient diagnostic imaging services to individuals within the community. The District had a 50% interest in this joint venture at December 31, 2018 and 2017, which is accounted for using the equity method of accounting. During the years ended December 31, 2018 and 2017, the District recognized income of $1.7 million and $1.8 million, respectively, for its share of the Evergreen Radia, LLC’s net income, which is recorded as other operating revenue. The District’s recorded investment in Evergreen Radia, LLC was $4.7 million and $5.4 million as of December 31, 2018 and 2017, respectively, and is included in other assets in the District’s statements of net position.

The following represents the summary financial information of Evergreen Radia, LLC as of December 31, 2018 and 2017 (in thousands):

		2018	2017
		Evergreen Radia, LLC	**Evergreen Radia, LLC**
Current assets	$	4,346	4,693
Noncurrent assets, net		683	774
	$	5,029	5,467
Current liabilities	$	1,758	1,574
Long-term liabilities		70	207
Equity		3,201	3,686
	$	5,029	5,467
Revenue	$	13,634	12,757
Expenses		9,918	9,170
Net income	$	3,716	3,587

PacLab, LLC

In May 2017, PacLab, LLC was purchased by Laboratory Corporation of America (LabCorp). The District was paid approximately $19 million for its interest in PacLab, which was classified as a deferred inflow of resources as of December 31, 2017. The closing and the associated sale were effective February 5, 2018, at which time the deferred inflow of resources was recognized as nonoperating income.

		2017 PacLab, LLC (Unaudited)
Current assets	$	4,254
Noncurrent assets, net		2,675
	$	6,929
Current liabilities	$	574
Long-term liabilities		—
Equity		6,355
	$	6,929
Revenue	$	190
Expenses		1,059
Net loss	$	(869)

(Continued)

(6) Long-Term Debt and Capital Lease Obligations

Long-term debt and capital lease obligations of the District consist of the following:

		December 31	
		2018	2017
		(In thousands)	
Limited Tax General Obligation Bonds (LTGO) Series 2010 (fixed rate), payable annually through 2028, interest at 2.00% to 5.25%	$	22,635	24,350
LTGO Series 2011 (fixed rate), payable annually through 2030, interest at 2.00% to 5.00%		20,270	21,565
LTGO Series 2015 (fixed rate), payable annually through 2031, interest at 3.63 to 5.00%		52,250	55,065
LTGO Series 2015 B (fixed rate), payable annually through 2037, interest at 4.00% to 5.00%		54,000	54,000
Unlimited Tax General Obligation Refunding Bonds (UTGO), Series 2013 (fixed rate), payable semiannually through 2023, interest at 3.00% to 5.00%		36,035	42,300
Capital lease obligations, $8,919 (fixed rate), payable monthly including interest at 0.18% to 10.0%, collateralized by equipment		7,913	8,918
		193,103	206,198
Plus bond discounts and premiums		12,769	14,999
		205,872	221,197
Less current portion		(13,752)	(13,101)
	$	192,120	208,096

Long-term debt and capital lease obligations 2018 and 2017 activity summary for the District is as follows (in thousands):

	January 1, 2018	Additions	Reductions	December 31, 2018	Amounts due within one year
Limited general obligation bonds:					
2010 series	$ 24,350	—	1,715	22,635	1,800
2011 series	21,565	—	1,295	20,270	1,360
2015 series	55,065	—	2,815	52,250	2,955
2015 series B	54,000	—	—	54,000	—
Unlimited general obligation bonds:					
2013 series	42,300	—	6,265	36,035	6,580
Total long-term debt	197,280	—	12,090	185,190	12,695
Capital lease obligations	8,918	—	1,005	7,913	1,057
Total long-term debt and capital lease obligations	206,198	—	13,095	193,103	13,752
Bond discounts and premiums	14,999	—	2,230	12,769	—
Total long-term debt and capital lease obligations	$ 221,197	—	15,325	205,872	13,752

	January 1, 2017	Additions	Reductions	December 31, 2017	Amounts due within one year
Limited general obligation bonds:					
2010 series	$ 25,980	—	1,630	24,350	1,715
2011 series	22,800	—	1,235	21,565	1,295
2015 series	57,740	—	2,675	55,065	2,815
2015 series B	54,000	—	—	54,000	—
Unlimited general obligation bonds:					
2013 series	48,265	—	5,965	42,300	6,265
Total long-term debt	208,785	—	11,505	197,280	12,090
Capital lease obligations	9,855	—	937	8,918	1,011
Total long-term debt and capital lease obligations	218,640	—	12,442	206,198	13,101
Bond discounts and premiums	17,447	—	2,448	14,999	—
Total long-term debt and capital lease obligations	$ 236,087	—	14,890	221,197	13,101

A summary of the District future maturities on long-term debt for the next five years and thereafter as of December 31, 2018 for both principal and interest is presented below (in thousands):

	Principal	Interest
2019	$ 12,695	8,750
2020	13,280	8,156
2021	13,870	7,564
2022	14,570	6,895
2023	15,240	6,195
Amounts due 2024–2028	42,350	23,321
Amounts due 2029–2033	35,750	13,713
Amounts due 2034–2038	37,435	4,134
	185,190	$ 78,728
Plus amount representing net unamortized bond discounts and premiums	12,769	
	$ 197,959	

UTGO bonds are secured by the irrevocable pledge of the District to levy taxes annually, without limitation as to rate or amount based on a vote of the electors, on all taxable property within the District. LTGO are secured by the irrevocable pledge of the District to levy taxes annually, within the constitutional and statutory limitations provided by law without a vote of the electors, upon property in the District, as well as the net revenue of the District for amounts that exceed that available through the levy.

Component Unit – EHM

Long-term debt and capital lease obligations of EHM consist of the following (in thousands):

		December 31	
		2018	**2017**
LTGO Improvement and Refunding Bonds, 2009, payable annually through 2034, interest at 5.00% to 5.38%	$	17,510	17,510
LTGO Bonds, 2004, payable annually through 2018, interest at 4.10% to 4.50%		—	535
Capital lease obligations, payable monthly including interest at 6.70% to 10.51%, collateralized by equipment		293	518
		17,803	18,563
Plus bond discounts and premiums		(190)	(204)
		17,613	18,359
Less current portion		(675)	(761)
	$	16,938	17,598

Long-term debt and capital lease obligations 2018 and 2017 activity summary of EHM is as follows (in thousands):

		January 1, 2018	Additions	Reductions	December 31, 2018	Amounts due within one year
Limited general obligation bonds:						
2009 series	$	17,510	—	—	17,510	585
2004 series		535	—	535	—	—
Total long-term debt		18,045	—	535	17,510	585
Capital lease obligations		518	—	225	293	90
Total long-term debt and capital lease obligations		18,563	—	760	17,803	675
Bond discounts and premiums		(204)	14	—	(190)	—
Total long-term debt and capital lease obligations	$	18,359	14	760	17,613	675

		January 1, 2017	Additions	Reductions	December 31, 2017	Amounts due within one year
Limited general obligation bonds:						
2009 series	$	17,510	—	—	17,510	—
2004 series		1,025	—	490	535	535
Total long-term debt		18,535	—	490	18,045	535
Capital lease obligations		532	387	401	518	226
Total long-term debt and capital lease obligations		19,067	387	891	18,563	761
Bond discounts and premiums		(218)	14	—	(204)	—
Total long-term debt and capital lease obligations	$	18,849	401	891	18,359	761

(Continued)

A summary of EHM's future maturities on long-term debt for the next five years and thereafter as of December 31, 2018 for both principal and interest is presented below (in thousands):

		Principal		Interest
2019	$	585		906
2020		635		876
2021		690		845
2022		745		810
2023		805		773
Amounts due 2024–2028		5,070		3,193
Amounts due 2029–2033		7,215		1,681
2034		1,765		94
		17,510	$	9,178
Plus amount representing net unamortized bond discounts		(190)		
	$	17,320		

Capital Leases

The District acquired certain equipment under capital lease obligations. The leases are collateralized by the related equipment. Future minimum lease payments are as follows (in thousands):

		Amount (in thousands)
Year(s) ending December 31:		
2019	$	1,383
2020		1,218
2021		1,228
2022		1,268
2023		1,309
2024–2028		2,863
Total minimum lease payments		9,269
Less amount representing interest		(1,356)
Total capital lease payments	$	7,913

EHM acquired certain equipment under capital lease obligations. The leases are collateralized by the related equipment. Future minimum lease payments are as follows (in thousands):

		Amount (in thousands)
Year(s) ending December 31:		
2019	$	104
2020		98
2021		89
2022		29
Total minimum lease payments		320
Less amount representing interest		(27)
Total capital lease payments	$	293

(7) Tenant Lease Receipts

The District owns and operates the Evergreen Professional Center (EPC), the Evergreen Surgical and Physicians Center (ES&PC), and the DeYoung Pavilion, which contain approximately 53,547 total square feet of space for physician offices available for lease. As of December 31, 2018 and 2017, the District had space under operating lease terms from 5 to 15 years.

Future minimum rent receipts and sublease receipts on noncancelable operating leases are as follows:

		Owned property receipts	Leased property receipts	Total amount
			(In thousands)	
Year ending December 31:				
2019	$	1,777	4,530	6,307
2020		1,286	4,490	5,776
2021		1,293	4,183	5,476
2022		1,188	3,717	4,905
2023		752	3,255	4,007
Thereafter		802	13,926	14,728
	$	7,098	34,101	41,199

Rental income related to the EPC, ES&PC, and the DeYoung Pavilion leases was approximately $1.8 million and $1.8 million in 2018 and 2017, respectively, and is included in other operating revenue.

(Continued)

Rental income related to subleases was approximately $4.6 million and $3.9 million in 2018 and 2017, respectively.

(8) Commitment and Contingencies

(a) Leases

The District leases various equipment and facilities under operating leases. Total rental expense in 2018 and 2017 for all operating leases and various rental agreements was approximately $14.3 million and $13.8 million, respectively.

The future minimum lease payments under noncancelable operating leases that have initial lease terms in excess of one year are as follows:

		Payments (In thousands)
Year ending December 31:		
2019	$	9,556
2020		9,318
2021		9,330
2022		9,300
2023		9,481
Thereafter		61,725
	$	108,710

(b) Insurance Coverage

The District holds professional liability insurance coverage through an independent insurance company. The insurance coverage is based on a claims-made policy. The District is self-insured for professional liability tail and expected claims payout on this coverage. The policy’s self-insured retention limit is $1.0 million per claim and $4.0 million per aggregate.

The District records its actuarial estimate for professional claims liability at its best estimate of the ultimate losses and costs associated with settling claims. The professional liability expense was $2.4 million and $2.4 million for the years ended December 31, 2018 and 2017, respectively. At December 31, 2018 and 2017, the estimated long term and short term professional claims liability was $4.8 million and $1.4 million and $5.2 million and $1.7 million, respectively.

The District is self-insured for various programs, including employee medical benefits and workers’ compensation. The estimated ultimate costs of claims under these programs are accrued when the incidents occur that give rise to the claims. Accrued amounts for these programs of approximately $5.4 million and $5.7 million at December 31, 2018 and 2017, respectively, are reported as part of accrued compensation and related liabilities in the accompanying statements of net position. The accrued amounts include known liabilities of the programs and estimated incurred but not reported claims.

(Continued)

(c) Litigation

The District is involved in litigation arising in the ordinary 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.

(d) Compliance with Laws and Regulations

The healthcare industry is subject to numerous laws and regulations of federal, state, and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, governmental healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government agencies are actively conducting investigations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion by healthcare providers, 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 known or unasserted at this time.

(e) Risk Management

The District is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses; and natural disasters. The District maintains commercial insurance coverage designed to provide for claims arising from such matters.

(9) Retirement Plans

The District has a defined-contribution retirement plan covering substantially all eligible employees. The District makes a matching contribution of up to a maximum of 8% of the employee's eligible compensation. All contributions vest over a five-year schedule.

In addition to the retirement plan, the District maintains a voluntary employee deferred compensation program under the provision of Section 457 of the Internal Revenue Service Code. Under this program, the District employees can defer a portion of their income until withdrawn in future years. All assets are required to be held in trust for the exclusive benefit of participants and their beneficiaries. The District also contributes up to 4% of compensation as base pension depending on years of service.

Retirement plan expense, incurred and reflected in employee benefits, was approximately $17.8 million and $18.1 million in 2018 and 2017, respectively. Contributions made by employees to the benefit plans totaled approximately $27.8 million and $26.2 million in 2018 and 2017, respectively. Both plans are administered by the District under record-keeping and trust agreements with third parties.

The District has a postemployment benefit plan covering the executive management team. The District makes annual contributions to the SERP. The SERP is recorded under assets limited as to use and under noncurrent liabilities on the statements of net position. At December 31, 2018 and 2017, the SERP balance was $2.8 million and $2.7 million, respectively.

(Continued)

(10) Concentration 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 hospital receivables at December 31 was as follows:

	Receivables	
	2018	**2017**
Non-Government third party payors	42.6 %	44.6 %
Medicare	32.9	31.8
Patient self-pay	15.6	11.5
Medicaid	8.9	12.1
	100.0%	100.0%

(11) Property Taxes

The King 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 King 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 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. The Washington State Constitution and Washington State Law, RCW 84.55.100, limit the rate. The District may also levy taxes at a lower rate. Additional amounts of tax need to be authorized by a vote of the residents of the District.

For 2018 and 2017, the District’s regular levy request was $.22 per $1,000 and $0.24 per $1,000 on a total assessed valuation of the property within the District of $80.8 billion and $72.0 billion for a total regular levy of $18.0 million and $17.5 million, respectively. Excess levies totaled $8.2 million in both 2018 and 2017, related to debt service, mainly due to the hospital-based emergency department and patient facility, which opened in 2007.

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

(Continued)

(12) Blended Component Unit

Condensed combining statements for the District and its blended component unit, the Foundation, are shown below:

	Statement of net position – December 31, 2018			
	Combined entities	**Eliminations/ reclassifications**	**District**	**Foundation**
	(In thousands)			
Assets:				
Current assets:				
Total current assets	$ 173,063	(1,831)	167,970	6,924
Noncurrent assets:				
Total other assets	190,207	716	184,072	5,419
Capital assets, net	319,041	—	319,041	—
Total assets	682,311	(1,115)	671,083	12,343
Deferred outflows of resources	3,070	—	3,070	—
Total assets and deferred outflows of resources	$ 685,381	(1,115)	674,153	12,343
Liabilities:				
Total current liabilities	$ 98,221	(1,115)	98,221	1,115
Total noncurrent liabilities	199,750	—	199,750	—
Total liabilities	297,971	(1,115)	297,971	1,115
Deferred inflows of resources:				
Deferred proceeds	—	—	—	—
Net position:				
Invested in capital assets, net of related debt	113,169	—	113,169	—
Restricted:				
Expendable	13,416	—	7,372	6,044
Nonexpendable	4,795	—	1,674	3,121
Unrestricted	256,030	—	253,967	2,063
Total net position	387,410	—	376,182	11,228
Total liabilities, deferred inflows of resources and net position	$ 685,381	(1,115)	674,153	12,343

	Statement of net position – December 31, 2017			
	Combined entities	Eliminations/ reclassifications	District	Foundation
	(In thousands)			
Assets:				
Current assets:				
Total current assets	$ 154,678	(682)	149,740	5,620
Noncurrent assets:				
Total other assets	179,550	310	175,322	3,918
Capital assets, net	327,097	—	327,097	—
Total assets	661,325	(372)	652,159	9,538
Deferred outflows of resources	3,645	—	3,645	—
Total assets and deferred outflows of resources	$ 664,970	(372)	655,804	9,538
Liabilities:				
Total current liabilities	$ 86,449	(372)	86,449	372
Total noncurrent liabilities	215,997	—	215,997	—
Total liabilities	302,446	(372)	302,446	372
Deferred inflows of resources:				
Deferred proceeds (current)	19,139	—	19,139	—
Net position:				
Invested in capital assets, net of related debt	105,899	—	105,899	—
Restricted:				
Expendable	1,716	—	(108)	1,824
Nonexpendable	6,031	—	717	5,314
Unrestricted	229,739	—	227,711	2,028
Total net position	343,385	—	334,219	9,166
Total liabilities, deferred inflows of resources and net position	$ 664,970	(372)	655,804	9,538

(Continued)

	Statement of revenue, expenses, and changes in net position – year ended December 31, 2018		
	Combined entities	District	Foundation
		(In thousands)	
Revenue:			
Operating revenue:			
Net patient service revenue	$ 664,805	664,805	—
Other operating revenue	35,920	31,411	4,509
Total operating revenue	700,725	696,216	4,509
Expenses:			
Operating expenses:			
Other operating expenses	661,148	657,802	3,346
Depreciation and amortization	35,523	35,523	—
Total operating expenses	696,671	693,325	3,346
Excess of revenue over expenses from operations	4,054	2,891	1,163
Nonoperating income, net of expenses:			
Property taxes	26,216	26,216	—
Interest and amortization expense	(8,027)	(8,027)	—
Other nonoperating revenue	20,884	21,093	(209)
Net nonoperating income	39,073	39,282	(209)
Excess of revenue over expenses	43,127	42,173	954
Capital grants and contributions	898	(211)	1,109
Total change in net position	44,025	41,962	2,063
Net position, beginning of year	343,385	330,838	12,547
Net position, end of year	$ 387,410	372,800	14,610

(Continued)

	Statement of revenue, expenses, and changes in net position – year ended December 31, 2017		
	Combined entities	**District**	**Foundation**
		(In thousands)	
Revenue:			
Operating revenue:			
Net patient service revenue	$ 627,360	627,360	—
Other operating revenue	41,906	39,744	2,162
Total operating revenue	669,266	667,104	2,162
Expenses:			
Operating expenses:			
Other operating expenses	639,387	636,917	2,470
Depreciation and amortization	34,229	34,229	—
Total operating expenses	673,616	671,146	2,470
Deficit of revenue over expenses from operations	(4,350)	(4,042)	(308)
Nonoperating income, net of expenses:			
Property taxes	25,731	25,731	—
Interest and amortization expense	(8,490)	(8,490)	—
Other nonoperating revenue	1,723	1,310	413
Net nonoperating income	18,964	18,551	413
Excess of revenue over expenses	14,614	14,509	105
Capital grants and contributions	222	(855)	1,077
Total change in net position	14,836	13,654	1,182
Net position, beginning of year	328,549	317,184	11,365
Net position, end of year	$ 343,385	330,838	12,547

(Continued)

		Statement of cash flows – year ended December 31, 2018		
		Combined entities	**District**	**Foundation**
			(In thousands)	
Net cash provided by (used in):				
Operating activities	$	46,557	44,052	2,505
Noncapital financing activities		4,868	4,742	126
Capital and related financing activities		(34,785)	(34,785)	—
Investing activities		(7,695)	(6,081)	(1,614)
Net increase in cash and cash equivalents		8,945	7,928	1,017
Cash and cash equivalents, beginning of year		43,503	38,152	5,351
Cash and cash equivalents, end of year	$	52,448	46,080	6,368

		Statement of cash flows – year ended December 31, 2017		
		Combined entities	**District**	**Foundation**
			(In thousands)	
Net cash provided by (used in):				
Operating activities	$	5,787	6,330	(543)
Noncapital financing activities		4,343	4,206	137
Capital and related financing activities		(45,720)	(45,720)	—
Investing activities		56,803	57,005	(202)
Net increase (decrease) in cash and cash equivalents		21,213	21,821	(608)
Cash and cash equivalents, beginning of year		22,290	16,331	5,959
Cash and cash equivalents, end of year	$	43,503	38,152	5,351

(13) Subsequent Events

The District has performed an evaluation of subsequent events through May 30, 2019, which is the date these financial statements were issued.