



Office of the Washington State Auditor
Pat McCarthy

**Financial Statements and Federal Single Audit
Report**

**North Sound Behavioral Health
Organization**

For the period January 1, 2018 through December 31, 2018

Published September 26, 2019

Report No. 1024663





**Office of the Washington State Auditor
Pat McCarthy**

September 26, 2019

Board of Directors
North Sound Behavioral Health Organization
Mount Vernon, Washington

Report on Financial Statements and Federal Single Audit

Please find attached our report on the North Sound Behavioral Health Organization's financial statements and compliance with federal laws and regulations.

We are issuing this report in order to provide information on the Organization's financial condition.

Sincerely,

Pat McCarthy
State Auditor
Olympia, WA

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SCHEDULE OF FINDINGS AND QUESTIONED COSTS

North Sound Behavioral Health Organization January 1, 2018 through December 31, 2018

SECTION I – SUMMARY OF AUDITOR’S RESULTS

The results of our audit of the North Sound Behavioral Health Organization are summarized below in accordance with Title 2 *U.S. Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance).

Financial Statements

We issued an unmodified opinion on the fair presentation of the financial statements of the governmental activities and each major fund in accordance with accounting principles generally accepted in the United States of America (GAAP).

Internal Control over Financial Reporting:

- *Significant Deficiencies:* We identified deficiencies in the design or operation of internal control over financial reporting that we consider to be significant deficiencies.
- *Material Weaknesses:* We identified no deficiencies that we consider to be material weaknesses.

We noted no instances of noncompliance that were material to the financial statements of the Organization.

Federal Awards

Internal Control over Major Programs:

- *Significant Deficiencies:* We reported no deficiencies in the design or operation of internal control over major federal programs that we consider to be significant deficiencies.
- *Material Weaknesses:* We identified no deficiencies that we consider to be material weaknesses.

We issued an unmodified opinion on the Organization's compliance with requirements applicable to its major federal program.

We reported no findings that are required to be disclosed in accordance with 2 CFR 200.516(a).

Identification of Major Federal Programs

The following program was selected as a major program in our audit of compliance in accordance with the Uniform Guidance.

<u>CFDA No.</u>	<u>Program or Cluster Title</u>
93.958	Block Grants for Community Mental Health Services

The dollar threshold used to distinguish between Type A and Type B programs, as prescribed by the Uniform Guidance, was \$750,000.

The Organization qualified as a low-risk auditee under the Uniform Guidance.

SECTION II – FINANCIAL STATEMENT FINDINGS

See finding 2018-001.

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

None reported.

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

North Sound Behavioral Health Organization January 1, 2018 through December 31, 2018

2018-001 The Behavioral Health Organization did not have adequate internal controls in place over financial statement preparation to ensure accurate financial reporting.

Background

Behavioral Health Organization (Organization) management is responsible for designing, implementing, and maintaining internal controls to ensure financial statements are fairly presented and to provide reasonable assurance regarding the reliability of financial reporting.

The Organization prepares its financial statements in accordance with generally accepted accounting principles (GAAP), as prescribed by the Governmental Accounting Standards Board (GASB).

Our audit identified deficiencies in the Organization's internal controls over financial reporting that hindered its ability to produce reliable financial statements. We consider this weakness in controls to be a significant deficiency. *Government Auditing Standards* requires the auditor to communicate significant deficiencies, defined in the Applicable Laws and Regulations section below, as a finding.

Description of Condition

The Organization's financial statements classify ending fund balance and net position into separate line items, including net investment in capital assets, several lines for external restrictions, and unrestricted/unassigned. For fiscal year 2018, the Organization reported negative balances for restricted line items on both the Governmental Activities Statement of Net Position and the General Fund Balance Sheet.

GASB 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and the *Budgeting, Accounting and Reporting System (BARS)* manual prescribe that restricted fund balance or restricted net position cannot be negative.

This was not reported as a finding in prior audits.

Cause of Condition

The Organization actively tracks external restrictions made by oversight agencies. However during the fiscal year expenditures exceeded assets held for these restricted purposes due to a lack of funding. Organization management believed that the negative restricted balances reported more accurately reflected the deficit.

Staff responsible for preparing the financial statements were not aware of financial reporting requirements for fund balance classifications and did not perform additional research to determine the reporting requirements.

Effect of Condition

Because the Organization did not properly classify fund balance, Unrestricted Net Position on the Governmental Activities Statement of Net Position and Unassigned Fund Balance on the General Fund Balance Sheet were over-reported by \$2,807,372. The related balances, Restricted Net Position and Restricted Fund Balance were under-reported by the same amount.

Recommendation

We recommend the Organization ensure that financial statement preparation controls are adequate to ensure accurate financial reporting, including researching accounting treatment for unique reporting situations to ensure it reports financial statements in accordance with GAAP.

Organization's Response

The question we did not get right is how to show a negative fund balance with other restricted funding sources. We thought the blending of the negative fund balance with the other restricted funding sources did not give a clear picture of the financial situation. Presenting the information separately would be a clearer presentation of the situation. We looked at the GAAP, GASB principles along with the state BARS manual and could not find a clear answer on how to report this particular situation. We should have contacted the Washington State Auditor's Office for guidance on this issue.

Our corrective action plan is to seek help in the future if we run into the problem of having a restricted funding source with a negative fund balance or other strange situations, we cannot find clear GAAP or GASB guidance on. We will check with the Washington State Auditor's Office on how to properly present the financial situation with a help desk question.

Auditor's Remarks

We thank the Organization for its commitment to resolving the issues identified above. We will follow up on the status of this finding during our next audit.

Applicable Laws and Regulations

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in its Codification of Statements on Auditing Standards, section 265, Communicating Internal Control Related Matters Identified in an Audit, paragraph 7.

Government Auditing Standards, December 2011 Revision, paragraph 4.23 establishes reporting requirements related to significant deficiencies or material weaknesses in internal control, instances of fraud or abuse, and noncompliance with provisions of law, regulations, contracts, or grant agreements.

Governmental Accounting Standards – Statement 54 Fund Balance Reporting and Governmental Fund Type Definitions states, in part, *restricted* fund balance category includes amounts that can be spent only for the specific purposes stipulated by constitution, external resource providers, or through enabling legislation.

Budgeting, Accounting and Reporting Systems (BARS) manual 4.2.8.60 states, in part, no category of restricted component of net position can be negative, if liabilities related to restricted assets exceed those assets, no balance should be reported. The negative amount should be reported as reduction of unrestricted component of net position.

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

**North Sound Behavioral Health Organization
January 1, 2018 through December 31, 2018**

Board of Directors
North Sound Behavioral Health Organization
Mount Vernon, Washington

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities and each major fund of the North Sound Behavioral Health Organization, as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise the Organization's basic financial statements, and have issued our report thereon dated September 18, 2019. As discussed in Note 11 to the financial statements, on June 30, 2019 North Sound Behavioral Health Organization ceased operation and as of July 1, 2019 became North Sound Behavioral Health Administrative Service Organization (ASO).

INTERNAL CONTROL OVER FINANCIAL REPORTING

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of Organization's financial statements will not be prevented, or detected and

corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Audit Findings and Responses as Finding 2018-001 that we consider to be significant deficiencies.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the Organization's financial statements are free from material misstatement, we performed tests of the Organization's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

ORGANIZATION'S RESPONSE TO FINDINGS

The Organization's response to the findings identified in our audit is described in the accompanying Schedule of Audit Findings and Responses. The Organization's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

PURPOSE OF THIS REPORT

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

It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink that reads "Pat McCarthy". The signature is written in a cursive style with a large, stylized initial "P".

Pat McCarthy

State Auditor

Olympia, WA

September 18, 2019

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR
EACH MAJOR FEDERAL PROGRAM AND REPORT ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE
WITH THE UNIFORM GUIDANCE**

**North Sound Behavioral Health Organization
January 1, 2018 through December 31, 2018**

Board of Directors
North Sound Behavioral Health Organization
Mount Vernon, Washington

**REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL
PROGRAM**

We have audited the compliance of the North Sound Behavioral Health Organization, with the types of compliance requirements described in the U.S. *Office of Management and Budget (OMB) Compliance Supplement* that could have a direct and material effect on each of the Organization's major federal programs for the year ended December 31, 2018. The Organization's major federal programs are identified in the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Organization's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 *U.S. Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements

referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Organization's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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

Opinion on Each Major Federal Program

In our opinion, the Organization complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2018.

REPORT ON INTERNAL CONTROL OVER COMPLIANCE

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

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

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Purpose of this Report

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.



Pat McCarthy

State Auditor

Olympia, WA

September 18, 2019

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

North Sound Behavioral Health Organization January 1, 2018 through December 31, 2018

Board of Directors
North Sound Behavioral Health Organization
Mount Vernon, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the governmental activities and each major fund of the North Sound Behavioral Health Organization, as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise the Organization's basic financial statements as listed on page 18.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Organization'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 Organization'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 opinions.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the North Sound Behavioral Health Organization, as of December 31, 2018, and the respective changes in financial position thereof, and the budgetary comparison for the General Fund, for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Matters of Emphasis

As discussed in Note 11 to the financial statements, on June 30, 2019 North Sound Behavioral Health Organization ceased operation and as of July 1, 2019 became North Sound Behavioral Health Administrative Service Organization (ASO). Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and required supplementary information listed on page 18 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express

an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary and Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Organization's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by Title 2 *U.S. Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). This schedule is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated September 18, 2019 on our consideration of the Organization's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Organization's internal control over financial reporting and compliance.



Pat McCarthy
State Auditor
Olympia, WA

September 18, 2019

FINANCIAL SECTION

North Sound Behavioral Health Organization January 1, 2018 through December 31, 2018

REQUIRED SUPPLEMENTARY INFORMATION

Management's Discussion and Analysis – 2018

BASIC FINANCIAL STATEMENTS

Statement of Net Position – 2018

Statement of Activities – 2018

Balance Sheet – Governmental – 2018

Reconciliation of Balance Sheet of Governmental Funds to the Statement of Net Position
– 2018

Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental –
2018

Reconciliation of Governmental Funds Statement of Revenues, Expenditures and
Changes in Fund Balance to the Statement of Activities – 2018

Statement of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual
– General Fund – 2018

Notes to Financial Statements – 2018

REQUIRED SUPPLEMENTARY INFORMATION

Schedule of Proportionate Share of Net Pension Liability – PERS 1 – 2018

Schedule of Employer Contributions – PERS 1 – 2018

Schedule of Proportionate Share of Net Pension Liability – PERS 2/3 – 2018

Schedule of Employer Contributions – PERS 2/3 – 2018

SUPPLEMENTARY AND OTHER INFORMATION

Schedule of Expenditures of Federal Awards – 2018

Notes to the Schedule of Expenditures of Federal Awards – 2018

North Sound Behavioral Health Organization

MANAGEMENT'S DISCUSSION AND ANALYSIS

North Sound Behavioral Health Organization (NSBHO) discussion and analysis offers readers of our financial statements a narrative overview and analysis of our financial activities for the fiscal year ended December 31, 2018. We encourage readers to consider the information presented here in conjunction with the financial statements and notes to the financial statements (which immediately follow this discussion). We are a joint venture between five counties, and we have eight American Indian tribes in our region.

The North Sound Regional Support Network did a business conversion in 2016 to become the North Sound Behavioral Health Organization LLC. We changed our name and business structure because we added the public substance use disorder business for our five-county region. The state government passed Second Substitute Senate Bill 6312 on April 4, 2014. This bill directs the integration of mental health and substance use disorder treatment. On April 1, 2016, North Sound BHO took over the responsibility to fund both outpatient and residential substance use disorder treatment services with our state managed care contract.

In October 2017 the Counties Executive Authorities Committee (Board) voted to become a mid-adopter and become a "Behavioral Health Administrative Service Organization" (BH-ASO). This means the agency will become a behavioral health crisis service agency and administer a few of the other state and grant funded services. The ASO will not have a Medicaid service contract with the state of Washington. The state of Washington will contract with five Apple Health Managed Care Organizations (MCOs) and the BH-ASO will provide Medicaid and non-Medicaid crisis services. The State's Medicaid contracts will be with the five MCOs. The original plan was having the BHO transition to a BH-ASO on January 1, 2019. However, that did not happen. Our plan was revised by the Health Care Authority to do the transition on July 1, 2019.

FINANCIAL HIGHLIGHTS

Total expenditures are \$19,610,344 higher in 2018 compared to 2017 on the statement of revenues and expenditures. Total revenues are \$9,971,957 higher than the prior year on the same statements. Ending fund balance decreased to \$19,188,928 in 2018 from \$41,118,243 in 2017. The Executive Committee has again committed fund balances aimed at projects to expand, improve and meet the changing requirements of the mental health and substance use disorder systems in our region. This includes increasing infrastructure development and substance use disorder funding needs higher than projected revenues.

The Medicaid service rules changed July 1, 2017. The Institution for Mentally Diseased (IMD) rule changed. If a Medicaid client stays in an IMD facility for more than 15 days in a month the BHO or MCO will not receive a Medicaid PM/PM payment for that person for that month. That means we cannot use Medicaid funds for that person's service expenses for that month. However, we are required to treat this person as a Medicaid eligible person who is entitled to all of the services. We just have to use state funds to pay for those services. We reported on our quarterly compliance reports on our cash basis. The first 18 months (July 1, 2017 to December 31, 2018) of the IMD rule change we received \$4,702,507 in back fill funds. We paid out \$10,420,988 in expenses. The loss of \$5,718,481 took away our state funds reserve and we have a negative fund balance. We have been working with the state on this issue to document the level of unfunded IMD expenditures and develop a corrective action plan. We have reduced state funded services as much as possible. However, that will not solve the negative funds balance problem.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to North Sound BHO's basic financial statements. The basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements.

Government-wide Financial Statements

There are two government-wide financial statements designed to provide readers with a broad overview of the North Sounds finances in a manner similar to a private-sector business. The accounting rules require governmental agencies to distinguish functions that are principally supported by taxes and intergovernmental revenues (referred to as "governmental activities") from functions that are intended to recover all or a significant portion of their costs through user fees and charges (referred to as "business-type activities"). All North Sounds activities are considered governmental activities and are dedicated to providing behavioral health services to the community. The statement of net position presents information on all North Sounds assets and liabilities, with the difference between the two reported as net position. This statement serves a purpose similar to that of the balance sheet of a private-sector business. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the North Sound is improving or deteriorating. However, this is just one indicator of the financial health of the organization. Other indicators include the statement of activities information showing how North Sounds net position changed during 2018. All changes in net position are reported using the accrual basis of accounting, similar to the method used by most private-sector companies. The accrual basis of accounting requires that revenues be reported when they are earned, and expenses are reported when the goods and services are received, regardless of the timing of the cash flow. Items such as unpaid vendor invoices for items received in 2018 and earned but unused vacation leave and a portion of sick leave, will be included in the statement of activities as revenue and expense, even though the cash associated with these items will not be received or distributed in 2018.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. North Sound BHO, like other state and local governments, is required to use fund accounting. Because North Sound BHO is an organization dedicated to a single purpose, it has only one category of funds, the Governmental Fund type. Governmental Funds are used to account for most, if not all, of a government's tax-supported activities.

Governmental Funds

North Sound BHO has only one fund under this category, called the General Fund. The Balance Sheet and the Statement of Revenues, Expenditures, and Changes in Fund Balances present North Sound BHO's financial data for its General Fund.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike government-wide financial statements' use of accrual accounting, governmental fund financial statements focus on near-term inflows and outflows of spendable resources and on balances of spendable resources available at the end of the fiscal year. Such information is useful in evaluating a government's near-term financing requirements in comparison to near-term resources available. Because the focus of governmental fund financial statements is narrower than that of government-wide financial statements, it is useful to compare information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide reconciliation to the governmental activity's column in the government-wide statements in order to facilitate this comparison.

The North Sound BHO maintains budgetary controls over its operating funds. As stated above, North Sound BHO has only one fund, the General Fund. Because of this, there is substantial similarity between the Governmental Funds financial statements and the Government Wide financial statements. However, the above discussion of accrual vs. non-accrual reporting explains the minor differences that may be found.

Proprietary Funds

North Sound BHO has no proprietary funds.

Fiduciary Funds

North Sound BHO has no fiduciary funds.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found immediately following the basic financial statements in this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Statement of Net Position

As noted earlier, Net Position may serve over time as a useful indicator of a government's financial position. Refer to Table 1 when reading the following analysis of Net Position. North Sound BHO's Net Position total was \$17,965,887 at December 31, 2018 compared to \$39,995,437 at December 31, 2017. Please note the unrestricted net position has gone from \$6,798,707 to \$1,675,628.

Table 1: Summary of Net Position 2018 versus 2017		
As of December 31, 2018		
	2017	2018
Current Assets	\$56,829,204	\$33,171,243
Capital Assets	937,947	684,240
Total Assets	\$57,767,151	\$33,855,483
Deferred outflow of Resources	\$719,526	\$594,359
Total Deferred outflow of Resources	\$719,526	\$594,359
Current Liabilities	\$15,611,614	\$13,965,118
Non-Current Liabilities	2,417,961	1,888,348
Total Liabilities	\$18,029,575	\$15,853,466
Deferred Inflow of Resources	\$461,665	\$630,489
Total Deferred Inflow of Resources	\$461,665	\$630,489
Net Position:		
Investment in Capital Assets	\$937,947	\$684,240
Restricted for Medicaid	31,557,711	15,606,019
Restricted for State Funds	701,072	0
Unrestricted	6,798,707	1,675,628
Total Net Position	\$39,995,437	\$17,965,887

North Sound BHO's total assets are \$33,855,483 at December 31, 2018. The majority of North Sound BHO assets were accounted for in cash, cash equivalents, and investments. At December 31, 2018, the North Sound BHO had outstanding liabilities of \$15,853,466, a majority of which is due within a year. Included in liabilities in the table is \$9,775,993 in accounts payable, \$4,189,125 due to governmental units.

The deferred outflow of resources decreased to \$594,359 in 2018 from \$719,526 in 2017 due to the pension adjustment. The Deferred inflows of resources increased from \$461,665 in 2017 to \$630,489 in 2018.

Statement of Activities

Refer to Table 2 when reading the following analysis of the Statement of Activities. North Sound BHO's total net position decreased by (\$22,029,550) in 2018 compared to a decrease of (\$12,349,183) in 2017. Governmental revenue increased in 2018 by \$9,850,258 and expenses increased by \$19,652,324 compared to 2017.

Table 2: Summary of Statement of Activities		
For the Year Ended December 31, 2018		
	2017	2018
Governmental Activities		
Governmental Revenues	\$157,665,607	\$167,515,865
Governmental Expenditures	170,530,103	190,182,427
Net Governmental Activities	(\$12,864,496)	(\$22,666,562)
General Revenues		
Investment Earnings	\$514,888	\$597,832
Miscellaneous Revenue	425	39,180
Total General Revenue	\$515,313	\$637,012
Change in Net Position	(\$12,349,183)	(\$22,029,550)
Net Position - Beginning	\$52,344,620	\$39,995,437
Net Position - Ending	\$39,995,437	\$17,965,887

FINANCIAL ANALYSIS OF THE NORTH SOUND BHO FUNDS

As noted earlier, North Sound BHO uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. North Sound BHO only has one fund, the General Fund and it is a governmental type fund.

Governmental Funds Balance Sheet Analysis

The Balance Sheet is an analysis of North Sound's General Fund assets and liabilities as of December 31, 2018.

North Sound BHO General Fund

The focus of North Sound BHO's general fund is to provide information on near-term inflows, outflows, and balances of spendable resources. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. As of December 31, 2018, North Sound's general fund reported a fund balance of \$19,188,928 compared to the prior year of \$41,118,243. There is an unassigned fund balance of \$3,471,909 in 2018 compared to the unassigned fund balance of \$8,859,459 in 2017. A Medicaid risk and inpatient reserve fund balance of \$13,151,855 is not available for spending because it is a contractually required reserve. The state funds inpatient reserves is \$0 at the end of 2018. Our reserve requirements are as follows: For the Medicaid fund a 10.5% risk and inpatient reserve and up to 20.4% for operating reserves. On the state fund side, we are required to have a 5.8% inpatient reserve and can have up to a 16.8% operating reserve. The negative state fund balance of \$2,807,372 is netted against the unassigned fund balance. This has the effect of reducing the unassigned fund balance from \$6,390,281 to 3,582,909.

The general fund is in good condition at the end of 2018 for Medicaid funding. The state funds fund balance is not in good condition at the end of 2018 it has a negative fund balance. Reductions in state funded services have been implemented in 2018 to reduce state fund expenditures. Unless additional state funds are provided to cover IMD expenditures to the North Sound BHO. The IMD funding short fall for North Sound will continue.

GENERAL FUND BUDGETARY HIGHLIGHTS

The original adopted operating budget for the North Sound BHO was \$147,775,296 for revenue and expense. The final budget was \$190,550,296 for revenue and expense (see Statement of Revenue Expenditures and Change in fund Balance – Budget to Actual for more information). The budget was increased by using beginning fund balance as a source of revenue in the amount of \$27,000,000 and charges for service in the amount of \$15,775,000.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

North Sound has computers and lease hold improvements recorded as capital assets. We added lease hold improvements and equipment to our office in the amount of \$93,315 during 2018. The total net book value at December 31, 2018 is \$684,240.

* Reference the accompanying notes to the financial statements for more information.

Long-Term Debt

North Sound had no long-term debt during 2018.

ECONOMIC FACTORS

North Sound BHO serves at the pleasure of the state, federal and local governments who provide funding through the Washington Health Care Authority (HCA). Our role is to serve the clients in our five-county region. The North Sound took over the public substance use disorder system in 2016. In 2017 we struggled with the availability of state funds due to the change in the IMD rules. In 2018 the IMD issue depleted the state reserve balance and we have a negative state fund balance. We are working with the HCA and the Governor's office on this issue. No additional funds were appropriated in the state budget passed in 2019 by the legislator.

In July 2018 the IMD rule was modified and Substance Use Disorder (SUD) residential services were removed. Since then we receive \$11,043 a month in IMD back fill funds from the state. Our IMD hospital expenses have been between \$91,422 and \$565,428 a month in 2018. In March of 2019 we had a monthly IMD hospital bill of over \$611,000.

The closing of the BHO and the transition to the ASO is proceeding as planned and will happen July 1, 2019. We will have a six-month close out of the BHO from July 1, 2019 to December 31, 2019. We will also be operating the ASO at the same time.

Requests for Information

This financial report is designed to provide a general overview of North Sound BHO's finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to:

Bill Whitlock, Fiscal Officer
North Sound Behavioral Health Organization
301 Valley Mall Way, Suite 110
Mount Vernon, WA 98273
360-416-7013
Visit our website at <http://www.northsoundbho.org/>

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION

Statement of Net Position

December 31, 2018

	Governmental Activities General Fund
<u>ASSETS</u>	
Current Assets	
Cash	\$ 1,833,204
Cash Equivalents	\$ 22,661,207
Investments	3,049,075
Deposits	17,000
Miscellaneous receivables	698,401
Accrued Interest	49,875
Due From Other Gov't Units	4,862,481
TOTAL CURRENT ASSETS	\$ 33,171,243
Non-current Assets	
Capital Assets Not being Depreciated	-
Capital Assets being Depreciated	1,434,772
Less: Accumulated Depreciation	750,532
Net Assets Being Depreciated	684,240
TOTAL LONG TERM ASSETS	\$ 684,240
TOTAL ASSETS	\$ 33,855,483
<u>Deferred outflow of Resources</u>	
Revenue Outflows	594,359
TOTAL DEFERRED OUTFLOW OF RESOURCES	\$ 594,359
<u>LIABILITIES</u>	
Current Liabilities	
Accounts/Vouchers Payable	\$ 9,775,993
Due To Other Gov't Units	4,189,125
Current Portion of long term Debt	-
TOTAL CURRENT LIABILITIES	\$ 13,965,118
Non-current Liabilities	
Compensated Absences	269,951
Notes Payable	-
Net Pension Liability	1,618,397
Total Non-current Liabilities	\$ 1,888,348
TOTAL LIABILITIES	\$ 15,853,466
<u>Deferred inflow of Resources</u>	
Deferred inflows	630,489
TOTAL DEFERRED INFLOW OF RESOURCES	\$ 630,489
Net Position	
Net Investment in Capital Assets	\$ 684,240
Restricted for Medicaid	15,606,019
Restricted for State Funds	-
Unrestricted	1,675,628
TOTAL Net Position	\$ 17,965,887

The notes to financial statements are an integral part of this statement.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION

Statement Of Activities
For The Year Ended December 31, 2018

		Program Revenue		
		Grants & Fees		Primary Government
		Grants and Contribution		Business
		service	s	Governmental Type
				Activities Total
<u>Governmental Activities:</u>				
Mental & Physical Health	\$190,182,427	162,928,742	\$ 4,587,123	(22,666,562)
Total Governmental Activities	\$190,182,427	162,928,742	\$ 4,587,123	-\$ (22,666,562)
<u>Business-Type Activities:</u>				
Total Business-Type Activities:	-	-	-	-
Total Primary Government	\$190,182,427	162,928,742	\$ 4,587,123	-\$ (22,666,562)
<u>General Revenues</u>				
Investment Earnings			597,832	597,832
Miscellaneous			39,180	39,180
<u>Transfers</u>			-	-
Total General Revenue & Transfers			\$ 637,012	-\$ 637,012
Change in Net Position			-\$ (22,029,550)	-\$ (22,029,550)
Net Position-Beginning			39,995,437	39,995,437
Net Position-Ending			\$ 17,965,887	\$ 17,965,887

The notes to financial statements are an integral part of this statement.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION

Balance Sheet Governmental

December 31, 2018

	General Fund	Total
<u>ASSETS</u>		
Assets		
Cash	\$ 1,833,204	\$ 1,833,204
Cash Equivalents	22,661,207	22,661,207
Investments	3,049,075	3,049,075
Deposits	17,000	17,000
Accrued Interest	49,875	49,875
Miscellaneous Receivable	698,401	698,401
Due From Other Gov't Units	4,862,481	4,862,481
TOTAL CURRENT ASSETS	\$ 33,171,243	\$ 33,171,243
 <u>LIABILITIES AND FUND BALANCE</u>		
Liabilities		
Accounts/Vouchers Payable	\$ 9,775,993	\$ 9,775,993
Due To Other Gov't Units	4,189,125	4,189,125
TOTAL CURRENT LIABILITIES	\$ 13,965,118	\$ 13,965,118
 <u>Deferred Inflow of Resources</u>		
Intergovernmental Revenue Received But Not Earned	17,197	17,197
	\$ 17,197	\$ 17,197
 <u>Fund Balance</u>		
Restricted Fund Balance - Risk & Inpatient Medicaid	\$ 13,151,855	\$ 13,151,855
Restricted Fund Balance - Inpatient State	-	-
Restricted Fund Balance - Contracts Medicaid	2,454,164	2,454,164
Restricted Fund Balance - Contracts State	-	-
Unassigned Fund Balance	3,582,909	3,582,909
TOTAL FUND BALANCE	\$ 19,188,928	\$ 19,188,928
 Total Liabilities, Deferred Inflows of Resources and Fund Balances		
	\$ 33,171,243	\$ 33,171,243

The notes to financial statements are an integral part of this statement.

North Sound Behavioral Health Organization

Reconciliation of the Balance Sheet of Governmental Funds to the Statement of Net Position for the Year Ended December 31, 2018

Total fund balance as shown on the Governmental Statement Balance Sheet is \$19,188,928 compared to \$17,965,887 shown on the Statement of Net Position. This is a difference of \$1,223,041.

The reconciling item is compensated absences in the amount of \$269,591. This is not shown on the Balance Sheet of the Governmental Funds but is part of the Statement of Net Position.

The deferred outflows of revenue related to the pension are \$594,359 along with the deferred inflows and the net pension liability in the amounts of \$613,292 and \$1,618,397.

The capital assets net of accumulated depreciation in the amount of \$684,240 are shown on the Statement of Net Position and not on the Balance Sheet.

The difference between the statements is $\$1,223,041 = 269,951 - 594,359 + 1,618,397 + 613,292 - 684,240$.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION

**Statement of Revenue, Expenditures
and Changes In Fund Balance
Governmental
Year Ended December 31, 2018**

	General Fund 2018
<u>REVENUES</u>	
<u>Intergovernmental Revenue</u>	
Direct Federal Grants	\$ 34,826
Indirect Federal Grants	4,552,297
<u>Charges for Service</u>	
Charges for Service	162,425,600
Local Funds	503,142
<u>Miscellaneous Revenues</u>	
Investment Interest	597,832
Miscellaneous Revenues	39,180
TOTAL REVENUE	<u>\$ 168,152,877</u>
<u>EXPENDITURES</u>	
<u>Current:</u>	
Behavioral Health	\$ 189,830,055
<u>Capital Outlay</u>	
Behavioral Health	252,137
TOTAL EXPENDITURES	<u>\$ 190,082,192</u>
Excess of Revenues Over (Under) Expenditures	\$ (21,929,315)
Net Change in Fund Balance	\$ (21,929,315)
Fund Balance - Beginning 1/1/18	41,118,243
Fund Balance - Ending 12/31/18	<u>\$ 19,188,928</u>

The notes to financial statements are an integral part of this statement.

North Sound Behavioral Health Organization

Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities for the Year Ended December 31, 2018

The net change in fund balances as shown on Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balance is (\$21,929,315) The change in net position on the Statement of Activities equals (\$22,029,550). This represents a difference of \$100,235.

The revenues are the same under both reporting methods. However, the expenditures are different because the statement of activities capitalizes assets and uses depreciation. The governmental funds expense assets in the year purchased and do not depreciate assets. The depreciation expense for the year ended 2018 is \$347,022. Capitalized Assets purchased during 2018 are \$93,315. One dollar rounding

Another difference in reporting is the change in compensated absences from \$214,988 at December 31, 2017 to \$269,951 at December 31, 2018. The difference is \$54,963. Compensated absences represent the vacation and some sick leave pay off amount at year end.

The statement of activities recognizes additional pension expense per GASB 68 and the governmental funds do not. The additional pension expense is (\$203,424). Change in deferred outflows from DRS reporting method to accrual basis for 7/1/17 to 12/31/17 resulted in an additional reduction in pension expense of (\$5,010).

The total difference between the statements is \$100,235 = \$347,022-93,315+54,963-203,424-5,010-1.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION

**Statement of Revenues, Expenditures
and Changes In Fund Balance - Budget and Actual
General Fund**

Year Ended December 31, 2018

<u>REVENUES</u>	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Variance Positive (Negative)</u>
<u>Intergovernmental Revenue</u>				
Direct Federal Grants		-	34,826	34,826
Indirect Federal Grants	4,532,519	4,532,519	4,552,297	19,778
<u>Charges for Service</u>				
Charges for Service	143,122,777	158,897,777	162,425,600	3,527,823
Local Funds			503,142	503,142
<u>Miscellaneous Revenues</u>				
Investment Interest	100,000	100,000	597,832	497,832
Miscellaneous Revenues	20,000	20,000	39,180	19,180
TOTAL REVENUE	\$ 147,775,296	\$ 163,550,296	\$ 168,152,877	\$ 4,602,581
<u>EXPENDITURES</u>				
Behavioral Health	\$ 147,735,296	\$ 190,290,296	\$ 189,830,055	\$ 460,241
Capital Outlays	40,000	260,000	252,137	7,863
Debt Service	0	0	0	-
TOTAL EXPENDITURES	\$ 147,775,296	\$ 190,550,296	\$ 190,082,192	\$ 468,104
Excess of Revenues Over (Under) Expenditures	\$ -	\$ (27,000,000)	\$ (21,929,315)	\$ 5,070,685
<u>Other Financing Sources</u>				
Proceeds from Long Term Note			\$ -	\$ -
Net Change in Fund Balance	\$ -	\$ (27,000,000)	\$ (21,929,315)	\$ 5,070,685
Fund Balance - Beginning 1/1/18		27,000,000	\$ 41,118,243	\$ 14,118,243
Fund Balance Ending - 12/31/18	\$ -	\$ -	\$ 19,188,928	\$ 19,188,928

The notes to financial statements are an integral part of this statement.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of North Sound Behavioral Health Organization have been prepared in conformity with generally accepted accounting principles (GAAP), as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The chart of accounts conforms to the Budgeting, Accounting, and Reporting Systems (BARS) prescribed by the office of the State Auditor, to promote uniformity among the cities and counties of Washington resulting in better comparability. The significant accounting policies are described below.

A. Reporting Entity

State Senate Bill 5400, regionalizing mental health services in Washington State was passed and signed into law in May 1989. This bill allowed geographical areas to jointly provide mental health services to the combined populations. In October 1989, an Interlocal Agreement was approved by Island County, San Juan County, Skagit County, Snohomish County, and Whatcom County creating the North Sound Regional Support Network (NSRSN). In March 1990, the State Legislature provided funding for the NSRSN to begin operations on January 1, 1991. The NSRSN first had financial activity in October 1990.

North Sound Behavioral Health Organization is a governmental agency providing a variety of mental health and substance use disorder services to a five-county region. During 2016, the North Sound Regional Support Network changed their entity status and name to the North Sound Behavioral Health Organization February 2016. We did a business conversion to a limited liability corporation and changed the name to North Sound Behavioral Health Organization. On April 1, 2016, the North Sound BHO started administering the public substance use disorder contracts along with the public Mental Health contracts for our five-county region.

The North Sound BHO does not have any component units.

B. Government-Wide and Fund Financial Statements

Government wide financial statements consist of the statement of net position and the statement of activities. These statements report information on all of the non-fiduciary activities of the primary government. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separate from business-type activities, which rely to a significant extent on fees and charges for support.

The North Sound Behavioral Health Organization only has one fund, the general fund.

The statement of activities demonstrates the degree to which the expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment.

Program revenues include grants and contributions that are restricted to meeting the operation or capital requirements of a particular function. Fund financial statements are used to report additional and more detailed information about the primary government.

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the North Sound considers revenues to be available if they are collected within 120 days of the end of the current fiscal period. The North Sound considers property taxes as available if they are collected within 60 days after year end. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

C. Measurement Focus, Basis of Accounting, and Financial Statement Presentation (continued)

See Note 1 D 8 Compensated Absences.

The North Sound reports the following major governmental fund: The General Fund is the North Sound's primary and only operating fund. It is used to account for all activities of the government unit.

D. Assets, Liabilities, Fund Balance, Net Position

1. Cash and Equivalents

At December 31, 2018, \$2,000 is on deposit at Skagit State Bank for our petty cash and advanced travel. The employee flexible spending account had a balance of \$ 54,387 at December 31, 2018. Cash and Cash equivalents on hand at the County Treasurer's office is \$ 24,438,023. Cash Equivalents are invested in the state treasurer's investment pool and money market funds. Cash equivalents are short-term, highly liquid investments that are readily convertible to a known amount of cash and mature within three months. These amounts are classified on the Balance Sheet or in the statement of Net Position as cash and cash equivalents.

In accordance with GASB 79, qualifying short-term investments in general 2a7-like pools, money market investment and other investment with a remaining maturity of one year or less at the time of purchase are amortized at cost. All other investments are stated at fair value. For additional investment information see note 4 A.

2. Temporary Investments – See Note 4 B.

3. Receivables and Payables

Receivables are due from private companies including not for profit agencies and individuals. Due from other governments include amounts due from other government agencies. Interest Receivable consists of amounts earned on investments at the end of the year and fair value changes in accordance with GASB 31, Accounting and Financial Reporting for Certain Investments and for External Investment Pools, are included.

Payables are owed to individuals, private companies including not for profit agencies. Due to other governments include amounts owed to government agencies for services. The BHO recognize hospital inpatient bills in the month when they are billed by the Health Care Authority. The hospitals have up to twelve months to bill and the state may take years to process and bill the BHO.

4. Inventories and Prepayments

The North Sound does not carry inventories. All supplies are considered expensed when purchased. Prepayments made for services that will benefit future periods are recorded as prepaid items in government-wide statements.

5. Capital Assets

Capital assets include information technology equipment and lease hold improvements. The North Sound defines capital assets as assets with an initial, individual cost of more than \$7,500 and an estimated useful life in excess of one year.

When capital assets are purchased, they are capitalized and depreciated in the government-wide financial statements. Capital assets are recorded as expenditures of the current period in the government fund financial statements. Capital assets are valued at cost where historical records are available and at an estimated historical cost where no records exist. Donated capital assets are valued at their estimated fair value on the date received. Improvements to capital assets that materially add to the value or extend the life of the asset are capitalized. Other repairs and normal maintenance are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed. Estimated useful lives are as follows:

Information Technology Equipment – 3 to 20 years

Lease hold improvements – over the life of the lease (For more information see Note 4.)

6. Deferred Inflows of Resources

The deferred inflow of resources for the North Sound is to account for amounts for which revenue recognition criteria have not been met. The funds are associated with obligations that are allocated to specific contracts but have not been spent or earned.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

Note 1 D. Assets, Liabilities, Fund Balance, Net Position (continued)

7. Deferred Outflows of Resources

Deferred outflow of resources is a consumption of net assets by the government that is applicable to a future reporting period. This is the portion of the state's pension funding system that relates to the BHO.

8. Compensated Absences

It is the North Sound's policy to permit employees to accumulate earned but unused vacation leave benefits. All vacation pay is accrued when incurred in the government-wide fund financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements. The non-current portion for governmental funds is not reported in the governmental fund statements and represents a reconciling item between the fund and government-wide presentations.

Employees receive vacation pay, which may be accumulated up to a maximum of 30 days, is payable upon resignation, retirement or death. Sick leave may accumulate up to a maximum of 120 days. An employee leaving the North Sound Behavioral Health Organization is entitled to be paid for unused vacation and 25% of sick leave after completion of five years of service. Employee benefit payout for 2018 was \$269,951 including estimated benefits.

9. Long-Term Debt - See Note 5

10. Fund Equity

Fund equity is recognized as fund balance in governmental fund types. Fund equity is classified by the nature of the restriction on future use. The following are classifications of fund balance; nonspendable, restricted, committed, assigned, unassigned. The North Sound has restricted, committed, and unassigned fund balances.

Nonspendable Fund Balance – The portion of net resources that cannot be spent because either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

Restricted Fund Balance - That portion of net resources that contains limitations imposed by creditors, grantors, contributors, or laws and regulations of other governments or enabling legislation.

Committed Fund Balance – Are amounts that are to be used for a specific purpose pursuant to constraints imposed by formal action of the government's highest level of decision making authority.

Assigned fund balance - Funds set aside by the governing body for a specific purpose. The North Sound Executive has the authority to restrict and unrestricted the funds.

Unassigned Fund Balance - The residual net resources in excess of Nonspendable, Restricted, Committed and Assigned. See Note 10 for more information.

11. Pensions

For purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of all state sponsored pension plans and additions to/deductions from those plans' fiduciary net position have been determined on the same basis as they are reported by the Washington State Department of Retirement Systems. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

NOTE 2 - RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

A. Explanation of Certain Differences between the Balance Sheet of the Governmental Funds and the Government-Wide Statement of Net Position

The net change in fund balances as shown on Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balance is (\$21,929,315) The change in net position on the Statement of Activities equals (\$22,029,550). This represents a difference of \$100,235.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 2 - RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS (continued)

The revenues are the same under both reporting methods. However, the expenditures are different because the statement of activities capitalizes assets and uses depreciation. The governmental funds expense assets in the year purchased and do not depreciate assets. The depreciation expense for the year ended 2018 is \$347,022. Capitalized Assets purchased during 2018 are \$93,315. One dollar rounding

Another difference in reporting is the change in compensated absences from \$214,988 at December 31, 2017 to \$269,951 at December 31, 2018. The difference is \$54,963. Compensated absences represent the vacation and some sick leave pay off amount at year end.

The statement of activities recognizes additional pension expense per GASB 68, and the governmental funds do not. The additional pension expense is (\$203,424). Change in deferred outflows from DRS reporting method to accrual basis for 7/1/17 to 12/31/17 resulted in an additional reduction in pension expense of (\$5,010).

The total difference between the statements is $\$100,235 = \$347,022 - 93,315 + 54,963 - 203,424 - 5,010 - 1$.

B. Explanation of Certain Differences Between the Governmental Fund Statement of Revenues, Expenditures, and Changes in Fund Balances and the Government-Wide Statement of Activities

Total fund balance as shown on the Governmental Statement Balance Sheet is \$19,188,928 compared to \$17,965,887 shown on the Statement of Net Position. This is a difference of \$1,223,041.

The reconciling item is compensated absences in the amount of \$269,591. This is not shown on the Balance Sheet of the Governmental Funds but is part of the Statement of Net Position.

The deferred outflows of revenue related to the pension are \$594,359 along with the deferred inflows and the net pension liability in the amounts of \$613,292 and \$1,618,397.

The capital assets net of accumulated depreciation in the amount of \$684,240 are shown on the Statement of Net Position and not on the Balance Sheet.

The difference between the statements is $\$1,223,041 = 269,951 - 594,359 + 1,618,397 + 613,292 - 684,240$.

NOTE 3 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Information

1. Scope of Budget

The annual budget for North Sound is adopted in accordance with the provisions of the Revised Code of Washington (RCW), as interpreted by the Budgeting, Accounting, and Reporting System (BARS) of the State of Washington, and on a basis consistent with generally accepted accounting principles. The annual appropriated budget is adopted at the fund level. All appropriations lapse after the close of each fiscal year. All expenditures incurred prior to year-end, but not paid until this thirty-day period are considered expenditures against the budget for the prior year and are reported as accounts payable.

2. Procedure for Adopting the Original Budget

On or before December 1 of each year, a budget is prepared showing for each object, actual expenditures for the prior year, current year estimated, and requested appropriations for the next fiscal year. A proposed budget is presented to the Executive Committee and public. After public meetings and Advisory Board approval a recommended budget is brought to the Board of Directors for approval. The Board of Directors approves the recommended budget on or before December 31st of each year and it becomes the adopted budget.

3. Amending the Budget

The Executive Director is authorized to approve budget transfers between appropriation units (sub-object of expenditure). However, the following circumstances require Executive Committee approval:

Revisions that affect the appropriation units of salaries and wages or capital outlay. Revisions that create new salaried positions. Revisions that establish new programs. Revisions that delete ongoing programs. Revisions that alter the total expenditures of the budget. The budget amounts shown in the financial statements are the final authorized amounts revised during 2018.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 3 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY (continued)

B. Deficit fund balance

The North Sound does have a negative fund balances on the balance sheet. We have a negative fund balance in our state funds account in the amount of (\$2,807,372). This is due to the change in the Institution for Mentally Diseased (IMD) rule starting July 1, 2017. The rules say if a Medicaid client stays in an IMD facility for more than 15 days in a month the BHO will not receive a Medicaid PM/PM payment for that person for that month. That means the persons Medicaid eligibility is suspended and we cannot use Medicaid funds for that person's service expenses for that month. However, we are required to treat this person as a Medicaid eligible person who is entitled to all of the services. We just have to use state funds to pay for those services. We reported on our quarterly compliance reports on our cash basis. The first 18 months (July 1, 2017 to December 31,2018) of the IMD rule change we received \$4,702,507 in back fill funds. We paid out \$10,420,988 in expenses. The loss of \$5,718,481 depleted our state funds reserve and we have a negative fund balance. We have been working with the state on this issue to document the level of unfunded IMD expenditures and develop a corrective action plan. We have reduced state funded services as much as possible. However, that will not solve the negative funds balance problem at the end of 2018.

NOTE 4 – DETAILED NOTES ON THE GENERAL FUND

A. Deposits

The North Sound Behavioral Health Organization utilizes the services of the Skagit County Treasurer. All deposits are covered by Federal deposit insurance corporation (FDIC) and also covered by the Washington State Public Deposit Protection Commission (PDPC). The PDPC protection is in the nature of collateral and not insurance, pursuant to Governmental Accounting Standards Board of Statement No. 3.

As of December 31, 2018, the North Sound Behavioral Health Organization held the following deposits and short-term investments operating within the parameters outlined in GASB 79 and qualifying to be reported at amortized cost: money market accounts \$10,656,723 and state investment pool \$12,004,483, petty cash \$56,387. The deposit shown on the balance sheet in the amount of \$17,000 is a damage deposit required for the office-building lease.

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a failure of the counterparty to an investment transaction North Sound Behavioral Health Organization would not be able to recover the value of the investment or collateral securities. North Sound Behavioral Health Organization has no custodial credit risk as of December 31, 2018.

The North Sound Behavioral Health Organization does not hold investments for other local governments, individuals or private organizations. Statutes authorize the County, acting as an agent of the North Sound Behavioral Health Organization, to invest in obligations of the U.S. Treasury and its instrumentalities, banker's acceptances issued in the secondary market, primary certificates of deposit issued by Washington State qualified public depositories as defined under Chapter 39.58 of the Revised Code of Washington, and the State Treasurer's investment pool.

B. Investments Measured at Fair Value

The North Sound Behavioral Health Organization measures and reports investments at fair value using the valuation input hierarchy established by generally accepted accounting principles, as follows:

- Level 1: Quoted prices in active markets for identical assets or liabilities;
- Level 2: These are quoted market prices for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other than quoted prices that are not observable;
- Level 3: Unobservable inputs for an asset or liability.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

NOTE 4 – DETAILED NOTES ON THE GENERAL FUND (continued)

At December 31, 2018, the North Sound Behavioral Health Organization had the following investments measured at fair value:

Investments by Fair Value	12/31/2018	in Active Markets for Identical Assets (Level1)	Significant Other Observable Input (Level 2)	Significant Unobservable Input (Level 3)
Treasury Bills	\$ 3,049,075		\$ 3,049,075	
Total Investments by Fair Value	\$ 3,049,075		\$ 3,049,075	

C. Receivables

Accrued interest receivable consists of amounts earned on investments at the end of the year. At the end of 2018 the accrued interest receivable is \$49,875.

Accounts receivable are \$698,401. They consist of amounts owed from private individuals or organizations for goods and services including amounts owed for which billings have not been prepared. Most of our accounts receivable are from reconciliations of budget payment to actual for start-up organizations when we took over the substance use disorder business.

Due from other governmental units in the amount of \$4,862,481 represent grant funds that were owed but not received by year-end. Most of the amounts owed were from Washington State Health Care Authority some were from other Behavioral Health organizations.

D. Capital Assets and Depreciation

1. General Policies

Major expenditures for capital assets, including capital leases and major repairs that increase useful lives are capitalized. Maintenance, repairs, and minor renewals are accounted for as expenditures or expenses when incurred. All capital assets are valued at historical cost (or estimated cost, where historical cost is not known). The North Sound BHO has acquired certain assets with funding provided by federal financial assistance programs. Depending on the terms of the agreements involved, the federal government could retain an equity interest in these assets, however, the NSBHO has sufficient legal interest to accomplish the purposes for which the assets were acquired, and has included such assets within the applicable account group.

2. Capital Assets

Our capitalization policy is to capitalize assets that have a useful life of more than two years and cost more than \$7,500. See note 1 D 5.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

NOTE 4 – DETAILED NOTES ON THE GENERAL FUND (continued)

A summary of changes in capital assets follows:

	Balance 1/1/18	Additions	Deletions	Balance 12/31/18
Capital Assets, not being depreciated:				
Construction in Progress:	\$	\$	\$	\$
Total capital assets, not being depreciated:	\$	\$	\$	\$
Capital Assets being depreciated:				
Machinery & Equipment	\$ 494,874	\$ 93,315	\$ 101,559	\$ 486,630
Leasehold Improvements	\$ 948,142	\$	\$	\$ 948,142
Total Assets being depreciated	\$ 1,443,016	\$ 93,315	\$ 101,559	\$ 1,434,772
Less accumulated depreciation	\$ 505,069	\$ 347,022	\$ 101,559	\$ 750,532
Total capital asset being depreciated, net	\$ 937,947	\$ (253,707)	\$ 0	\$ 684,240
Total Capital assets, net	\$ 937,947	\$ (253,707)	\$	\$ 684,240

NOTE 5 – LONG TERM DEBT

The long-term debt the North Sound has are compensated absences (see note 1 D-8) and pension liabilities (see note 7).

Type of Debt	Beginning Balance 1/1/18	New Issue	Retirements	Current Portion	Ending Balance 12/31/18
Compensated Absences	\$ 214,988	\$ 74,595	\$ 19,632		\$ 269,951
Pension Liabilities	2,202,973		584,576		1,618,397
Total	\$ 2,417,961	\$ 74,595	\$ 604,208	\$ 0	\$ 1,888,348

NOTE 6 – LEASES

The North Sound Behavioral Health Organization leases the office building and other equipment under noncancelable operating leases. Total cost for such leases was \$0 for the year ended December 31, 2018. The future minimum lease payments for these leases are as follows:

Year ending December 31	Amounts
2019	\$ 257,829
2020	\$ 262,464
2021	\$ 8,691
2022	\$ 1,292
2023	\$ 0
Total	\$ 530,276

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

NOTE 7 - PENSION PLANS

The following table represents the aggregate pension amounts for all plans for the year 2018:

Aggregate Pension Amounts – All Plans	
Pension liabilities	\$ (1,618,397)
Pension assets	\$ 0
Deferred outflows of resources	\$ 594,359
Deferred inflows of resources	\$ (613,292)
Pension expense/expenditures	\$ 208,945

State Sponsored Pension Plans

Substantially all North Sound Behavioral Health Organization’s full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing, multiple-employer public employee defined benefit and defined contribution retirement plans. The state Legislature establishes, and amends, laws pertaining to the creation and administration of all public retirement systems.

The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to:

Department of Retirement Systems
 Communications Unit
 P.O. Box 48380
 Olympia, WA 98540-8380

Or the DRS CAFR may be downloaded from the DRS website at www.drs.wa.gov.

Public Employees’ Retirement System (PERS)

PERS members include elected officials; state employees; employees of the Supreme, Appeals and Superior Courts; employees of the legislature; employees of district and municipal courts; employees of local governments; and higher education employees not participating in higher education retirement programs. PERS is comprised of three separate pension plans for membership purposes. PERS plans 1 and 2 are defined benefit plans, and PERS plan 3 is a defined benefit plan with a defined contribution component.

PERS Plan 1 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member’s average final compensation (AFC) times the member’s years of service. The AFC is the average of the member’s 24 highest consecutive service months. Members are eligible for retirement from active status at any age with at least 30 years of service, at age 55 with at least 25 years of service, or at age 60 with at least five years of service. Members retiring from active status prior to the age of 65 may receive actuarially reduced benefits. Retirement benefits are actuarially reduced to reflect the choice of a survivor benefit. Other benefits include duty and non-duty disability payments, an optional cost-of-living adjustment (COLA), and a one-time duty-related death benefit, if found eligible by the Department of Labor and Industries. PERS 1 members were vested after the completion of five years of eligible service. The plan was closed to new entrants on September 30, 1977.

Contributions

The PERS Plan 1 member contribution rate is established by State statute at 6 percent. The employer contribution rate is developed by the Office of the State Actuary and includes an administrative expense component that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates. The PERS Plan 1 required contribution rates (expressed as a percentage of covered payroll) for 2018 were as follows:

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

NOTE 7 - PENSION PLANS (continued)

PERS Plan 1		
Actual Contribution Rates:	Employer	Employee*
January – August 2018:		
PERS Plan 1	7.49%	6.00%
PERS Plan 1 UAAL	5.03%	
Administrative Fee	0.18%	
Total	12.70%	6.00%
September – December 2018:		
PERS Plan 1	7.52%	6.00%
PERS Plan 1 UAAL	5.13%	
Administrative Fee	0.18%	
Total	12.83%	6.00%

* For employees participating in JBM, the contribution rate was 12.26%.

PERS Plan 2/3 provides retirement, disability and death benefits. Retirement benefits are determined as two percent of the member's average final compensation (AFC) times the member's years of service for Plan 2 and 1 percent of AFC for Plan 3. The AFC is the average of the member's 60 highest-paid consecutive service months. There is no cap on years of service credit. Members are eligible for retirement with a full benefit at 65 with at least five years of service credit. Retirement before age 65 is considered an early retirement. PERS Plan 2/3 members who have at least 20 years of service credit and are 55

years of age or older, are eligible for early retirement with a benefit that is reduced by a factor that varies according to age for each year before age 65. PERS Plan 2/3 members who have 30 or more years of service credit and are at least 55 years old can retire under one of two provisions:

- With a benefit that is reduced by three percent for each year before age 65; or
- With a benefit that has a smaller (or no) reduction (depending on age) that imposes stricter return-to-work rules.

PERS Plan 2/3 members hired on or after May 1, 2013 have the option to retire early by accepting a reduction of five percent for each year of retirement before age 65. This option is available only to those who are age 55 or older and have at least 30 years of service credit. PERS Plan 2/3 retirement benefits are also actuarially reduced to reflect the choice of a survivor benefit. Other PERS Plan 2/3 benefits include duty and non-duty disability payments, a cost-of-living allowance (based on the CPI), capped at three percent annually and a one-time duty related death benefit, if found eligible by the Department of Labor and Industries. PERS 2 members are vested after completing five years of eligible service. Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service if 12 months of that service are earned after age 44.

PERS Plan 3 defined contribution benefits are totally dependent on employee contributions and investment earnings on those contributions. PERS Plan 3 members choose their contribution rate upon joining membership and have a chance to change rates upon changing employers. As established by statute, Plan 3 required defined contribution rates are set at a minimum of 5 percent and escalate to 15 percent with a choice of six options. Employers do not contribute to the defined contribution benefits. PERS Plan 3 members are immediately vested in the defined contribution portion of their plan.

Contributions

The PERS Plan 2/3 employer and employee contribution rates are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. The Plan 2/3 employer rates include a component to address the PERS Plan 1 UAAL and an administrative expense that is currently set at 0.18 percent. Each biennium, the state Pension Funding Council adopts Plan 2 employer and employee contribution rates and Plan 3 contribution rates. The PERS Plan 2/3 required contribution rates (expressed as a percentage of covered payroll) for 2018 were as follows:

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

NOTE 7 - PENSION PLANS (continued)

PERS Plan 2/3		
Actual Contribution Rates:	Employer 2/3	Employee 2*
January – August 2018:		
PERS Plan 2/3	7.49%	7.38%
PERS Plan 1 UAAL	5.02%	
Administrative Fee	0.18%	
Employee PERS Plan 3		varies
Total	12.70%	7.38%
September – December 2018:		
PERS Plan 2/3	7.52%	7.41%
PERS Plan 1 UAAL	5.13%	
Administrative Fee	0.18%	
Employee PERS Plan 3		Varies
Total	12.83%	7.41%

* For employees participating in JBM, the contribution rate was 18.45% to 18.53%

The North Sound Behavioral Health Organization’s actual PERS plan contributions were \$166,194 to PERS Plan 1 and \$246,175 to PERS Plan 2/3 for the year ended December 31, 2018.

Actuarial Assumptions

The total pension liability (TPL) for each of the DRS plans was determined using the most recent actuarial valuation completed in 2018 with a valuation date of June 30, 2017. The actuarial assumptions used in the valuation were based on the results of the Office of the State Actuary’s (OSA) 2007-2012 Experience Study and the 2017 Economic Experience Study.

Additional assumptions for subsequent events and law changes are current as of the 2017 actuarial valuation report. The TPL was calculated as of the valuation date and rolled forward to the measurement date of June 30, 2018. Plan liabilities were rolled forward from June 30, 2017, to June 30, 2018, reflecting each plan’s normal cost (using the entry-age cost method), assumed interest and actual benefit payments.

- Inflation: 2.75% total economic inflation; 3.50% salary inflation
- Salary increases: In addition to the base 3.50% salary inflation assumption, salaries are also expected to grow by promotions and longevity.
- Investment rate of return: 7.4%

Mortality rates were based on the RP-2000 report’s Combined Healthy Table and Combined Disabled Table, published by the Society of Actuaries. The OSA applied offsets to the base table and recognized future improvements in mortality by projecting the mortality rates using 100 percent Scale BB. Mortality rates are applied on a generational basis; meaning, each member is assumed to receive additional mortality improvements in each future year throughout his or her lifetime.

There were changes in methods and assumptions since the last valuation.

- Lowered the valuation interest rate from 7.70% to 7.50% for all systems except LEOFF 2. For LEOFF 2 the valuation interest rate was lowered from 7.50% to 7.40%.
- Lowered the assumed general salary growth from 3.75% to 3.50% for all systems.
- Lowered assumed inflation from 3.00% to 2.75% for all systems.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

- NOTE 7 - PENSION PLANS (continued)
 - Modified how the valuation software calculates benefits paid to remarried duty-related death survivors of LEOFF 2 members.
 - Updated the trend that the valuation software uses to project medical inflation for LEOFF 2 survivors of a duty-related death, and for certain LEOFF 2 medical-related duty disability benefits.

Discount Rate

The discount rate used to measure the total pension liability for all DRS plans was 7.4 percent.

To determine that rate, an asset sufficiency test included an assumed 7.5 percent long-term discount rate to determine funding liabilities for calculating future contribution rate requirements. (All plans use 7.5 percent except LEOFF 2, which has assumed 7.4 percent). Consistent with the long-term expected rate of return, a 7.4 percent future investment rate of return on invested assets was assumed for the test. Contributions from plan members and employers are assumed to continue being made at contractually required rates (including PERS 2/3, PSERS 2, SERS 2/3, and TRS 2/3 employers, whose rates include a component for the PERS 1, and TRS 1 plan liabilities). Based on these assumptions, the pension plans' fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return of 7.4 percent was used to determine the total liability.

Long-Term Expected Rate of Return

The long-term expected rate of return on the DRS pension plan investments of 7.4 percent was determined using a building-block-method. In selecting this assumption, the Office of the State Actuary (OSA) reviewed the historical experience data, considered the historical conditions that produced past annual investment returns, and considered capital market assumptions and simulated expected investment returns provided by the Washington State Investment Board (WSIB). The WSIB uses the capital market assumptions and their target asset allocation to simulate future investment returns over various time horizons.

Estimated Rates of Return by Asset Class

Best estimates of arithmetic real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2018, are summarized in the table below. The inflation component used to create the table is 2.2 percent and represents the WSIB's most recent long-term estimate of broad economic inflation.

Asset Class	Target Allocation	% Long-Term Expected Real Rate of Return Arithmetic
Fixed Income	20%	1.70%
Tangible Assets	7%	4.90%
Real Estate	18%	5.80%
Global Equity	32%	6.30%
Private Equity	23%	9.30%
	100%	

Sensitivity of the Net Pension Liability/(Asset)

The table below presents the North Sound Behavioral Health Organization's proportionate share of the net pension liability calculated using the discount rate of 7.4 percent, as well as what the North Sound Behavioral Health Organization's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (6.4 percent) or 1-percentage point higher (8.4 percent) than the current rate.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

• NOTE 7 - PENSION PLANS (continued)

	1% Decrease (6.4%)	Current Discount Rate (7.4%)	1% Increase (8.4%)
PERS 1	\$ 1,336,170	\$ 1,087,256	\$ 871,646
PERS 2/3	\$ 2,429,453	\$ 531,141	\$ (1,025,262)

Pension Plan Fiduciary Net Position

Detailed information about the State's pension plans' fiduciary net position is available in the separately issued DRS financial report.

Pension Liabilities (Assets), Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At June 30, 2018, the North Sound Behavioral Health Organization reported a total pension liability of \$1,618,397 for its proportionate share of the net pension liabilities as follows (only report applicable plans):

	Liability (or Asset)
PERS 1	\$ 1,087,256
PERS 2/3	\$ 531,141

At June 30, the North Sound Behavioral Health Organization's proportionate share of the collective net pension liabilities was as follows:

	Proportionate Share 6/30/17	Proportionate Share 6/30/18	Change in Proportion
PERS 1	% .023908	% .024345	% .000437
PERS 2/3	% .030753	% .031108	% .000355

Employer contribution transmittals received and processed by the DRS for the fiscal year ended June 30 are used as the basis for determining each employer's proportionate share of the collective pension amounts reported by the DRS in the Schedules of Employer and Nonemployer Allocations for all plans except LEOFF 1.

The collective net pension liability (asset) was measured as of June 30, 2018, and the actuarial valuation date on which the total pension liability (asset) is based was as of June 30, 2017, with update procedures used to roll forward the total pension liability to the measurement date.

Pension Expense

For the year ended December 31, 2018, the North Sound Behavioral Health Organization recognized pension expense as follows:

	Pension Expense
PERS 1	\$ 117,403
PERS 2/3	\$ 91,542
TOTAL	\$ 208,945

Deferred Outflows of Resources and Deferred Inflows of Resources

At December 31, 2018, the North Sound Behavioral Health Organization reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

• NOTE 7 - PENSION PLANS (continued)

PERS 1	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$	\$
Net difference between projected and actual investment earnings on pension plan investments	\$	\$ (43,207)
Changes of assumptions	\$	\$
Changes in proportion and differences between contributions and proportionate share of contributions	\$	\$
Contributions subsequent to the measurement date	\$ 83,461	\$
TOTAL	\$ 83,461	\$ (43,207)

PERS 2 & 3	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 65,104	\$ (92,993)
Net difference between projected and actual investment earnings on pension plan investments	\$	\$ (325,933)
Changes of assumptions	\$ 6,213	\$ (151,159)
Changes in proportion and differences between contributions and proportionate share of contributions	\$ 316,600	\$
Contributions subsequent to the measurement date	\$ 122,980	\$
TOTAL	\$ 510,898	\$ (570,085)

Total for all Plans	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 65,104	\$ (92,993)
Net difference between projected and actual investment earnings on pension plan investments	\$	\$ (369,140)
Changes of assumptions	\$ 6,213	\$ (151,159)
Changes in proportion and differences between contributions and proportionate share of contributions	\$ 316,600	\$
Contributions subsequent to the measurement date	\$ 206,441	\$
TOTAL	\$ 594,359	\$ (613,292)

Deferred outflows of resources related to pensions resulting from the North Sound Behavioral Health Organization's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2019. Other amounts reported as deferred outflows and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	PERS 1
2019	\$ 1,890
2020	\$ (9,445)
2021	\$ (28,343)
2022	\$ (7,309)
2023	\$
Thereafter	\$
Total	\$ (43,207)

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

NOTE 7 - PENSION PLANS (continued)

Year ended December 31:	PERS 2/3
2019	\$ 42,949
2020	\$ (50,337)
2021	\$ (149,519)
2022	\$ (23,894)
2023	\$ 22,638
Thereafter	\$ (24,005)
Total	\$ (182,167)

Deferred Compensation

The North Sound Behavioral Health Organization offers its employees two deferred compensation programs created in accordance with Internal Revenue Code Section 457. The plan administrators are Mass Mutual Retirement Services and the Department of Retirement Services.

NOTE 8 - RISK MANAGEMENT

North Sound Behavioral Health Organization is a member of Enduris. Chapter 48.62 RCW provides the exclusive source of local government entity authority to individually or jointly self-insure risks, jointly purchase insurance or reinsurance, and to contract for risk management, claims, and administrative services. Enduris was formed July 10, 1987 pursuant to the provisions of Chapter 48.62 RCW, Chapter 200-100 WAC, and Chapter 39.34 RCW. Two (2) counties and two (2) cities in the State of Washington joined together by signing an interlocal governmental agreement to fund their self-insured losses and jointly purchase insurance and administrative services. As of August 31, 2018, there are 549 Enduris members representing a broad array of special purpose districts throughout the state. Enduris provides property and liability coverage as well as risk management services and other related administrative services.

Members make an annual contribution to fund Enduris and share in the self-insured retention of the jointly purchased excess and/or reinsurance coverage. The self-insured retention is:

\$1,000,000 self-insured retention on liability loss - the member is responsible for the first \$1,000 of the amount of each claim, while Enduris is responsible for the remaining \$999,000 on a liability loss.

\$250,000 self-insured retention on property loss - the member is responsible for the first \$1,000 of the amount of each claim, while Enduris is responsible for the remaining \$249,000 on a property loss. For property losses related to boiler and machinery Enduris is responsible for the first \$4,000 of the claim.

Enduris acquires reinsurance from unrelated insurance companies on a "per occurrence" basis to cover all losses over the self-insured retentions as shown on the policy maximum limits. Liability coverage is for all lines of liability coverage including Public Official's Liability. The Property coverage is written on an "all risk", blanket basis using current Statement of Values. The Property coverage includes but is not limited to mobile equipment, boiler and machinery, electronic data processing equipment, business interruption, course of construction and additions, property in transit, fine arts, cyber and automobile physical damage to insured vehicles. Liability coverage limit is \$20 million per occurrence and property coverage limit is \$1 billion per occurrence. Enduris offers crime coverage up to a limit of \$1 million per occurrence.

Since Enduris is a cooperative program, there is a joint liability among the participating members.

The contract requires members to continue membership for a period of not less than one (1) year and must give notice 60 days before terminating participation. The Master Agreement (Intergovernmental Contract) is automatically renewed after the initial one (1) full fiscal year commitment. Even after termination, a member is still responsible for contribution to Enduris for any unresolved, unreported and in-process claims for the period they were a signatory to the Master Agreement.

Enduris is fully funded by its member participants. Claims are filed by members with Enduris and are administered in house.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

NOTE 8 - RISK MANAGEMENT (continued)

A Board of Directors consisting of seven (7) board members governs Enduris. The Pool's members elect the Board and the positions are filled on a rotating basis. The Board meets quarterly and is responsible for conducting the business affairs of Enduris.

Enduris did not have any claim settlements that exceeded limits in the last three years.

NOTE 9 - CONTINGENCIES AND LITIGATION

North Sound Behavioral Health Organization has recorded in its financial statements all material liabilities. In the opinion of management, the North Sound Behavioral Health Organization's insurance policy is adequate to pay all known or pending claims. Grant funds are subject to audit by the grantors or their representatives. Such audits could result in requests for reimbursement to grantor agencies for expenditures disallowed under the terms of the grants. North Sound Behavioral Health Organization management believes that such disallowances, if any, will be immaterial.

NOTE 10 - FUND EQUITIES

GASB 54 requires breaking down fund balance reporting by classifying amounts by the types of restrictions placed upon them. The fund balances are classified by the following restrictions; non-spendable fund balance, restricted fund balance, committed fund balance, assigned fund balance and unassigned fund balance. The North Sound has restricted, assigned and unassigned fund balance.

Restricted fund balances have external strings attached to the funds such as contracts, agreements or legislation. These external strings have specific purposes attached to the funds limiting their use.

The committed fund balance classification includes amounts that can be used only for the specific purposes determined by a formal action of the government's highest level of decision-making authority.

Amounts in the assigned fund balance classification are intended to be used by the government for specific purposes but do not meet the criteria to be classified as restricted or committed. In governmental funds, other than the general fund, assigned fund balance represents the remaining amount that is not restricted or committed.

Assigned fund balances are amounts that are constrained by government's intent to be used for a specific purpose.

Unassigned fund balance is the residual classification for the government's general fund and includes all spendable amounts not contained in the other classifications.

A. Restricted Fund Balance

The General Fund has a total of \$13,151,855 in restricted fund balance at December 31, 2018. This is the amount set aside to satisfy the contractual reserve portion of the North Sound BHO contract with the Washington State Health Care Authority and contracts with agencies.

Medicaid Risk and Inpatient Restricted of Fund Balance at January 1, 2018	\$12,723,415
Increases in Restricted fund balance	428,440
Decreases in Restricted fund balance	
Medicaid Risk and Inpatient Restricted of Fund Balance at December 31, 2018	\$13,151,855
State Funds Inpatient Restricted of Fund Balance at January 1, 2018	\$701,072
Increases in Restricted fund balance	
Decreases in Restricted fund balance	701,072
State Funds Inpatient Restricted of Fund Balance at December 31, 2018	\$0

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 NOTES TO FINANCIAL STATEMENTS
 DECEMBER 31, 2018

NOTE 10 - FUND EQUITIES (continued)

Medicaid Contracts Fund Balance at January 1, 2018	\$18,834,297
Increases in Restricted fund balance	
Decreases in Restricted fund balance	16,380,133
Medicaid Contracts Fund Balance at December 31, 2018	\$2,454,164

State Funds Contracts Fund Balance at January 1, 2018	\$0
Increases in Restricted fund balance	
Decreases in Restricted fund balance	
State Funds Contracts Fund Balance at December 31, 2018	\$0

B. Committed Fund Balance

The General Fund has a total of \$0 in committed fund balance at December 31, 2018. This is the amount set aside by the North Sound BHO Executive Committee for implementation of the children’s mental health care redesign, expansion of our provider network.

Medicaid Committed Fund Balance at January 1, 2018	\$0
Increases in Committed fund balance	
Decreases in Committed fund balance	
Medicaid Committed Fund Balance at December 31, 2018	\$0

C. Unassigned Fund Balance

The General Fund has unassigned fund balance of \$2,807,372 at December 31, 2018.

Unassigned Fund Balance at January 1, 2018	\$8,859,459
Increases in Unassigned Fund Balance	
Decreases in Unassigned Fund Balance	\$5,276,550
Unassigned Fund Balance at December 31, 2018	\$3,582,909

The negative state fund balance of \$2,807,372 is netted against the unassigned fund balance. This has the effect of reducing the unassigned fund balance from \$6,390,281 to 3,582,909.

NOTE 11 – SUBSEQUENT EVENTS

The North Sound Behavioral Health Organization will stop providing services June 30, 2019 and will transition to an Administrative Service Organization (ASO) proceeding on July 1, 2019. The ASO will have a lot smaller scope of work. We will not continue to administer all of the Medicaid behavioral health services for the region. The main function will be on administering crisis services in the five-county region. The ASO will be a direct contractor with the state for crisis services for the non-Medicaid clients and a subcontractor to the five insurance companies that will be taking over Medicaid client services on July 1, 2019. The ASO will also have some grant funding and state proviso funding for additional service. The BHO will have a six-month close out period from July 1, 2019 to December 31,2019. We will also be operating the ASO at the same time.

REQUIRED SUPPLEMENTARY INFORMATION - State Sponsored Plans

North Sound Behavioral Health Organization
 Schedule of Proportionate Share of the Net Pension Liability
 PERS 1
 As of June 30, 2018
 Last 10 Fiscal Years*

	2018	2017	2016	2015	20XX	20XX	20XX	20XX	20XX
Employer's proportion of the net pension liability (asset) %	0.024345%	0.023908%	0.017726%	0.014286%					
Employer's proportionate share of the net pension liability \$	1,087,256	1,134,453	951,970	747,291					
Covered payroll \$	3,255,033	3,015,005	2,134,043	1,637,624					
Employer's proportionate share of the net pension liability as a percentage of covered payroll %	33.40%	37.63%	44.61%	45.63%					
Plan fiduciary net position as a percentage of the total pension liability %	63.22%	61.24%	57.03%	59.10%					

Notes to Schedule:

*Until a full 10-year trend is compiled, only information for those years available is presented.

REQUIRED SUPPLEMENTARY INFORMATION - State Sponsored Plans

North Sound Behavioral Health Organization
 Schedule of Employer Contributions
 PERS 1
 For the year ended December 31, 2018
 Last 10 Fiscal Years*

	2018	2017	2016	2015	20XX	20XX	20XX	20XX	20XX
Statutorily or contractually required contributions	\$ 166,194	154,248	124,238	80,003					
Contributions in relation to the statutorily or contractually required contributions	\$ (166,194)	(154,248)	(124,238)	(80,003)					
Contribution deficiency (excess)	\$ 0	0	0	0					
Covered payroll	\$ 3,282,342	3,160,622	2,604,581	1,842,035					
Contributions as a percentage of covered payroll	% 5.06%	4.88%	4.77%	4.34%					

Notes to Schedule:

*Until a full 10-year trend is compiled, only information for those years available is presented.

REQUIRED SUPPLEMENTARY INFORMATION - State Sponsored Plans

North Sound Behavioral Health Organization
 Schedule of Proportionate Share of the Net Pension Liability
 PERS 2/3
 As of June 30, 2018
 Last 10 Fiscal Years*

	2018	2017	2016	2015	20XX	20XX	20XX	20XX	20XX
Employer's proportion of the net pension liability (asset) %	0.031108%	0.030753%	0.022688%	0.018457%					
Employer's proportionate share of the net pension liability \$	531,141	1,068,520	1,142,323	659,479					
Covered payroll \$	3,255,033	3,015,005	2,134,043	1,637,624					
Employer's proportionate share of the net pension liability as a percentage of covered payroll %	16.32%	35.44%	53.53%	40.27%					
Plan fiduciary net position as a percentage of the total pension liability %	95.77%	90.97%	85.82%	89.20%					

Notes to Schedule:

*Until a full 10-year trend is compiled, only information for those years available is presented.

REQUIRED SUPPLEMENTARY INFORMATION - State Sponsored Plans

North Sound Behavioral Health Organization
Schedule of Employer Contributions

PERS 2/3

For the year ended December 31, 2018
Last 10 Fiscal Years*

	2018	2017	2016	2015	20XX	20XX	20XX	20XX	20XX
Statutorily or contractually required contributions	\$ 246,175	213,801	162,266	102,506					
Contributions in relation to the statutorily or contractually required contributions	\$ (246,175)	(213,801)	(162,266)	(102,506)					
Contribution deficiency (excess)	\$ 0	0	0	0					
Covered payroll	\$ 3,282,342	3,160,622	2,604,581	1,842,035					
Contributions as a percentage of covered payroll	% 7.50%	6.76%	6.23%	5.56%					

Notes to Schedule:

*Until a full 10-year trend is compiled, only information for those years available is presented.

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
 SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
 For the Fiscal Year Ended December 31, 2018

1 Federal Agency Name/Pass-Through Agency Name	2 Federal Program Name	3 CFDA Number	4 Other I.D. Number	5 Expenditures		Passed through to Subrecipients	6 Foot-note Ref.
				From Pass-Through Awards	From Direct Awards		
U.S. Department of Health and Human Services/Pass-Through from WA State Dept. of Social and Health Services	Project for Assistance in Transition from Homelessness (PATH)	93.150	1769-15573	28,489		28,489	
U.S. Department of Health and Human Services/Pass-Through from WA State Dept. of Social and Health Services	Project for Assistance in Transition from Homelessness (PATH)	93.150	1769-15574	92,848		92,848	
U.S. Department of Health and Human Services/Pass-Through from Health Care Authority	Project for Assistance in Transition from Homelessness (PATH)	93.150	K3136	10,640		10,640	
U.S. Department of Health and Human Services/Pass-Through from Health Care Authority	Project for Assistance in Transition from Homelessness (PATH)	93.150	K3138	41,815		41,815	
	Total CFDA Number 93.150			173,792		173,792	
Department of Health and Human Services Substance Abuse and Mental Health Services Administration	Medication Assisted Treatment - Prescription Drug and Opioid Addiction	93.243	1H79T1081585-01		34,826		3
U.S. Department of Health and Human Services/Pass-Through from WA State Dept. of Social and Health Services	Block Grant for Community Mental Health Services	93.958	1769-96821	245,753		245,753	
U.S. Department of Health and Human Services/Pass-Through from WA State Dept. of Social and Health Services	Block Grant for Community Mental Health Services	93.958	1769-94481	1,285,158		1,285,158	
	Total CFDA Number 93.958			1,530,911		1,530,911	
U.S. Department of Health and Human Services/Pass-Through from WA State Dept. of Social and Health Services	Substance Abuse Prevention and Treatment Block Grant	93.959	1669-58051	2,847,594		2,847,594	
	TOTAL FEDERAL AWARDS EXPENDED			4,552,297	34,826	4,587,123	1,710,906

The accompanying Notes to Schedules of Expenditures of Federal Awards is an integral part of this statement

NORTH SOUND BEHAVIORAL HEALTH ORGANIZATION
NOTES TO SCHEDULES OF EXPENDITURES OF FEDERAL AWARDS
DECEMBER 31, 2018

NOTE 1 – BASIS OF ACCOUNTING

The Schedule of Expenditures of Federal Awards is prepared on the same basis of accounting as the North Sound Behavioral Organization's financial statements. The North Sound Behavioral Organization uses the modified accrual basis of accounting for government funds.

Note 2 – PROGRAM COSTS

The amounts shown as current year expenditures represent only the federal grant portion of the program costs. Entire program costs, including the Sound Behavioral Organization's portion, are more than shown. Such expenditures are recognized following the cost principles contained in Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

Note 3 – INDIRECT COST RATE

The North Sound Behavioral Health Organization has elected to use the 10-percent de minimis indirect cost rate allowed under the Uniform Guidance on our direct federal grant CFDA 93.243. It is not being taken on any other grant.



North Sound Behavioral Health Organization, LLC

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CORRECTIVE ACTION PLAN FOR FINDINGS REPORTED UNDER UNIFORM GUIDANCE

**North Sound Behavioral Health Organization
January 1, 2018 through December 31, 2018**

This schedule presents the corrective action planned by the Organization for findings reported in this report in accordance with Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance).

Finding ref number: 2018-001	Finding caption: The Behavioral Health Organization did not have adequate internal controls in place over financial statement preparation to ensure accurate financial reporting.
Name, address, and telephone of Organization contact person: North Sound Behavioral Health Organization Bill Whitlock 360-416-7013	
Corrective action the auditee plans to take in response to the finding: <i>The question we did not get right is how to show a negative fund balance with other restricted funding sources. We thought the blending of the negative fund balance with the other restricted funding sources did not give a clear picture of the financial situation. Presenting the information separately would be a clearer presentation of the situation. We looked at the GAAP, GASB principles along with the state BARS manual and could not find a clear answer on how to report this particular situation. We should have contacted the Washington State Auditor’s Office for guidance on this issue.</i> <i>Our corrective action plan is to seek help in the future if we run into the problem of having a restricted funding sources with a negative fund balance or other strange situations, we cannot find clear GAAP or GASB guidance on. We will check with the Washington State Auditor’s Office on how to properly present the financial situation with a help desk question.</i>	
Anticipated date to complete the corrective action: Already done.	

ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

We work with our audit clients and citizens to achieve our vision of government that works for citizens, by helping governments work better, cost less, deliver higher value, and earn greater public trust.

In fulfilling our mission to hold state and local governments accountable for the use of public resources, we also hold ourselves accountable by continually improving our audit quality and operational efficiency and developing highly engaged and committed employees.

As an elected Organization, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments as well as [fraud](#), state [whistleblower](#) and [citizen hotline](#) investigations.

The results of our work are widely distributed through a variety of reports, which are available on our [website](#) and through our free, electronic [subscription](#) service.

We take our role as partners in accountability seriously, and provide training and technical assistance to governments, and have an extensive quality assurance program.

Contact information for the State Auditor's Office	
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Toll-free Citizen Hotline	(866) 902-3900
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