



Office of the Washington State Auditor
Pat McCarthy

Accountability Audit Report

Public Hospital District No. 2 of Clallam County

(Olympic Medical Center)

For the period January 1, 2022 through December 31, 2022

Published February 29, 2024

Report No. 1034337



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Office of the Washington State Auditor Pat McCarthy

February 29, 2024

Board of Commissioners
Olympic Medical Center
Port Angeles, Washington

Report on Accountability

Thank you for the opportunity to work with you to promote accountability, integrity and openness in government. The Office of the Washington State Auditor takes seriously our role of providing state and local governments with assurance and accountability as the independent auditor of public accounts. In this way, we strive to help government work better, cost less, deliver higher value and earn greater public trust.

Independent audits provide essential accountability and transparency for District operations. This information is valuable to management, the governing body and public stakeholders when assessing the government's stewardship of public resources.

Attached is our independent audit report on the District's compliance with applicable requirements and safeguarding of public resources for the areas we examined. We appreciate the opportunity to work with your staff and value your cooperation during the audit.

Sincerely,

Pat McCarthy, State Auditor
Olympia, WA

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AUDIT RESULTS

Results in brief

This report describes the overall results and conclusions for the areas we examined. In most of the areas we examined, District operations complied, in all material respects, with applicable state laws, regulations, and its own policies, and provided adequate controls over safeguarding of public resources.

As referenced above, we identified areas where the District could make improvements. These recommendations are included with our report as a finding.

In keeping with general auditing practices, we do not examine every transaction, activity, policy, internal control, or area. As a result, no information is provided on the areas that were not examined.

About the audit

This report contains the results of our independent accountability audit of Olympic Medical Center from January 1, 2022 through December 31, 2022.

Management is responsible for ensuring compliance and adequate safeguarding of public resources from fraud, loss or abuse. This includes the design, implementation and maintenance of internal controls relevant to these objectives.

This audit was conducted under the authority of RCW 43.09.260, which requires the Office of the Washington State Auditor to examine the financial affairs of all local governments. Our audit involved obtaining evidence about the District's use of public resources, compliance with state laws and regulations and its own policies and procedures, and internal controls over such matters. The procedures performed were based on our assessment of risks in the areas we examined.

Based on our risk assessment for the year ended December 31, 2022, the areas examined were those representing the highest risk of fraud, loss, abuse, or noncompliance. We examined the following areas during this audit period:

- Cash receipting – timeliness and completeness of deposits
- Accounts payable – traveling nurses and physicians
- Payroll – overtime and bonus and incentive payments
- Open public meetings – compliance with minutes, meetings and executive session requirements
- Financial condition – reviewing for indications of financial distress

SCHEDULE OF AUDIT FINDINGS AND RESPONSES

Olympic Medical Center January 1, 2022 through December 31, 2022

2022-001 The District's financial condition is declining, which places it at risk of not being able to meet obligations as they become due.

Background

An elected seven-member Board of Commissioners governs the District, which provides health care services to people in Port Angeles, Sequim and surrounding communities. The Board appoints an administrator to oversee the District's daily operations and about 1,700 employees. The District reported operating revenues and operating expenditures of \$244 million and \$262 million, respectively, in fiscal year 2022.

Description of Condition

The District reported an operating loss of \$17.7 million in fiscal year 2022, and reported a year-to-date loss of \$25 million as of November 2023.

Due to declining financial health, we calculated the District's available cash on hand based on its unrestricted cash and investments. We determined the District only had available cash to sustain operating expenditures of:

- 59 days at fiscal year-end 2021
- 32 days at fiscal year-end 2022
- 12 days as of November 30, 2023

Further, the District did not comply with the minimum debt ratio requirements of its 2018 general obligation bonds. For fiscal year-end December 31, 2022, the District's debt ratio was 0.16, which did not meet the minimum debt ratio of 1.25. The District also failed to maintain the required ratio in subsequent fiscal quarters, as specified in the related bond covenants. These bonds represent about \$17 million of the District's \$48.6 million outstanding bond debt. While the lender has not currently exercised its rights to remedy the default, it retains these rights and could do so at any time. In addition, the District was unable to pay off its 2013 bond and extended its terms for three additional years, which resulted in a 3 percent higher interest rate.

Lastly, the District has outstanding lawsuits that could potentially negatively affect its financial condition even further.

Cause of Condition

The District has limited means to increase revenue and is experiencing a decrease in commercial and private payer insurance revenue, which historically has helped cover the gap in Medicare and Medicaid payments. In addition, the District's payroll expenditures have continued to increase, representing 60 percent of its total operating expenditures in fiscal year 2022. Based on the District's budget, these expenditures are expected to increase to more than 65 percent at fiscal year-end 2023.

Effect of Condition

The District's financial condition puts it at risk of not being able to meet obligations as they become due. It is also at risk of paying a higher interest rate on bonds, or having to repay bonds on short notice, due to noncompliance with covenants.

Recommendation

The District's Board and management are aware of its declining financial condition, and they are taking steps to make improvements. However, we recommend the District establish a formal, written comprehensive plan to address its financial condition, as well as continue to evaluate and closely monitor financial operations to ensure it can meet its financial obligations.

District's Response

The Hospital District has engaged an operations partner that will provide information and process improvement in reducing operating cost and increasing revenue opportunities. The Safety Net Assessment Program (SNAP) is expected to provide \$10M in the certified public expenditures program. The Hospital District is dedicated to addressing the issue and continues to work on solutions to improve the position.

Auditor's Remarks

We appreciate the District's commitment to resolving this finding. We will review the status of the District's corrective action during our next audit.

Applicable Laws and Regulations

RCW 43.09.200, Local government accounting—Uniform system of accounting.

The *Budgeting, Accounting and Reporting System* (BARS Manual), Chapter 3, Accounting Principles and Internal Control

RELATED REPORTS

Financial

A financial statement audit was performed by a firm of certified public accountants. That firm's report on fiscal year 2022 is available from the Olympic Medical Center.

Federal grant programs

The firm has not yet completed the federal single audit for fiscal year 2022.

INFORMATION ABOUT THE DISTRICT

Public Hospital District No. 2 of Clallam County, doing business as Olympic Medical Center, provides health care services to Port Angeles, Sequim and surrounding communities. The District operates Olympic Memorial Hospital, a 126 bed licensed general acute-care facility, and home health services through Olympic Medical Home Health. The District also operates Olympic Medical Imaging Center, Olympic Medical Cancer Center, Olympic Medical Physical Therapy and Rehabilitation, Olympic Medical Laboratory, Olympic Medical Surgical Services, Olympic Medical Cardiac Services and Olympic Medical Physicians, which provides physician clinic services in 13 different specialties across the District.

An elected, seven-member Board of Commissioners governs the District. The Board appoints an Administrator to oversee the District's daily operations as well as its 1,757 employees. The District operated on an annual budget of approximately \$256 million for 2022.

Contact information related to this report

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Information current as of report publish date.

Audit history

You can find current and past audit reports for the Olympic Medical Center at <http://portal.sao.wa.gov/ReportSearch>.

ABOUT THE STATE AUDITOR'S OFFICE

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

We work with state agencies, local governments and the public to achieve our vision of increasing trust in government by helping governments work better and deliver higher value.

In fulfilling our mission to provide citizens with independent and transparent examinations of how state and local governments use public funds, we hold ourselves to those same standards by continually improving our audit quality and operational efficiency, and by developing highly engaged and committed employees.

As an agency, the State Auditor's Office has the independence necessary to objectively perform audits, attestation engagements and investigations. Our work is designed to comply with professional standards as well as to satisfy the requirements of federal, state and local laws. The Office also has an extensive quality control program and undergoes regular external peer review to ensure our work meets the highest possible standards of accuracy, objectivity and clarity.

Our audits look at financial information and compliance with federal, state and local laws for all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits and cybersecurity audits of state agencies and local governments, as well as state whistleblower, fraud and citizen hotline investigations.

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