SAN FRANCISCO HEALTH SERVICE SYSTEM
OTHER EMPLOYEE BENEFIT TRUST FUND

Financial Statements

June 30, 2019 and 2018

(With Independent Auditors' Report Thereon)

SAN FRANCISCO HEALTH SERVICE SYSTEM
OTHER EMPLOYEE BENEFIT TRUST FUND

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KPMG LLP
Suite 1400
55 Second Street
San Francisco, CA 94105

Independent Auditors' Report

Members of the Health Service Board,
The Honorable Mayor and Board of Supervisors
City and County of San Francisco

Report on the Financial Statements

We have audited the accompanying financial statements of the San Francisco Health Service System Other Employee Benefit Trust Fund (the Trust) (also referred to as the Health Service System Trust Fund), managed by Health Service System (the System), a department of the City and County of San Francisco, California (the City), as of and for the year ended June 30, 2019 and 2018, and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the San Francisco Health Service System Other Employee Benefit Trust Fund, managed by Health Service System, a department of the City, as of June 30, 2019 and 2018, and the changes in financial position thereof for the years then ended in accordance with U.S. generally accepted accounting principles.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Trust and do not purport to, and do not, present fairly the financial position of the City, as of June 30, 2019 and 2018, the changes in its financial position, or, where applicable, its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplementary Information

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3–10 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.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2019, on our consideration of the Trust's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Trust's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Trust's internal control over financial reporting and compliance.

KPMG LLP

San Francisco, California
December 20, 2019

SAN FRANCISCO HEALTH SERVICE SYSTEM
OTHER EMPLOYEE BENEFIT TRUST FUND

Management's Discussion and Analysis

June 30, 2019 and 2018

The management of the San Francisco Health Service System (the System), a department of the City and County of San Francisco (the City), is pleased to provide this overview and analysis of the financial performance as of and for the fiscal years ended June 30, 2019 and 2018. We encourage readers to consider the information presented below in conjunction with the financial statements and notes, which follow.

The System is a department of the City that is reflected as an Other Employee Benefit Trust Fund (the Trust) (also referred to as the San Francisco Health Service System Trust Fund), in the City's Comprehensive Annual Financial Report (CAFR). The Trust is distinguished from the Retiree Health Care Trust Fund in that it pays for the employee and retiree current benefits.

The System is the primary purchaser and administrator of health, dental, and other non-retirement/pension benefits for employees and retirees (and their respective eligible dependents) of the City, the San Francisco Unified School District, the San Francisco Community College District, and the San Francisco Superior Court. The members covered by the System increased 2% from 69,676 as of June 30, 2018 to 70,738 as of June 30, 2019, The System is governed by the Health Service Board (HSB) as described in note 1 to the financial statements.

Medical benefits during the fiscal years are provided to members of the System through six plan choices:

- United Healthcare (Preferred Provider Organization [PPO]) (UHC PPO)
- United Healthcare Medicare Advantage Prescription Drug (UHC MAPD) (fully insured PPO)
- Kaiser Permanente Foundation Health Plan (fully insured Health Maintenance Organization [HMO])
- Kaiser Permanente Senior Advantage Plan (fully insured HMO)
- Blue Shield of California Access+ HMO Plan (flex-funded plan with fully insured, capitated, and self-insured components)
- Blue Shield of California Trio HMO Plan (flex-funded plan with fully insured capitated component for professional services provided in the physician office, and self-insured components including claims).

Each of the above plan choices includes a vision benefit provided through Vision Service Plan (VSP). There is also a fully employee paid Premium Vision Plan.

The UHC PPO (also known as City Health Plan), which includes medical and prescription drug benefits, is a self-insured indemnity plan for active and early retired members and their dependents where the risk of loss due to claims in excess of revenues is borne by the Trust. The UHC MAPD also includes medical and prescription drug benefits and is a fully insured PPO plan for Medicare eligible members and their dependents.

The Kaiser Permanente HMO plan, for active and early retired members and their dependents, is a traditional, fully insured, external HMO, where the risk of loss due to excess claims for a given fiscal year is borne by the

HMO. The Kaiser Permanente Senior Advantage HMO plan is a fully insured plan for Medicare eligible members and their dependents.

The Blue Shield of California Access+ HMO and Trio HMO Plans are flex-funded. The flex-funded plan has a fully insured, capitated component for professional services provided in physician offices. Hospital and pharmacy services are self-insured, where the risk of loss due to claims in excess of revenues is borne by the Trust. Effective January 1, 2018, Blue Shield of California began offering two plan choices. In addition to the broad Blue Shield network of doctors, members of the System can select a narrow network of doctors and hospitals at a lower premium.

Dental benefits during the fiscal years are provided through three plan choices:

- Delta Dental (PPO)
- Delta Care (PMI, DHMO)
- United Healthcare Dental (formerly known as Pacific Union) (DMO).

The Delta Dental plan provided to active employees is a self-insured indemnity plan, administered by Delta Dental. Similar to the City Health Plan, however, the risk of loss due to claims in excess of revenues is borne by the City and any other participating employers. The Delta Dental plan offered to retired employees is a fully insured plan, where the risk of loss for a given fiscal year is borne by Delta Dental. The Delta Care (PMI, DHMO) dental plan and United Healthcare Dental plan are managed care dental plans and are fully insured with respect to both active and retired employees.

Overview of Financial Statements

The following discussion is intended to serve as an introduction to the Trust's financial statements, which consist of the statements of net position available for health benefits, the statements of changes in net position available for health benefits, and notes to financial statements:

- The statements of net position available for health benefits are a snapshot of account balances as of June 30, 2019 and 2018. These statements show assets, liabilities, and net position available for health benefits as of those dates.
- The statements of changes in net position available for health benefits show additions and deductions to the Trust's net position during the plan years ended June 30, 2019 and 2018.
- Notes to financial statements provide additional information that is essential to a full understanding of the numbers in the financial statements.

The financial statements and accompanying notes are presented in all material respects in accordance with the basis of accounting and accounting principles, as explained in note 2 to the financial statements. The Trust presents financial statements reflecting full accrual basis accounting.

Financial Analysis – Condensed Schedule of Net Position Available for Health Benefits

As of June 30, 2019, there was $92.2 million of net position available to meet future health care obligations. This compares to $77.4 million as of June 30, 2018 and $72.5 million as of June 30, 2017.

	2019	2018	2017	Dollar change (19 – 18)	Percent change (19 – 18)	Dollar change (18 – 17)	Percent change (18 – 17)
Total assets	$ 130,430,734	113,085,812	103,250,862	17,344,922	15%	$ 9,834,950	10%
Total liabilities	38,272,203	35,636,989	30,724,781	2,635,214	7%	4,912,208	16%
Net position	$ 92,158,531	77,448,823	72,526,081	14,709,708	19%	$ 4,922,742	7%

Fiscal Year 2019

The net position available for health benefits increased by $14.7 million in 2019. The components of the increases are:

- $3.6 million decrease in the City Health Plan net position was primarily due to use of claim stabilization reserve funding, per HSB approved policy.
- $12.6 million increase in the Blue Shield flex-funded plan net position was due to excess premium equivalents over claim costs of $2.2 million, pharmacy rebates of $7.0 million, and use of claim stabilization funding, per HSB approved policy, of $3.4 million.
- $1.2 million increase in the dental plans net position was due to excess premium equivalents over claim costs of $4.9 million offset by claim stabilization, per HSB approved policy, of $3.7 million.
- $0.8 million increase in Kaiser plan net position was based on pay calendars for the San Francisco Unified School District, and the San Francisco Community College District; contractual provisions governing the timing of premium payments; and members moving from active to retiree and from non-Medicare to Medicare status.
- $0.6 million increase in administrative savings.
- $0.3 million decrease in flexible spending account employee contributions over claim reimbursements to participants.
- $3.4 million increase in Trust Fund interest income, other investment earnings, performance guarantee penalties, and forfeitures.

Fiscal Year 2018

The net position available for health benefits increased by $4.9 million in 2018. The components of the increases are:

- $6.1 million decrease in the City Health Plan net position was due to use of claim stabilization reserve funding, per HSB approved policy.

(Continued)

- $5.6 million increase in the Blue Shield flex-funded plan net position was due to excess premium equivalents over claim costs of $1.2 million, and use of claim stabilization funding, per HSB approved policy, of $4.4 million.

- $2.7 million increase in the dental plans net position was due to excess premium equivalents over claim costs of $5.5 million offset by claim stabilization, per HSB approved policy, of $2.8 million.

- $0.9 million increase in Kaiser plan net position was based on contract premium arrangements for new enrollees, termed members, members eligible for Medicare, and members with changing contribution schedule.

- $0.8 million increase in administrative savings.

- $0.2 million increase in flexible spending account employee contributions over claim reimbursements to participants.

- $0.8 million increase in Trust Fund interest income, performance guarantee penalties, and forfeitures.

Fiscal Year 2019

- Cash and investments held with the City Treasurer as of June 30, 2019 totaled $102.3 million compared to $87.0 million as of June 30, 2018, an increase of 17.6 percent. The cash and investment balance fluctuate throughout the year depending on collections, claims, and timing of vendor payments. In addition, pursuant to the HSB Self-Insured Stabilization policy, $6.8 million was used to reduce 2018 and 2019 rates as described in note 7(b).

- Contributions receivable from employer increased from $19.0 million as of June 30, 2018 to $20.3 million as of June 30, 2019, a 6.8 percent increase. Contributions receivable from employees decreased from $4.3 million, as of June 30, 2018 to $4.2 million as of June 30, 2019, a 4.2 percent decrease. These changes are due to the timing of health premium collections from both the employer and the employee.

- Prepaid and other assets increased from $2.5 million as of June 30, 2018 to $3.1 million as of June 30, 2019, a 23.2 percent increase. In 2019, prepaid and other assets included $0.5 million in prepayments to the health care providers for July 2019 health coverage, and $2.6 million in pharmacy rebates. (In 2019, the performance guarantees are reflected as cash since they were received during the fiscal year). In 2018, prepaid and other assets included $0.5 million in prepayments to the health care providers for July 2018 health coverage, $1.9 million in pharmacy rebates and $0.1 million in performance guarantees as described in note 1 and 4 to the financial statements.

- Reserves for claims under the City Health Plan, Blue Shield flex-funded plan, and Delta Dental were $27.9 million as of June 30, 2019 and $27.8 million as of June 30, 2018. The reserve is actuarially determined.

- Premiums payable to HMO, dental, and disability plans increased by 49.5 percent, from $4.9 million as of June 30, 2018 to $7.3 million as of June 30, 2019. The increase was due to the timing of payments to health care providers for payments after the end of the fiscal year for the prior fiscal year.

- Unearned contributions represent health contributions received in advance of the period of benefit coverage. Unearned contributions increased from $2.9 million as of June 30, 2018 to $3.1 million as of June 30, 2019, or a 5.1 percent increase. The increase was due to the timing and processing of deductions for a pay period pertaining to July 2019 benefit coverage.

Fiscal Year 2018

- Cash and investments held with the City Treasurer as of June 30, 2018 totaled $87.0 million compared to $36.8 million as of June 30, 2017, an increase of 136.6 percent. The cash and investment balance fluctuate throughout the year depending on collections, claims, and timing of vendor payments. The monthly cash balance ranged between $36.8 million and $87.0 million during the year ended June 30, 2018. In addition, pursuant to the HSB Self-Insured Stabilization policy, $8.9 million was used to reduce 2017 and 2018 rates as described in note 7(b).

- Contributions receivable from employer increased from $17.6 million as of June 30, 2017 to $19.0 million as of June 30, 2018, a 7.7 percent increase. Contributions receivable from employees increased from $3.4 million as of June 30, 2017 to $4.3 million as of June 30, 2018, a 28.4 percent increase. These increases are due to the timing of health premium collections.

- Prepaid and other assets decreased from $45.4 million as of June 30, 2017 to $2.5 million as of June 30, 2018, a 94.5 percent decrease. In 2018, prepaid and other assets included $0.5 million in prepayments to the health care providers for July 2018 health coverage, $1.9 million in pharmacy rebates and $0.1 million in performance guarantees. In 2017, prepaid and other assets included $41.5 million in prepayments made to the health care providers for July 2017 health coverage, $2.5 million from Blue Shield for a one time refund of the Health Insurance Tax, $1.3 million in pharmacy rebates, and $0.1 million in performance guarantees as described in notes 1 and 4 to the financial statements.

- Reserves for claims under the City Health Plan, Blue Shield flex-funded plan, and Delta Dental were $27.8 million as of June 30, 2019 and 2018. The reserve is actuarially determined.

- Premiums payable to HMO, dental, and disability plans increased by 1,451.3 percent, from $0.3 million as of June 30, 2017 to $4.9 million as of June 30, 2018. The increase was due to the timing of payments to health care providers.

- Unearned contributions represent health contributions received in advance of the period of benefit coverage. Unearned contributions increased from $2.7 million as of June 30, 2017 to $2.9 million as of June 30, 2018, or a 10.7 percent increase. The increase was due to the timing and processing of deductions for a pay period pertaining to July 2018 benefit coverage.

Financial Analysis – Condensed Financial Information

For the year ended June 30, 2019, there was a $14.7 million increase in net position during the year. This compares to a $4.9 million increase and $3.9 million increase in net position for the years ended June 30, 2018 and 2017, respectively. The highlights regarding the changes in net position are as follows:

	2019	2018	2017	Dollar change (19-18)	Percent change (19-18)	Dollar change (18-17)	Percent change (18-17)
Additions:							
Employee and retiree contributions	$ 153,689,075	143,907,158	132,331,766	9,781,917	6.8 %	$ 11,575,392	8.7 %
Employer contributions	789,836,207	758,782,536	713,909,471	31,053,671	4.1 %	44,873,065	6.3 %
Total contributions	943,525,282	902,689,694	846,241,237	40,835,588	4.5 %	56,448,457	6.7 %
Plan provider penalties and forfeitures	510,701	107,541	711,440	403,160	374.9 %	(603,899)	(84.9)%
Total additions	944,035,983	902,797,235	846,952,677	41,238,748	4.6 %	55,844,558	6.6 %
Deductions:							
City Health Plan health benefits	108,978,325	100,978,374	75,024,440	7,999,951	7.9 %	25,953,934	34.6 %
Health maintenance organization health benefits	729,838,369	709,437,783	686,775,756	20,400,586	2.9 %	22,662,027	3.3 %
Vision plan health benefits	7,563,412	6,123,424	5,070,479	1,439,988	23.5 %	1,052,945	20.8 %
Dental benefits	62,568,494	61,231,760	58,524,013	1,336,734	2.2 %	2,707,747	4.6 %
Disability and flexible benefits	23,296,035	20,819,844	18,080,479	2,476,191	11.9 %	2,739,365	15.2 %
Total deductions	932,244,635	898,591,185	843,475,167	33,653,450	3.7 %	55,116,018	6.5 %
Change in net position before investment earnings	11,791,348	4,206,050	3,477,510	7,585,298	180.3 %	728,540	21.0 %
Investment earnings	2,918,360	716,692	445,373	2,201,668	307.2 %	271,319	60.9 %
Change in net position	$ 14,709,708	4,922,742	3,922,883	9,786,966	198.8 %	$ 999,859	25.5 %

Fiscal Year 2019

- Employees and retiree contributions totaled $153.7 million during the year ended June 30, 2019, compared to $143.9 million for the prior year, an increase of 6.8 percent primarily due to increases in premiums. Active employees contributed $103.1 million and retirees contributed $50.6 million of the $153.7 million collected in fiscal year 2019. The number of covered lives increased 1.2 percent from the 2018 levels. Of the total contributions, $116.4 million are for medical and vision coverage, $20.3 million for dental coverage, and $17.0 million for flexible spending accounts.

- Employer contributions on behalf of active employees increased from $541.2 million during the year ended June 30, 2018 to $563.6 million during the year ended June 30, 2019, an increase of 4.1 percent over the prior year. The primary factors causing the $22.4 million increase was an increase in rates and membership.

- Employer contributions on behalf of retirees increased from $217.6 million for the year ended June 30, 2018 to $226.3 million for the year ended June 30, 2019, or 4.0 percent due to increases in premiums. The cost of the plan benefits, retiree's number of dependents, and Medicare status of the retiree and dependents determines the premium for retirees. The 10-County Average Survey is used to calculate the retiree rates.

(Continued)

- Health benefits for UHC PPO (City Health Plan), which cover medical and prescription drug expenses, increased from $101.0 million for the year ended June 30, 2018, to $109.0 million for the year ended June 30, 2019, or 7.9 percent. The increase was due to an increase in rates and membership in the City Health Plan.

- HMO expenditures increased from $709.4 million for the year ended June 30, 2018, to $729.8 million for the year ended June 30, 2019, or 2.9 percent, due primarily to increases in contract rates, medical and pharmacy claims, and increases in membership.

- Vision plan health benefits totaled $7.6 million for the year ended June 30, 2019 compared to $6.1 million for the year ended June 30, 2018, for an increase of $1.4 million or 23.5 percent. The increase is due to an increase in membership with an introduction of Vision Premier Plan effective January 2018.

- Dental benefits totaled $62.6 million for the year ended June 30, 2019 compared to $61.2 million for the year ended June 30, 2018, for an increase of $1.3 million or 2.2 percent, due to an increase in membership.

- Disability and flexible benefits totaled $23.3 million for the year ended June 30, 2019 compared to $20.8 million for the year ended June 30, 2018, for an increase of 11.9 percent, due to an expansion of benefit offerings and subsequent membership.

- Investment earnings totaled $2.9 million for the year ended June 30, 2019 compared to $0.7 million for the year ended June 30, 2018, for an increase of $2.2 million or 307.2 percent, due to an increase in interest income and fair value of investments. Per Governmental Accounting Standards Board (GASB) Statement No. 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, financial statements must contain the fair market value of the investments as if they were liquidated on June 30.

Fiscal Year 2018

- Employees and retiree contributions totaled $143.9 million during the year ended June 30, 2018, compared to $132.3 million for the prior year, an increase of 8.7 percent, primarily due to increases in premiums. Active employees contributed $95.6 million and retirees contributed $48.3 million of the $143.9 million collected in fiscal year 2018. The number of covered lives increased 2 percent from the 2017 levels. Of the total contributions, $110.9 million are for medical and vision coverage, $19.2 million for dental coverage, and $13.8 million for flexible spending accounts.

- Employer contributions on behalf of active employees increased from $512.4 million during the year ended June 30, 2017 to $541.2 million during the year ended June 30, 2018, an increase of 5.6 percent over the prior year. The primary factors causing the $28.7 million increase was an increase in rates and membership.

- Employer contributions on behalf of retirees increased from $201.5 million for the year ended June 30, 2017, to $217.6 million for the year ended June 30, 2018, or 8.0 percent, due to increases in premiums. The cost of the plan benefits, retiree's number of dependents, and Medicare status of the retiree, and

dependents determines the premium for retirees. The 10-County Average Survey is used to calculate the retiree rates.

- UHC PPO (City Health Plan) health benefits, which covers medical and prescription drug expenses, increased from $75.0 million for the year ended June 30, 2017, to $101.0 million for the year ended June 30, 2018, or 34.6 percent. The increase was due to closing the Blue Shield of California plan for Medicare retirees which resulted in an increase in membership in the City Health Plan.

- The total expenditures for HMO increased from $686.8 million for the year ended June 30, 2017 to $709.4 million for the year ended June 30, 2018, or 3.3 percent, due primarily to increases in contract rates, medical and pharmacy claims, and increases in membership.

- Vision plan health benefits totaled $6.1 million for the year ended June 30, 2018 compared to $5.1 million for the year ended June 30, 2017, for an increase of $1.1 million or 20.8 percent. The increase is due to an increase in membership with an introduction of Vision Premier Plan effective January 2018.

- Dental benefits totaled $61.2 million for the year ended June 30, 2018 compared to $58.5 million for the year ended June 30, 2017, for an increase of $2.7 million or 4.6 percent, due to an increase in contract rates and membership.

- Disability and flexible benefits totaled $20.8 million for the year ended June 30, 2018 compared to $18.1 million for the year ended June 30, 2017, for an increase of 15.2 percent, due to an expansion of benefit offerings and subsequent membership.

- Investment earnings totaled $0.7 million for the year ended June 30, 2018 compared to $0.5 million for the year ended June 30, 2017, for an increase of $0.2 million or 60.9 percent, due to an increase in interest income. Per GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, financial statements must contain the fair market value of the investments as if they were liquidated on June 30.

There are no known facts, decisions, or conditions that are expected to have a significant effect on net position available for health benefits, or results of revenues, expenses, and other changes in the net position.

Request for Information

This report is designed to provide a general overview of the System's finances for the years ended June 30, 2019 and 2018. Questions regarding any of the information provided in this report or requests for additional information should be addressed to:

San Francisco Health Service System
City and County of San Francisco
Pamela Levin, Chief Financial Officer
1145 Market Street, Suite 300
San Francisco, CA 94103-1523

SAN FRANCISCO HEALTH SERVICE SYSTEM
OTHER EMPLOYEE BENEFIT TRUST FUND

Statements of Net Position Available for Health Benefits

June 30, 2019 and 2018

	2019	2018
Assets:		
Cash and investments held with City and County Treasurer	$ 102,303,863	$ 86,994,405
Contributions receivable from:		
Employer	20,258,176	18,973,554
Employees	4,153,646	4,334,167
Interest receivable	649,246	295,784
Prepaid and other assets:		
Prepayments to health plans	—	33,110
Other assets	3,065,803	2,454,792
Total prepaid and other assets	3,065,803	2,487,902
Total assets	130,430,734	113,085,812
Liabilities:		
Reserves for claims – medical, prescription drugs and dental	27,899,063	27,824,832
Health Maintenance Organization, dental, and disability premiums payable	7,280,981	4,871,229
Unearned contributions	3,092,159	2,940,928
Total liabilities	38,272,203	35,636,989
Total net position	$ 92,158,531	$ 77,448,823

See accompanying notes to financial statements.

SAN FRANCISCO HEALTH SERVICE SYSTEM
OTHER EMPLOYEE BENEFIT TRUST FUND

Statements of Changes in Net Position Available for Health Benefits

Years ended June 30, 2019 and 2018

	2019	2018
Additions:		
Employee and retiree contributions	$ 153,689,075	$ 143,907,158
Employer contributions for:		
Active employees	563,558,237	541,163,186
Retired employees	226,277,970	217,619,350
Total contributions	943,525,282	902,689,694
Plan providers penalties and forfeitures	510,701	107,541
Investment earnings:		
Net change in fair value of investments	887,475	(474,067)
Interest income	2,030,885	1,190,759
Total investment earnings	2,918,360	716,692
Total additions	946,954,343	903,513,927
Deductions:		
City Health Plan health benefits	108,978,325	100,978,374
Health Maintenance Organization health benefits	729,838,369	709,437,783
Vision benefits	7,563,412	6,123,424
Dental benefits	62,568,494	61,231,760
Disability and flexible benefits	23,296,035	20,819,844
Total deductions	932,244,635	898,591,185
Change in net position available for health benefits	14,709,708	4,922,742
Net position:		
Beginning of year	77,448,823	72,526,081
End of year	$ 92,158,531	$ 77,448,823

See accompanying notes to financial statements.

(1) Description of San Francisco Health Service System

(a) General

The City and County of San Francisco (the City) established the San Francisco Health Service System (the System) in March 1937, by amendment of the City Charter. A new City Charter was adopted on November 7, 1995 and became effective July 1, 1996. The City provides health care benefits to eligible active and retired employees and their dependents through the System. The System also provides health care benefits to active and retired employees and their dependents of the San Francisco Unified School District, the San Francisco Community College District, and the San Francisco Superior Court. Under Charter Section A8.422, the Health Service Board is responsible for adopting a plan or plans for providing medical care to members of the System.

The System is reflected as an Other Employee Benefit Trust Fund (the Trust) (also referred to as the Health Service System Trust Fund) and is an integral part of the City, and the accompanying financial statements are included as part of the primary government in the Comprehensive Annual Financial Report (CAFR) prepared by the City. The financial statements present only the Trust and do not purport to, and do not, present fairly the financial position of the City as of June 30, 2019 and 2018, and the changes in its financial position for the years then ended, in accordance with U.S. generally accepted accounting principles. The System, a City department, is overseen by the Health Service Board (HSB). The HSB voted, on April 3, 2017, to continue to have the Trust's cash balances deposited with, and managed by, the Office of the Treasurer and Tax Collector.

The overarching principles in setting the rates and benefits are to provide quality health care, contain costs, and stabilize insurance premiums for the members and the employer. The HSB must consider the increased cost resulting from the Patient Protection and Affordable Care Act (ACA) in determining the plan designs and premiums.

The composition of the seven-member HSB includes a seated member of the San Francisco Board of Supervisors (the Board), appointed by the Board President; an individual who regularly consults in the health care field, appointed by the Mayor; a doctor of medicine, appointed by the Mayor; a member nominated by the Controller and approved by the HSB; and three members of the System, active or retired, elected from among their members. The HSB is responsible for appointing a full-time administrator, who serves at the pleasure of the HSB and sets the policy for and oversees the administration of the System.

Under Charter Section A8.423, the City's contribution towards the System's medical plans is determined by the results of an annual survey of the amount of premium contributions provided by the 10 most populous counties in California (other than the City). The survey is commonly called the 10-County Average Survey and used to determine "the average contribution made by each such county toward the providing of health care plans, exclusive of dental care, for each employee of such county." Under Charter Section A8.423, the City is required to contribute to the Health Service System Trust Fund an amount equal to the "average contribution" for each City Beneficiary.

In the June 2014 collective bargaining for the 2015 Plan Year, the impact of the "average contribution" on rates was eliminated in the calculation of premiums for almost all active employees represented by most unions, in exchange for a percentage-based employee premium contribution model. It is

anticipated that the long-term impact of the premium contribution model will be the reduction in the relative proportion of the projected increases in the City's contributions for healthcare, stabilization of the medical plan membership and maintenance of competition among plans. The contribution amounts are paid by the City into the Trust. The 10-County Average Survey is used as a basis for calculating all City retiree premiums and premiums for the San Francisco Superior Court, San Francisco Unified School District, and San Francisco Community College District.

Membership in the System is available to (i) all active permanent employees, as well as eligible retired employees, of the City, and of the San Francisco Unified School District, San Francisco Community College District, and the San Francisco Superior Court; (ii) temporary employees who meet eligibility requirements; (iii) eligible dependents of members; and (iv) certain dependents of deceased and retired employees. Eligibility terminates when a member leaves employment for reasons other than retirement. The System is responsible for designing health care benefits, selecting and managing plan providers, and determining some aspects of benefit eligibility to supplement the eligibility rules contained in the Charter and applicable ordinances. In addition, the System is responsible for administration of health care benefits, including maintaining employee membership and financial accounting records.

Pursuant to provisions of the ACA, the System implemented, effective January 2015, the employer mandate that requires that "large employers" (i.e., employers with 50 or more full-time employees or full-time equivalents) offer affordable coverage that provides minimum value to all full-time employees and their dependents. ACA defined a full-time employee as one who works on average 30 hours a week. However, a threshold of 20 hours or more over a 12-month period was implemented.

Pursuant to the Charter, most administrative costs of the System are paid for by the City, the Unified School District, and the Community College District and are reflected in the respective financial statements of those entities. Certain expenses related to the typical annual open membership and member marketing and communications are, however, paid from the Trust pursuant to Section A8.423 of the Charter. In addition, third-party claims administration costs for the self-funded plans (City Health Plan and Delta Dental for active employees) and flex-funded plan (Blue Shield of California for active employees and early retirees) are included in the respective premium rates for those plans.

Pursuant to provisions of the ACA, two direct fees (Patient Centered Research Institute Fee and the Transitional Reinsurance Fee) and one Health Insurance Tax (HIT) were put in place beginning in fiscal year 2014. The HIT impacts the fully insured medical, vision, and dental plans offered by the System and is reflected in the premiums. The HIT was in effect in the 2016 calendar year and was reflected in the 2017 financial statements. In 2015, Congress approved a one-year moratorium on collecting the HIT for the 2017 calendar year. The HIT was reinstated for the 2018 calendar year.

When the rates were approved by the HSB for the 2016 calendar year, it was assumed that the HIT would be applicable for the Blue Shield Flex Plan due to the California Department of Managed Health (DMHC) filing as a fully insured plan. Blue Shield of California and the DMHC revisited the definition and as a result flex-funded plans are not being treated as fully insured by Blue Shield and DMHC and therefore were not required to be paid for the 2016 calendar year. The decision resulted in a one-time refund which is reflected in the 2017 net position. Furthermore, the HIT will not be collected on the flex-funded plan going forward and thus will not be included in future premium rate calculations. The HSB

has also considered the impact of the 2022 Excise Tax on High Cost Health Plans (Cadillac Tax) in the benefit design for the 2018 and 2019 calendar years.

(b) Types of Benefits and Premium Rates

Medical benefits during the fiscal years are provided to members of the System through six plan choices:

- United Healthcare (Preferred Provider Organization [PPO]) (UHC PPO) (aka City Plan)
- United Healthcare Medicare Advantage Prescription Drug (UHC MAPD) (fully insured PPO)
- Kaiser Permanente Foundation Health Plan (fully insured Health Maintenance Organization [HMO])
- Kaiser Permanente Senior Advantage Plan (fully insured HMO)
- Blue Shield of California Access+ Plan (flex-funded plan with fully insured, capitated, and self-insured components)
- Blue Shield of California Trio Plan (flex-funded plan with fully insured, capitated, and self-insured components).

Each of the above plan choices includes a vision benefit provided through Vision Service Plan (VSP).

The City Health Plan, which includes medical and prescription drug benefits, is a self-insured indemnity plan, where the risk of loss due to claims in excess of revenues is borne by the System Trust. The City Health Plan is administered by UHC. UHC offers a fully insured Medicare Advantage PPO for retirees with Medicare.

The Kaiser HMO is a fully insured external HMO, where the risk of loss due to excess claims for a given fiscal year is borne by the HMO.

On January 1, 2013, the Blue Shield of California Plan was converted from a fully insured external HMO plan to a flex-funded plan. The flex-funded plan has a fully insured, capitated component for professional services provided in physician offices. Hospital and pharmacy services are self-insured, where the risk of loss due to claims in excess of revenues is borne by the Trust. In 2017, Medicare coverage offered through Blue Shield of California was eliminated as an option to System members.

Effective January 1, 2018, Blue Shield of California began offering two plan choices. In addition to the broad Blue Shield network of doctors, members of the System can select a narrow network of doctors and hospitals at a lower premium.

Dental benefits during the fiscal years are provided through three plan choices:

- Delta Dental (PPO)
- Delta Care (PMI) (DMO)

- United Healthcare Dental (formerly known as Pacific Union) (DMO).

The Delta Dental plan provided to active employees is a self-insured indemnity plan, administered by Delta Dental and the risk of loss due to claims in excess of revenues is borne by the City and any other participating employers. The Delta Dental plan offered to retired employees is a fully insured plan, where the risk of loss for a given fiscal year is borne by Delta Dental. The Delta Care (PMI) and United Healthcare Dental (DMO) dental plans are managed care dental plans and are fully insured with respect to both active and retired employees.

Premium rates for the fully insured plans are set through periodic competitive solicitation of carriers and an annual negotiation process that includes participation of the System's independent actuary and consultants. Premium rates for the self-insured plans are set based on recommendations and certification of such actuaries and consultants.

The System offers two types of flexible spending accounts for all City employees: a health care reimbursement account and a dependent care reimbursement account. Most of the administration for these accounts is provided through a third-party administrator, whose fees are provided by the City through the System. The administrator was P & A Group in fiscal years 2019 and 2018.

The System utilizes a third-party administrator to provide most of the administration for a cafeteria plan offered to employees represented by the Municipal Executives Association, elected officials, and certain unrepresented employees. The fees of this administrator are provided by the City through the System. The current administrator is WORKTERRA.

In addition, the City provides a long-term disability plan to most of its employees. All costs of the long-term disability plan are paid by contributions from the City. The current plan provider is Aetna Life and Casualty.

The City also provides employer-paid group term life insurance to most employee groups. Voluntary accidental death and personal loss insurance is offered to most employee groups paid by the members. In fiscal year 2018 and 2019 the plan provider was Aetna Life and Casualty.

In 2017, the City offered a new adoption and surrogacy assistance plan paid for by the Trust. In addition, in fiscal year 2018 and 2019, expert medical case review services, provided by Best Doctors, is paid by members and the City through the Trust.

(c) Determination of Employer and Member Contributions

The overall cost of benefits is determined using ongoing periodic member eligibility data and the premium rates referred to above. The costs are allocated among members, the City, the San Francisco Unified School District, the San Francisco Community College District, and the San Francisco Superior Court as set forth below. Member premiums are received at the time of the benefit period.

The medical and dental plans and costs are determined annually by the HSB and approved by the San Francisco Board of Supervisors. Member contribution rates vary depending on the number of dependents, the cost of the plans selected by the member, and differing employer contribution levels depending on the employee's status as an active employee or a retiree and the application of employer

subsidies tied to collective bargaining agreements for active employees or Medicare eligibility for retirees. Member contributions do not accumulate or vest.

Employer contributions for health benefits are determined annually in accordance with Charter requirements and the applicable collective bargaining agreements with various employee organizations. The Charter-based contributions are determined using a formula based on surveying similar contributions made by the 10 most populous counties in California, not including San Francisco. In addition, most active employee groups have collectively bargained for enhanced contributions for single coverage as well as employer subsidized dependent health coverage, some in exchange for the 10-County Average. The 10-County Average is used as a basis for calculating all retiree premiums and premiums for the San Francisco Superior Court, San Francisco Unified School District, and San Francisco Community College District.

Pursuant to Charter section A8.428b(3), for retired employees hired on or before January 9, 2009, employers shall contribute to the health service fund, amounts subject to the following limitations: Monthly contributions required from Retired Persons and the surviving spouses and surviving domestic partners of active employees and Retired Persons participating in the system shall be equal to the monthly contributions required from members in the system for health coverage excluding health coverage or subsidies for health coverage paid for active employees as a result of collective bargaining, with the following modifications:

(i) the total contributions required from Retired Persons who are also covered under Medicare shall be reduced by an amount equal to the amount contributed monthly by such persons to Medicare;

(ii) because the monthly cost of health coverage for Retired Persons may be higher than the monthly cost of health coverage for active employees, the City and County, the School District and the Community College District shall contribute funds sufficient to defray the difference in cost to the system in providing the same health coverage to Retired Persons and the surviving spouses and surviving domestic partners of active employees and Retired Persons as is provided for active employee members excluding health coverage or subsidies for health coverage paid for active employees as a result of collective bargaining;

(iii) after application subsection (i) and (ii), the City and County, the School District and the Community College District shall contribute 50% of Retired Persons' remaining monthly contribution. Pursuant to Charter section A8.428b(4), for retired employees who were hired on or after January 10, 2009 employers shall contribute 100% of the employer contribution established in A8.428 Subsection (b)(3) for:

(i) A Retired Employee who was Hired on or After January 10, 2009, with 20 or more years of Credited Service with the Employers; and their surviving spouses or surviving domestic partners:

(ii) The surviving spouses or surviving domestic partners of active employees hired on or after January 10, 2009, with 20 or more years of Credited Service with the Employers;

(iii) Retired Persons who retired for disability; and their surviving spouses or surviving domestic partners; and

(iv) The surviving spouses or surviving domestic partners of active employees who died in the line of duty where the surviving spouse or surviving domestic partner is entitled to a death allowance as a result of the death in the line of duty.

Pursuant to A8.428b(5), for retired employees who were hired on or after January 10, 2009 there are provisions for the employer to pay for 50%-75% identified in A8.428 Subsections (a)(4), (a)(5) and (a)(6), the Employers shall contribute:

(i) 50% percent of the employer contribution established in A8.428 Subsection (b)(3) for a Retired Employee who was Hired on or After January 10, 2009, with, at least 10 but less than 15 years of Credited Service with the Employers: their surviving spouses or surviving domestic partners: and the surviving spouses or surviving domestic partners of active employees hired on or after January 10, 2009, with at least 10 but less than 15 years of Credited Service with the Employers; and

(ii) 75% percent of the employer contribution established in A8.428 Subsection (b)(3) for a Retired Employee who was Hired on or After January 10, 2009, with at least 15 but less than 20 years of Credited Service with the Employers; their surviving spouses or surviving domestic partners; and the surviving spouses or surviving domestic partners of active employees hired, on or after January 10, 2009, with at least 15 but less than 20 years of Credited Service with the Employers.

(2) Summary of Significant Accounting Policies

(a) Basis of Presentation

The accompanying financial statements are prepared using the economic resources measurement focus and on the accrual basis of accounting. The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

The System follows U.S. generally accepted accounting principles as promulgated by the Governmental Accounting Standards Board (GASB).

(b) Cash and Investments Held by the City

The Trust maintains its cash and investments as part of the City's internal pool of cash and investments. The Trust's portion of this pool is displayed on the balance sheet as "Cash and investments held with City and County Treasurer." Interest income arising from pooled investments is allocated monthly to the System based on the Trust's average daily cash balance.

In accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and External Investment Pools*, the City reports certain investments at fair value in the statement of net position and recognizes the corresponding change in fair value of investments in the year in which the change occurred. The System reports the Trust's cash and investment held by the City at fair value based on market information provided by the City and County Treasurer.

In fiscal year 2016, the Trust adopted GASB Statement No. 72, *Fair Value Measurement and Application*, which requires the Trust to use valuation techniques that are appropriate under the circumstances and are consistent with the market approach, the cost approach, or the income approach. GASB Statement No. 72 establishes a hierarchy of inputs used to measure fair value consisting of three levels. Level 1 inputs are quoted prices in active markets for identical assets or liabilities. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs.

GASB Statement No. 72 also contains note disclosure requirements regarding the hierarchy of valuation inputs and valuation techniques that were used for the fair value measurements. As of June 30, 2019, and 2018, the Trust did not have cash and investments outside of the City's pooled investments.

For those investments held with the City Treasury, the City discloses the requirements regarding the hierarchy of valuation inputs and techniques used for the fair value measurements at the City-wide level. However, such disclosure is not required at the department level for those investments held with the City Treasury.

(c) Unearned Contributions

Unearned contributions represent monies received or receivable from members and from the City, San Francisco Unified School District, San Francisco Superior Court, and San Francisco Community College District prior to year-end for benefits in future periods.

(d) Use of Estimates

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

(e) Future Implementation of New Accounting Standards

In January 2017, the GASB issued Statement No. 84, *Fiduciary Activities*. GASB Statement No. 84 establishes criteria for state and local governments to identify fiduciary activities and how those activities should be reported. The new standard is effective for periods beginning after December 15, 2018. Management is currently evaluating the impact is update will have on its financial statements.

(3) Cash and Investments Held with City Treasurer

The Trust maintains its cash and investments as part of the City's internal investment pool of cash and investments. The City investment pool is an unrated pool pursuant to investment policy guidelines established by the City Treasurer. The objectives of the policy are, in order of priority, preserve capital, meet the daily cash flow demands of the City, and provide a market rate of return while conforming to all state and local statutes governing the investment of public funds. The policy addresses soundness of financial institutions in which the City will deposit funds; types of investment instruments, as permitted by the California Government Code; and the percentage of the portfolio that may be invested in certain

instruments with longer terms of maturity. As of June 30, 2019, and 2018, the System's cash and investment balances were $102.3 million and $87.0 million, respectively, which represented less than 1 percent of the City's investment pool. The following table shows the percentage distribution of the City's pooled investments by maturity in months:

Under 1 month	1 month to less than 6 months	6 months to less than 12 months	12 months to 60 months
17.4%	22.2%	16.3%	44.1%

(4) Prepaid and Other Assets

As of June 30, 2019, prepaid and other assets included $0.5 million in prepayments to the health care providers for July 2019 health coverage, and $2.6 million in pharmacy rebates. As of June 30, 2018, prepaid and other assets included $0.5 million in prepayments to the health care providers for July 2018 health coverage, $1.9 million in pharmacy rebates, and $0.1 million in performance guarantees.

(5) Reserves for Claims for Self-Insured Plans – Medical, Prescription Drugs, and Dental

Reserves for claims for Self-Insured Plans, including medical, prescription drugs, and dental, which have been actuarially determined, represent estimates of claims reported and in process of payment and estimates of claims incurred but not yet reported. Reserves for medical claims are based on actual claim lag reports and historical payment patterns. The net position of the Trust is available to be used as directed by the HSB and may be used to minimize the impact of possible future adverse experience. Management believes that the actuarially determined reserves are adequate to cover the ultimate cost of all claims incurred but unpaid at year end.

The UHC PPO (City Health) Plan, excluding the Medicare Advantage Plan PPO (MAPD PPO), and the hospital and pharmacy services for employees and early retirees under the Blue Shield of California Access+ and Trio Plans are self-funded plans. Should deductions from the net position of the self-funded plans exceed related additions to net position and reserves, System members and participating employers would be required to provide such additional funds. The City's contributions to the Trust for employees in the Delta Dental plan are made on an estimated basis during the year and any over or under payment will be reflected in the subsequent year's rate using claims stabilization reserves. The reserves for dental benefits are actuarially determined based on actual claim payment patterns.

Reserves for prescription drug benefits are also actuarially determined based on claim payment patterns.

The following summarizes the changes in the reserves for claims of the System's Self-Insured Plans which consist of the UHC PPO (City Health) Plan excluding the MAPD PPO, Blue Shield Flex-Funded Access+ and Trio Plans (medical benefits and prescription drug benefits), and dental plans during the years ended June 30, 2019 and 2018:

	Medical benefits	Prescription drugs	Dental benefits	Total reserves
Reserves as of June 30, 2017	$ 23,096,221	$ 1,701,694	$ 2,956,951	$ 27,754,866
Claim Payments	(188,030,102)	(54,519,901)	(43,833,311)	(286,383,314)
Current Year Claims and Changes in Estimates	189,429,395	53,204,111	43,819,774	286,453,280
Reserves as of June 30, 2018	24,495,514	385,904	2,943,414	27,824,832
Claim Payments	(187,898,990)	(57,834,553)	(44,116,343)	(289,849,886)
Current Year Claims and Changes in Estimates	188,122,982	57,803,581	43,997,554	289,924,117
Reserves as of June 30, 2019	$ 24,719,506	$ 354,932	$ 2,824,625	$ 27,899,063

(6) Postretirement Health Benefits

Medical benefits for eligible retired employees feature the same basic plan design as those for active employees and such benefits are paid for by both the former employer and the retiree (note 1).

The total employer cost of providing benefits for 28,859 and 28,305 retirees as of June 30, 2019 and 2018, respectively, is shown as employer contributions to the Trust totaling $226.3 million ($186.5 million for the City and $39.8 million for the San Francisco Unified School District and the San Francisco Community College District) and $217.6 million ($178.5 million for the City and $39.1 million for the San Francisco Unified School District and the San Francisco Community College District) for the years ending June 30, 2019 and 2018, respectively, in the Statement of Changes in Net Position for Health Benefits in the accompanying financial statements.

(7) Commitments and Contingencies

(a) Contingency Reserve Policy

The HSB adopted a contingency reserve policy for the self-funded health plans including the UHC PPO (City Health) Plan, the Delta Dental self-funded plan, and the Blue Shield Flex-funded Plan. The contingency reserve is an actuarially determined amount, based on historical claims experience required to cover the exposure of excess losses above anticipated claims expenses. The amount is established for the self-funded plans and is calculated on a fiscal year basis. It is presently set at a 99 percent confidence interval of the statistical variance of the historical claims experience. The contingency reserve amounts as of June 30, 2019 and 2018, were $6.5 million and $5.9 million, respectively, for the City Health Plan; $14.0 million and $14.1 million, respectively, for the Blue Shield flex-funded plan; and $3.0 million and $3.0 million, respectively, for the Delta Dental self-funded plan. The Contingency Reserve is part of the Trust's net position.

(b) Stabilization Reserve

The HSB adopted a self-funded plans' stabilization policy for the self-funded health plans, including the UHC PPO (City Health) Plan , Blue Shield Access+ and Trio plans, and the Delta Dental plan for active employees. The objective of a stabilization reserve is to spread any underwriting gains and losses into the following year's premium calculation in an even-handed manner such that the employers and membership are not subject to volatile year-over-year changes in premium. Pursuant to this policy, the stabilization reserve balances as of June 30, 2019 and 2018 were $1.3 million and $1.7 million, respectively, for the City Health Plan; $(5.7) million and $(9.5) million for the Blue Shield Flex plan (including Access+ and Trio); and $14.0 million and $12.7 million for Delta Dental plan. The negative reserve amounts for the Blue Shield flex plan (including Access+ and Trio); will be recovered through premium increases in subsequent years. In fiscal year 2018, the HSB approved the use of the stabilization reserve for UHC (City Health) Plan $(3.1) million and Delta Dental $(3.7) million to stabilize premium increases in fiscal year 2019. The Stabilization Reserve is part of the Trust's net position.

(c) Contingent Incentive Obligations

Based on calendar plan year results, the System calculated incentive obligation payments to medical groups under the Blue Shield Accountable Care Organization (ACO) network. The System's actuarial consultant negotiates an annual plan year cost target with the HMO and each participating ACO provider partnership group. Incentive payments are only distributed if underwriting gains are achieved at or above the negotiated target. An incentive payment of $1.1 million was made in July 2019 for plan year 2018.

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Independent Auditors' 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*

Members of the Health Service Board,
The Honorable Mayor and Board of Supervisors
City and County of San Francisco:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the San Francisco Health Service System Other Employee Benefit Trust Fund (the Trust) (also referred to as the Health Service System Trust Fund), managed by the Health Service System (the System), a department of the City and County of San Francisco, California (the City), which comprise the statements of net position available for health benefits as of June 30, 2019, and the related statements of changes in net position available for health benefits, and the related notes to the financial statements, and have issued our report thereon dated December 20, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Trust'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Trust's internal control. Accordingly, we do not express an opinion on the effectiveness of Trust's internal control.

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Trust's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the 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*.

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 Trust'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 Trust's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

San Francisco, California
December 20, 2019