

**CUMBERLAND HEIGHTS FOUNDATION, INC.
AND AFFILIATE**

Consolidated Financial Statements and Schedules

December 31, 2015 and 2014

(With Independent Auditors' Report Thereon)

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

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INDEPENDENT AUDITORS' REPORT

The Board of Directors of
Cumberland Heights Foundation, Inc.:

We have audited the accompanying consolidated financial statements of Cumberland Heights Foundation, Inc. and Affiliate, which comprise the consolidated statements of financial position as of December 31, 2015 and 2014, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statement presentation.

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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Cumberland Heights Foundation, Inc. and Affiliate as of December 31, 2015 and 2014, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Supplementary Information

Our audits were made for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The consolidating information is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position, statements of activities and cash flows of the individual entities and is not a required part of the consolidated 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 consolidated financial statements. The information has been subjected to the auditing procedures and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated 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 consolidated financial statements as a whole.

L B M C, PC

Brentwood, Tennessee
May 25, 2016

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Financial Position

December 31, 2015 and 2014

	<u>Assets</u>	
	<u>2015</u>	<u>2014</u>
Current assets:		
Cash and cash equivalents, including cash designated for debt service of \$3,588,966 in 2015 and \$2,705,972 in 2014	\$ 8,864,571	\$ 5,290,550
Accounts receivable for services, less allowance for doubtful accounts of \$577,023 in 2015 and \$473,467 in 2014	3,751,665	3,304,932
Contributions receivable, less allowance for uncollectible pledges of \$13,500 in 2015 and \$14,073 in 2014	31,046	17,185
Other current assets	<u>211,059</u>	<u>153,255</u>
Total current assets	12,858,341	8,765,922
Property and equipment, net	16,298,238	16,424,775
Investments	2,281,455	2,256,875
Beneficial interest in perpetual trust	504,582	551,534
Other assets	<u>-</u>	<u>212,500</u>
	\$ <u>31,942,616</u>	\$ <u>28,211,606</u>
	<u>Liabilities and Net Assets</u>	
Current liabilities:		
Current installments of long-term debt	\$ 433,339	\$ 464,893
Accounts payable	399,696	257,705
Accrued expenses	<u>751,824</u>	<u>802,356</u>
Total current liabilities	1,584,859	1,524,954
Long-term debt, excluding current installments	4,616,340	4,222,335
Fair value of interest rate swap agreement	<u>153,057</u>	<u>260,043</u>
Total liabilities	<u>6,354,256</u>	<u>6,007,332</u>
Net assets:		
Unrestricted	22,810,708	19,330,946
Temporarily restricted	2,273,070	2,321,794
Permanently restricted	<u>504,582</u>	<u>551,534</u>
Total net assets	<u>25,588,360</u>	<u>22,204,274</u>
	\$ <u>31,942,616</u>	\$ <u>28,211,606</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Activities

Years ended December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Changes in unrestricted net assets:		
Public support and revenue:		
Patient service revenue, net	\$ 27,083,989	\$ 25,193,540
Contributions	310,818	283,948
Gain (loss) on investments, net	(25,296)	69,320
Other	<u>412,828</u>	<u>381,968</u>
Total public support and revenue	27,782,339	25,928,776
Satisfaction of restrictions	<u>643,421</u>	<u>618,147</u>
Total unrestricted public support and revenue	<u>28,425,760</u>	<u>26,546,923</u>
Expenses:		
Program services:		
Clinical services	13,650,367	13,139,154
Ancillary services	<u>4,945,814</u>	<u>4,099,002</u>
Total program services	18,596,181	17,238,156
Supporting services:		
Administrative and fiscal	4,369,467	5,409,482
Marketing and public relations	<u>2,087,336</u>	<u>2,701,020</u>
Total supporting services	6,456,803	8,110,502
Gain on interest rate swap agreement	<u>(106,986)</u>	<u>(112,435)</u>
Total expenses	<u>24,945,998</u>	<u>25,236,223</u>
Increase in unrestricted net assets	<u>3,479,762</u>	<u>1,310,700</u>
Changes in temporarily restricted net assets:		
Contributions	640,549	918,583
Gain (loss) on investments, net	(72,088)	122,219
Net assets released from restrictions	<u>(617,185)</u>	<u>(592,762)</u>
Increase (decrease) in temporarily restricted net assets	<u>(48,724)</u>	<u>448,040</u>
Changes in permanently restricted net assets:		
Gain (loss) on investments, net	(20,716)	10,451
Income distributed	<u>(26,236)</u>	<u>(25,385)</u>
Decrease in permanently restricted net assets	<u>(46,952)</u>	<u>(14,934)</u>
Increase in net assets	3,384,086	1,743,806
Net assets at beginning of year	<u>22,204,274</u>	<u>20,460,468</u>
Net assets at end of year	\$ <u>25,588,360</u>	\$ <u>22,204,274</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Cash Flows

Years ended December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Cash flows from operating activities:		
Increase in net assets	\$ 3,384,086	\$ 1,743,806
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	1,175,163	1,150,015
Provision for doubtful accounts	579,011	705,490
Provision (recovery) on uncollectible pledges	(573)	2,293
(Gain) loss on sale of property and equipment	15,476	(3,772)
Net (gain) loss on investments	146,522	(164,560)
Gain on interest rate swap agreement	(106,986)	(112,435)
(Increase) decrease in operating assets:		
Accounts receivable for services	(1,025,744)	(800,428)
Contributions receivable	(13,288)	9,813
Other current assets	(57,804)	1,915
Increase (decrease) in operating liabilities:		
Accounts payable	141,991	11,063
Accrued expenses	<u>(50,532)</u>	<u>(28,853)</u>
Total adjustments	<u>803,236</u>	<u>770,541</u>
Net cash provided by operating activities	<u>4,187,322</u>	<u>2,514,347</u>
Cash flows from investing activities:		
Proceeds from disposal of property and equipment	-	9,645
Purchases of property and equipment	(1,039,102)	(1,721,252)
Proceeds from sale of investments	96,486	79,659
Purchases of investments	(220,636)	(140,679)
Purchase of other long-term assets	<u>-</u>	<u>(212,500)</u>
Net cash used by investing activities	<u>(1,163,252)</u>	<u>(1,985,127)</u>
Cash flows from financing activities:		
Repayments on long-term debt	(450,049)	(372,374)
Proceeds from long-term debt	1,000,000	687,500
Principal payments on capital leases	<u>-</u>	<u>(4,467)</u>
Net cash provided by financing activities	<u>549,951</u>	<u>310,659</u>
Increase in cash and cash equivalents	3,574,021	839,879
Cash and cash equivalents at beginning of year	<u>5,290,550</u>	<u>4,450,671</u>
Cash and cash equivalents at end of year	\$ <u>8,864,571</u>	\$ <u>5,290,550</u>
Supplemental disclosure of cash flow information:		
Cash paid during the year for:		
Interest	\$ <u>197,981</u>	\$ <u>205,387</u>
Noncash investing and financing activities:		
Disposal of other assets and property and equipment		
Other assets	\$ (212,500)	\$ -
Property and equipment	25,000	-
Note payable	<u>187,500</u>	<u>-</u>
	\$ <u>-</u>	\$ <u>-</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

(1) Nature of operations

Cumberland Heights Foundation, Inc. (the "Foundation") is a charitable organization that maintains and operates treatment centers for the rehabilitation of persons addicted to the use of alcohol and/or drugs. Cumberland Heights Professional Associates, Inc. (the "Affiliate") is a separate organization that was formed to provide medical and outpatient services to the patients of the Foundation. Due to the Foundation's economic interest in Cumberland Heights Professional Associates, Inc. and since the Foundation and the Affiliate share a common board of directors, the Affiliate has been included in the consolidated financial statements of the Foundation. Creative Recovery Communities, Inc. ("CRC") was a private high school, d/b/a Community High School, that shared a common board with the Foundation. CRC was closed in a prior year and effective October 28, 2015, CRC ceased to exist as a legal entity.

(2) Summary of significant accounting policies

The consolidated financial statements of the Foundation and Affiliate are presented on the accrual basis. The significant accounting policies followed are described below.

(a) Principles of consolidation

These consolidated financial statements include the accounts of the Foundation and its Affiliate (collectively, the "Organizations"). All significant intercompany accounts and transactions have been eliminated.

(b) Basis of presentation

Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Foundation and Affiliate and changes therein are classified and reported as follows:

Unrestricted net assets - Net assets that are not subject to donor-imposed stipulations.

Temporarily restricted net assets - Net assets subject to donor-imposed stipulations that may or will be met either by actions of the Foundation and Affiliate and/or the passage of time.

Permanently restricted net assets - Net assets subject to donor-imposed stipulations that they be maintained permanently by the Foundation and Affiliate.

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support.

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

(c) Investments

Investments in marketable equity securities with readily determinable fair values and all investments in debt securities are shown at their fair values in the consolidated statements of financial position. Investment income shown in the consolidated statements of activities includes interest, dividends, and realized and unrealized gains and losses, net of investment expenses. Investment income is reported in the period earned as an increase in unrestricted net assets unless the use of the assets received is limited by donor-imposed restrictions. Investment income that is temporarily restricted by the donor is reported as an increase in unrestricted net assets if the restrictions are met or expire in the year in which the income is recognized. Other donor-restricted investment income is reported as an increase in temporarily restricted net assets, depending on the nature of the restrictions. Interest and dividend income for permanently restricted net assets is reported as an increase in unrestricted net assets. Unrealized gains and losses on permanently restricted net assets are reported as increases or decreases in permanently restricted net assets, based on the donor's explicit instructions.

(d) Receivables and credit policies

The Foundation and Affiliate report accounts receivable, net of an allowance for doubtful accounts, at the amount which represents management's estimate of the amount that ultimately will be realized. The Foundation and Affiliate review the adequacy of the allowance for doubtful accounts on an ongoing basis, using historical payment trends, analyses of accounts receivable by payor source and aging of receivables, as well as review of specific accounts, and make adjustments to the allowance as necessary. The carrying amount of accounts receivable is reduced by the allowance, which reflects management's best estimate of the amounts that will not be collected. Late or interest charges on delinquent accounts are not recorded until collected. Accounts are sent to collections after 90 days of non-payments and are written off in the event of the inability to pay.

(e) Property and equipment

Property and equipment are stated at cost. Donated property and equipment are recorded at their estimated market value at the date of the gift. Depreciation and amortization are provided over the assets' estimated useful lives using the straight-line method as follows:

	<u>Years</u>
Transportation equipment	5
Furniture and fixtures	3 - 5
Machinery and equipment	3 - 5
Buildings and improvements	3 - 30

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

Expenditures for maintenance and repairs are expensed when incurred. Expenditures for renewals or betterments are capitalized. When property is retired or sold, the cost and the related accumulated depreciation or amortization are removed from the accounts, and the resulting gain or loss is recorded as a change in net assets.

(f) Income taxes

The Foundation and Affiliate are exempt from federal and state income taxes under the provisions of Internal Revenue Code Section 501(c)(3), and, accordingly, no provision for income taxes is included in the consolidated financial statements.

Under generally accepted accounting principles, a tax position is recognized as a benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the "more likely than not" test, no tax benefit is recorded. The Foundation and Affiliate had no material uncertain tax positions that qualify for recognition or disclosure in the consolidated financial statements.

As of December 31, 2015, the Organizations have no accrued interest or penalties related to uncertain tax positions. It is their policy to recognize interest and/or penalties related to income tax matters in income tax expense.

The Foundation and Affiliate file separate U.S. Federal information tax returns. The Organizations are currently open to audit under the statute of limitations by the Internal Revenue Service for the years ended after December 31, 2012.

(g) Revenue recognition

Net patient service revenue is recognized at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are made on an estimated basis in the period the related services are rendered and adjusted in future periods, as final settlements are determined.

The Foundation has a Patient Assistance Fund that provides treatment scholarships for persons who have not had a previous treatment experience, who demonstrate a high level of motivation, and who have no financial resources. The Foundation also provides for indigent patients, under certain circumstances. Revenue is not recognized in the financial statements for charity care. Direct and indirect costs of charity care which are based on the ratio of total costs to total gross charges were approximately \$479,000 and \$817,000 in 2015 and 2014, respectively.

Certain cash contributions are recognized as revenue when received.

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

Contributions receivable which are unconditional promises to give that are expected to be collected within one year are recorded at their net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of estimated future cash flows. The discounts on those amounts are computed, and recorded if material, using a risk-free interest rate applicable to the year in which the promise is received. Amortization of the discount is included in contribution revenue. Conditional promises to give are not included as support until such time as the conditions are substantially met.

(h) Advertising and promotion costs

Advertising and promotion costs are expensed as incurred.

(i) Long-lived assets

The carrying values of long-lived assets are reviewed whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable. If this review indicates that the asset will not be recoverable, as determined based on the undiscounted cash flows of the operating entity or asset over the remaining amortization period, the carrying value of the asset will be reduced to its fair value.

(j) Fair value of interest rate swap agreement

The Foundation uses derivatives to manage risks related to interest rate movements. Interest rate swap contracts designated and qualifying as cash flow hedges are reported at fair value. The gain or loss on the hedge is included in the consolidated statements of activities. The Foundation's interest rate risk management strategy is to stabilize cash flow requirements by maintaining interest rate swap contracts to convert variable-rate debt to a fixed rate.

(k) Fundraising costs

For the years ended December 31, 2015 and 2014, expenses totaling \$390,164 and \$391,990, respectively, were associated with fundraising and are classified in the consolidated statements of activities under marketing and public relations.

(l) Events occurring after reporting date

The Organizations have evaluated events and transactions that occurred between December 31, 2015 and May 25, 2016 which is the date that the consolidated financial statements were available to be issued, for possible recognition or disclosure in the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

(3) Credit risk and other concentrations

The Foundation generally maintains cash on deposit at banks in excess of federally insured amounts. All cash balances in excess of FDIC insurance are secured under repurchase agreements or other deposit arrangements. The Foundation has not experienced any losses in such accounts and management believes the Foundation is not exposed to any significant credit risk related to cash.

The Foundation utilizes various investment instruments. Investment securities, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the consolidated statements of financial position.

The Foundation and Affiliate provide rehabilitation treatment for individuals with alcohol and other chemical dependencies under various payor programs. Accordingly, the concentration of accounts receivable and revenue from Blue Cross/Magellan, private insurance companies, and individuals as of and for the years ended December 31, 2015 and 2014, is as follows:

	<u>2015</u>		<u>2014</u>	
	<u>Accounts Receivable</u>	<u>Revenue</u>	<u>Accounts Receivable</u>	<u>Revenue</u>
Other private insurance	36 %	32 %	30 %	40 %
Individuals	21	15	21	18
Blue Cross/Magellan	<u>43</u>	<u>53</u>	<u>49</u>	<u>42</u>
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

(4) Assets and liabilities measured at fair value

Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 820, *Fair Value Measurements and Disclosures*, provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Foundation's management has the ability to access.

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

Level 2 - Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The following is a description of the valuation methodologies used for asset measurement at fair value. There have been no changes in the methodologies used at December 31, 2015 and 2014.

- (i) *Mutual funds*: Valued at the net asset value of shares held by the Foundation at year end.
- (ii) *Equity securities*: Valued at the closing price reported on the active market on which the individual securities are traded.
- (iii) *Contributions receivable*: Valued at the net realizable value of the contributions receivable outstanding at year-end.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Foundation's management believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

The following table sets forth by level, within the fair value hierarchy, the Foundation's assets at fair value as of December 31, 2015 and 2014:

	<u>2015</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Cash held in interest program	\$ <u>186,257</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>186,257</u>
Mutual funds:				
Fixed income	644,701	-	-	644,701
Domestic index	107,300	-	-	107,300
International	<u>93,692</u>	<u>-</u>	<u>-</u>	<u>93,692</u>
	<u>845,693</u>	<u>-</u>	<u>-</u>	<u>845,693</u>
Equity securities:				
Consumer	354,564	-	-	354,564
Industrial and energy	284,026	-	-	284,026
Information	148,707	-	-	148,707
Healthcare	287,359	-	-	287,359
Telecommunications and utilities	51,666	-	-	51,666
Other	<u>123,183</u>	<u>-</u>	<u>-</u>	<u>123,183</u>
	<u>1,249,505</u>	<u>-</u>	<u>-</u>	<u>1,249,505</u>
Beneficial trust	<u>504,582</u>	<u>-</u>	<u>-</u>	<u>504,582</u>
Contributions receivable, net	<u>-</u>	<u>-</u>	<u>31,046</u>	<u>31,046</u>
Total	\$ <u>2,786,037</u>	\$ <u>-</u>	\$ <u>31,046</u>	\$ <u>2,817,083</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

	<u>2014</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Cash held in interest program	\$ <u>190,030</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>190,030</u>
Mutual funds:				
Fixed income	660,227	-	-	660,227
Domestic index	111,330	-	-	111,330
International	<u>112,272</u>	<u>-</u>	<u>-</u>	<u>112,272</u>
	<u>883,829</u>	<u>-</u>	<u>-</u>	<u>883,829</u>
Equity securities:				
Consumer	284,853	-	-	284,853
Industrial and energy	273,489	-	-	273,489
Information	102,919	-	-	102,919
Healthcare	316,141	-	-	316,141
Telecommunications and utilities	56,806	-	-	56,806
Other	<u>148,808</u>	<u>-</u>	<u>-</u>	<u>148,808</u>
	<u>1,183,016</u>	<u>-</u>	<u>-</u>	<u>1,183,016</u>
Beneficial trust	<u>551,534</u>	<u>-</u>	<u>-</u>	<u>551,534</u>
Contributions receivable, net	<u>-</u>	<u>-</u>	<u>17,185</u>	<u>17,185</u>
Total	\$ <u>2,808,409</u>	\$ <u>-</u>	\$ <u>17,185</u>	\$ <u>2,825,594</u>

The beneficial interest in perpetual trust consists of mutual funds and equity securities. The interest rate swap, within the fair value hierarchy, is considered a Level 2 liability and is measured at settlement value, which approximates fair value, on a recurring basis.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

The following table provides a summary of changes in fair value of the Foundation's Level 3 assets for the year ended December 31, 2015 and 2014:

**Fair Value Measurements Using Significant
Unobservable Inputs (Level 3)**

	<u>Contributions receivable, net</u>
Balance at December 31, 2013	\$ 29,291
New contributions	111,745
Contributions received	(120,448)
Increase in allowance for uncollectible pledges	(2,293)
Write-off of pledges	<u>(1,110)</u>
Balance at December 31, 2014	17,185
New contributions	49,196
Contributions received	(32,958)
Decrease in allowance for uncollectible pledges	573
Write-off of pledges	<u>(2,950)</u>
Balance at December 31, 2015	\$ <u>31,046</u>

(5) Contributions receivable

The Foundation solicits pledges of support from board members and others for contributions to be used for specific purposes. The pledges are discounted when recorded to reflect the present value of expected future collections due after one year. Contributions receivable are reported as temporarily restricted net assets in the accompanying consolidated financial statements and are scheduled to be received as follows:

	<u>2015</u>	<u>2014</u>
Receivable in less than one year	\$ 50,375	\$ 37,087
Less allowance for uncollectible pledges	(13,500)	(14,073)
Less discount	<u>(5,829)</u>	<u>(5,829)</u>
	\$ <u>31,046</u>	\$ <u>17,185</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

(6) Investments

A summary of the fair value of investments as of December 31, 2015 and 2014 is as follows:

	<u>2015</u>	<u>2014</u>
Cash held in interest program	\$ 186,257	\$ 190,030
Mutual funds	845,693	883,829
Equity securities	<u>1,249,505</u>	<u>1,183,016</u>
	<u>\$ 2,281,455</u>	<u>\$ 2,256,875</u>

As of December 31, 2015 the fair value of invested assets assigned to permanently restricted endowment net asset balances required to be maintained in perpetuity had a deficiency of \$36,520. There was no such deficiency as of December 31, 2014.

(7) Beneficial interest in perpetual trust

The Foundation is the beneficiary of a trust created by a donor, the assets of which are not in the possession of the Foundation. The Foundation has legally enforceable rights and claims to such income therefrom. Net realized and unrealized gains or losses related to the beneficial interest are reported as changes in permanently restricted net assets based on the explicit donor stipulation. The fair value of the beneficial interest was \$504,582 and \$551,534 at December 31, 2015 and 2014, respectively, and is included in permanently restricted net assets in the accompanying consolidated financial statements.

(8) Investment income

The following schedule summarizes the investment income (loss) in the consolidated statements of activities for 2015 and 2014:

	<u>2015</u>	<u>2014</u>
Interest and dividend income	\$ 63,571	\$ 70,752
Net gain (loss) on investments	(146,522)	164,560
Fees paid	<u>(35,149)</u>	<u>(33,322)</u>
	<u>\$ (118,100)</u>	<u>\$ 201,990</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

(9) Property and equipment

A summary of property and equipment as of December 31, 2015 and 2014 is as follows:

	<u>2015</u>	<u>2014</u>
Land	\$ 744,257	\$ 640,442
Buildings and improvements	24,875,107	24,377,163
Machinery and equipment	2,399,186	2,620,209
Transportation equipment	224,708	224,438
Furniture and fixtures	768,197	713,547
Construction in progress	<u>231,894</u>	<u>120,837</u>
	29,243,349	28,696,636
Accumulated depreciation and amortization	<u>(12,945,111)</u>	<u>(12,271,861)</u>
	<u>\$ 16,298,238</u>	<u>\$ 16,424,775</u>

Depreciation and amortization expense amounted to approximately \$1,175,000 and \$1,150,000 for the years ended December 31, 2015 and 2014, respectively.

Construction in progress primarily consists of amounts incurred relating to the geothermal project. At December 31, 2015, the estimated cost to complete was approximately \$2,530,000.

(10) Lines of credit

At December 31, 2015, the Foundation had a \$950,000 revolving line of credit, payable on demand, which matures August 27, 2016. There were no borrowings on the line at December 31, 2015 and 2014. Borrowings under the line bear interest, payable monthly, at an annual interest rate equal to the one-month LIBOR plus 1.50 percentage points over the index. The line of credit is secured by accounts receivable.

During 2015, the Foundation entered into a non-revolving \$1,167,000 line of credit arrangement available through February 1, 2017, that bears interest at the one-month LIBOR plus 1.74 percentage points through February 1, 2017, or earlier if the line is converted at the Foundation's election with 30 days notice to a fixed interest rate, at which time the outstanding balance will be payable in monthly principal and interest installments through February 1, 2021. During the period from the earlier of the conversion date or February 1, 2017 through February 1, 2021, the principal balance bears interest at a fixed rate equal to 1.6 percentage points plus the rate quoted in the Wall Street Journal on the earlier of the conversion date or February 1, 2017. There were no borrowings on the line at December 31, 2015.

The lines of credit agreements are cross-collateralized with the related long-term debt (see Note 11). The security agreements with the bank contain certain financial covenants, including requirements for the maintenance of specified current ratios and minimum levels of debt service coverage.

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

(11) Long-term debt

A summary of long-term debt as of December 31, 2015 and 2014 is as follows:

	<u>2015</u>	<u>2014</u>
Note payable to bank in connection with \$9,991,000 Series 2007 Health Facilities Bonds issued by the Metropolitan Government of Nashville and Davidson County, Tennessee; due in scheduled principal installments ranging from \$9,818 to \$13,208 plus interest at a variable rate based on the 30-day LIBOR rate (1.47% at December 31, 2015) through May 15, 2017.	\$ 3,791,346	\$ 3,958,061
Note payable to bank due in scheduled principal installments of \$12,500 plus interest at a fixed rate of 3.70% per annum. The note payable matured in September 2015 and was paid in full.	-	100,000
Note payable to bank due in monthly installments of \$8,333 plus interest at a fixed rate of 2.68% per annum through May 28, 2019.	341,667	441,667
Noninterest bearing note payable to individual due in annual principal installments of \$62,500 through October 14, 2016; secured by assets acquired under a purchase agreement. This agreement was cancelled in 2015, with no further payments required.	-	187,500
Note payable to bank due in monthly installments of \$16,333 plus interest at a fixed rate of 2.96% per annum through August 1, 2020.	<u>916,666</u>	<u>-</u>
Total	5,049,679	4,687,228
Less current installments	<u>433,339</u>	<u>464,893</u>
Long-term debt, excluding current installments	\$ <u>4,616,340</u>	\$ <u>4,222,335</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

A summary of future maturities of long-term debt as of December 31, 2015 is as follows:

<u>Year</u>	<u>Amount</u>
2016	\$ 433,339
2017	3,941,340
2018	300,000
2019	241,667
2020	<u>133,333</u>
	<u>\$ 5,049,679</u>

The notes payable to bank are secured by a first mortgage of the Foundation's property, a negative pledge and the Foundation's equipment, respectively. Certain loan agreements also require maintenance of certain covenants (see Note 10).

(12) Interest rate swap agreement

In May 2007, the Foundation entered into an interest rate swap agreement with a commercial bank to reduce the impact of changes in interest rates on its taxable revenue bond Series 2007. Under the interest rate swap agreement, which is classified as a cash flow hedge, the Foundation pays interest at a fixed rate of 3.39% and receives interest at 70% of the one-month LIBOR plus 1.24%. The existing agreement terminates in May 2017 and has an original notional amount of \$9,991,000. The current notional amount is \$3,784,547 as of December 31, 2015. Notional amounts do not quantify risk or represent assets or liabilities of the Foundation, but are used in the determination of cash settlements under the agreement. At December 31, 2015 and 2014, the settlement value, which approximates fair value, of the agreement was \$153,057 and \$260,043, respectively, and is reported as a long-term liability in the consolidated statements of financial position. The change in the estimated settlement value of the interest rate swap agreement of \$106,986 and \$112,435 during the years ended December 31, 2015 and 2014, respectively, is reported as a gain in the consolidated statements of activities.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

(13) Net assets

As of December 31, 2015 and 2014, the Board of Directors had designated \$516,634 and \$517,083, respectively, of unrestricted net assets as a general endowment fund to support the mission of the Organization. Since that amount resulted from an internal designation and is not donor-restricted, it is classified and reported as unrestricted net assets.

The primary objective of the Foundation's endowment funds is the preservation of capital. Secondly, the endowment funds should provide reasonable growth of principal within the unfolding market environment, as well as an adequate level of income to supplement the financial needs of the Foundation. The monies of the endowment funds are to be invested in a portfolio that is comprised of equity securities (50-70%), fixed income securities (30-50%) and cash reserves (0-10%).

Composition of and changes in endowment net assets for the years ended December 31, 2015 and 2014 were as follows:

	<u>2015</u>	<u>2014</u>
Board-designated endowment net assets,		
beginning of year	\$ 517,083	\$ 444,766
Net change during year	<u>(449)</u>	<u>72,317</u>
Board-designated endowment net assets, end of year	\$ <u>516,634</u>	\$ <u>517,083</u>

Endowment net asset composition by type of fund as of December 31, 2015 and is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Donor-restricted endowment funds	\$ -	\$ 1,764,821	\$ 504,582	\$ 2,269,403
Board-designated endowment funds	<u>516,634</u>	<u>-</u>	<u>-</u>	<u>516,634</u>
Total funds	\$ <u>516,634</u>	\$ <u>1,764,821</u>	\$ <u>504,582</u>	\$ <u>2,786,037</u>
Endowment net assets,				
beginning of year	\$ 517,083	\$ 1,782,091	\$ 551,534	\$ 2,850,708
Contributions	43,823	106,092	-	149,915
Amounts appropriated for expenditure	(18,976)	(51,274)	(26,236)	(96,486)
Gain (loss) on investment, net	<u>(25,296)</u>	<u>(72,088)</u>	<u>(20,716)</u>	<u>(118,100)</u>
Endowment net assets, end of year	\$ <u>516,634</u>	\$ <u>1,764,821</u>	\$ <u>504,582</u>	\$ <u>2,786,037</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

Endowment net asset composition by type of fund as of December 31, 2014 and is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowment Assets</u>
Donor-restricted endowment funds	\$ -	\$ 1,782,091	\$ 551,534	\$ 2,333,625
Board-designated endowment funds	<u>517,083</u>	<u>-</u>	<u>-</u>	<u>517,083</u>
Total funds	<u>\$ 517,083</u>	<u>\$ 1,782,091</u>	<u>\$ 551,534</u>	<u>\$ 2,850,708</u>
Endowment net assets, beginning of year	\$ 444,766	\$ 1,610,726	\$ 566,468	\$ 2,621,960
Contributions	49,263	91,934	-	141,197
Amounts appropriated for expenditure	(11,487)	(42,788)	(25,385)	(79,660)
Gain (loss) on investment, net	<u>34,541</u>	<u>122,219</u>	<u>10,451</u>	<u>167,211</u>
Endowment net assets, end of year	<u>\$ 517,083</u>	<u>\$ 1,782,091</u>	<u>\$ 551,534</u>	<u>\$ 2,850,708</u>

The unrestricted and temporarily restricted endowment net assets noted above include \$42,299 of cash and cash equivalents and \$2,256,875 of investments at December 31, 2014.

Temporarily restricted net assets as of December 31, 2015 and 2014 are available for the following purposes:

	<u>2015</u>	<u>2014</u>
Patient assistance (including endowment net assets of \$1,764,821 and \$1,782,091 at December 31, 2015 and 2014, respectively)	\$ 2,128,433	\$ 2,243,799
Other specific operational programs	<u>144,637</u>	<u>77,995</u>
	<u>\$ 2,273,070</u>	<u>\$ 2,321,794</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

Permanently restricted net assets are held in perpetuity with the unrealized gain (loss) reflected as permanently restricted net assets and the income from assets expendable to support certain programs. A summary of the permanently restricted net assets for which the related income is expendable as of December 31, 2015 and 2014 is as follows:

	<u>2015</u>	<u>2014</u>
Olcott Foundation	\$ <u>504,582</u>	\$ <u>551,534</u>

The endowment funds are primarily invested in equity and fixed income securities. As determined by the restrictions imposed by the donors and the guidelines established by the endowment committee, the permanently restricted endowment is generally expended at a rate between 3% and 5% of the calendar year end principal balance.

(14) Natural classification of expenses

A summary of the natural classification of expenses for the years ended December 31, 2015 and 2014 is as follows:

	<u>2015</u>	<u>2014</u>
Salaries and temporary labor	\$ 16,485,557	\$ 16,321,856
Contract services	984,650	1,129,755
Provision for doubtful accounts	579,011	705,490
Depreciation and amortization	1,175,163	1,150,015
Interest, including swap agreement	90,995	92,952
General insurance	534,693	520,841
Utilities	570,442	739,769
Food service	929,981	880,914
Supplies	612,224	654,709
Other	<u>2,983,282</u>	<u>3,039,922</u>
	\$ <u>24,945,998</u>	\$ <u>25,236,223</u>

(15) Profit-sharing plan

Eligible employees of the Foundation may participate in the Cumberland Heights 401(k) Retirement Plan (the "Plan"). Employees are generally eligible after they reach age 20 1/2 and are employed for six months. The Foundation matches salary deferral contributions equal to 100% of salary deferral contributions up to 3% of compensation and 50% of the next 2% of compensation. The Foundation made contributions of \$204,280 and \$206,837 to the Plan in 2015 and 2014, respectively.

(16) Advertising expenses

Advertising costs of \$327,652 and \$474,248 were expensed during 2015 and 2014, respectively.

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

(17) Lease commitments

The Foundation leases office space and various office equipment under operating leases. Rent expense under these leases amounted to \$326,258 and \$380,045 in 2015 and 2014, respectively.

A summary of future minimum payments under these leases as of December 31, 2015 is as follows:

<u>Year</u>	<u>Amount</u>
2016	\$ 253,113
2017	226,483
2018	170,812
2019	<u>4,366</u>
	<u>\$ 654,774</u>

(18) Contingencies

Healthcare Industry

The delivery of personal and health care services entails an inherent risk of liability. Participants in the health care services industry have become subject to an increasing number of lawsuits alleging negligence or related legal theories, many of which involve large claims and result in the incurrence of significant exposure and defense costs. The Foundation and Affiliate are insured with respect to medical malpractice risk on a claims-made basis. The Foundation and Affiliate also maintain insurance for general liability, director and officer liability and property. Certain policies are subject to deductibles. In addition to the insurance coverage provided, the Foundation and Affiliate indemnify certain officers and directors for actions taken on behalf of the Foundation and Affiliate. Management is not aware of any claims against the Foundation or Affiliate which would have a material financial impact.

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, fraud and abuse. Recently, government activity has increased with respect to investigations and/or allegations concerning possible violations of fraud and abuse statutes and/or regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Foundation and Affiliate are in compliance with fraud and abuse statutes, as well as other applicable government laws and regulations.

Notes to the Consolidated Financial Statements

December 31, 2015 and 2014

Healthcare Reform

In March 2010, Congress adopted comprehensive health care insurance legislation, the Patient Care Protection and Affordable Care Act and the Health Care and Education Reconciliation Act (collectively, the "Health Care Reform Legislation"). The Health Care Reform Legislation, among other matters, is designed to expand access to health care coverage to substantially all citizens through a combination of public program expansion and private industry health insurance. Provisions of the Health Care Reform Legislation became effective in 2014. Due to the complexity of the Health Care Reform Legislation, reconciliation and implementation of the legislation continues to be under consideration by lawmakers, and it is not certain as to what changes may be made in the future regarding health care policies. Changes to existing Medicaid coverage and payments are also expected to occur as a result of this legislation. While the full impact of Health Care Reform Legislation is not yet fully known, changes to policies regarding reimbursement, universal health insurance and managed competition may materially impact the Organizations' operations.

Litigation

The Foundation and Affiliate are involved in various legal actions arising in the normal course of business. In the opinion of management, such matters will not have a material adverse effect on the Foundation's consolidated financial position or results of operations. As these matters develop, it is reasonably possible management's estimate of their effect could change and an accrual for additional liabilities could be required.

(19) Related party transactions

The Foundation sometimes purchases goods or services from companies or organizations that are affiliated with or owned, directly or indirectly, by members of the Board of Directors. Additionally, the Foundation receives pledges from companies or organizations that are affiliated with or owned, directly or indirectly, by members of the Board of Directors.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidating Statement of Financial Position

December 31, 2015

Assets	Cumberland Heights Foundation, Inc.	Cumberland Heights Professional Associates, Inc.	Eliminating Entries		Consolidated
			Debit	Credit	
Current assets:					
Cash and cash equivalents	\$ 8,596,213	\$ 268,358	-	\$ -	\$ 8,864,571
Accounts receivable for services, net	3,613,111	138,554	-	-	3,751,665
Receivable from related parties	1,293	-	-	1,293	-
Contributions receivable, net	31,046	-	-	-	31,046
Other current assets	200,048	10,105	-	-	210,153
Total current assets	12,441,711	417,017	-	1,293	12,857,435
Property and equipment, net	16,298,238	-	-	-	16,298,238
Investments	2,281,455	-	-	-	2,281,455
Beneficial interest in perpetual trust	504,582	-	-	-	504,582
	<u>\$ 31,525,986</u>	<u>\$ 417,017</u>	<u>-</u>	<u>1,293</u>	<u>\$ 31,941,710</u>
Liabilities and Net Assets					
Current liabilities:					
Current installments of long term debt	\$ 433,339	\$ -	-	\$ -	\$ 433,339
Payable to related parties	-	1,293 (a)	1,293	-	-
Accounts payable	354,469	45,227	-	-	399,696
Accrued expenses	709,700	42,124	-	-	751,824
Total current liabilities	1,497,508	88,644	1,293	-	1,584,859
Long-term debt, excluding current installments	4,616,340	-	-	-	4,616,340
Fair value of interest rate swap agreement	153,057	-	-	-	153,057
Total liabilities	6,266,905	88,644	1,293	-	6,354,256
Net assets					
Unrestricted	22,482,335	328,373	-	-	22,810,708
Temporarily restricted	2,273,070	-	-	-	2,273,070
Permanently restricted	504,582	-	-	-	504,582
Total net assets	25,259,987	328,373	-	-	25,588,360
	<u>\$ 31,526,892</u>	<u>\$ 417,017</u>	<u>1,293</u>	<u>-</u>	<u>\$ 31,942,616</u>

(a) To eliminate intercompany receivables and payables.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidating Statement of Activities

Year Ended December 31, 2015

	Cumberland Heights Foundation, Inc.	Cumberland Heights Professional Associates, Inc.	Eliminating Entries		
			Debit	Credit	Consolidated
Changes in unrestricted net assets:					
Public support and revenue:					
Patient service revenue, net	\$ 26,331,573	\$ 752,416	-	\$ -	\$ 27,083,989
Contributions	310,818	-	-	-	310,818
Gain (loss) on investments, net	(25,296)	-	-	-	(25,296)
Other	412,828	155,000 (a)	155,000	-	412,828
Total public support and revenue	27,029,923	907,416	155,000	-	27,782,339
Satisfaction of restrictions	643,421	-	-	-	643,421
Total unrestricted public support and revenue	27,673,344	907,416	155,000	-	28,425,760
Expenses:					
Program services:					
Clinical services	12,751,816	933,551	-	(a) 35,000	13,650,367
Ancillary services	4,945,814	-	-	-	4,945,814
Total program services	17,697,630	933,551	-	35,000	18,596,181
Supporting services:					
Administrative and fiscal	4,460,975	28,492	-	(a) 120,000	4,369,467
Marketing and public relations	2,087,336	-	-	-	2,087,336
Total supporting services	6,548,311	28,492	-	120,000	6,456,803
Gain on interest rate swap agreement	(106,986)	-	-	-	(106,986)
Total expenses	24,138,955	962,043	-	155,000	24,945,998
Increase (decrease) in unrestricted net assets	3,534,389	(54,627)	155,000	155,000	3,479,762
Changes in temporarily restricted net assets:					
Contributions	640,549	-	-	-	640,549
Gain (loss) on investments, net	(72,088)	-	-	-	(72,088)
Net assets released from restrictions	(617,185)	-	-	-	(617,185)
Decrease in temporarily restricted net assets	(48,724)	-	-	-	(48,724)
Changes in permanently restricted net assets					
Gain (loss) on investments, net	(20,716)	-	-	-	(20,716)
Income distributed	(26,236)	-	-	-	(26,236)
Decrease in permanently restricted net assets	(46,952)	-	-	-	(46,952)
Increase (decrease) in net assets	3,438,713	(54,627)	155,000	155,000	3,384,086
Net assets at beginning of year	21,821,275	382,999	400,745	400,745	22,204,274
Net assets at end of year	\$ 25,259,988	\$ 328,372	\$ 555,745	\$ 555,745	\$ 25,588,360

(a) To eliminate intercompany administrative fee income/expense.