

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

Consolidated Financial Statements and Schedules

December 31, 2012 and 2011

(With Independent Auditors' Report Thereon)



LATTIMORE BLACK MORGAN & CAIN, PC
CERTIFIED PUBLIC ACCOUNTANTS AND BUSINESS ADVISORS

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Table of Contents

	<u>Page</u>
Independent Auditors' Report	1 - 2
Financial Statements:	
Consolidated Statements of Financial Position	3
Consolidated Statements of Activities	4
Consolidated Statements of Cash Flows	5
Notes to the Consolidated Financial Statements	6 - 23
Schedules:	
Consolidating Statement of Financial Position	24
Consolidating Statement of Activities	25

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, 2012 and 2011, 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, 2012 and 2011, 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.

Lattimore Black Morgan + Cain, PC

Brentwood, Tennessee
May 23, 2013

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Financial Position

December 31, 2012 and 2011

	<u>Assets</u>	
	<u>2012</u>	<u>2011</u>
Current assets:		
Cash	\$ 3,184,168	\$ 1,063,832
Accounts receivable for services, less allowance for doubtful accounts of \$527,954 in 2012 and \$495,683 in 2011	2,911,228	3,158,501
Current portion of contributions receivable, less allowance for uncollectible pledges of \$46,325 in 2012 and \$88,648 in 2011	57,575	60,563
Other current assets	<u>176,412</u>	<u>274,619</u>
Total current assets	6,329,383	4,557,515
Property and equipment, net	16,292,348	15,269,028
Contributions receivable, excluding current portion	1,279	38,201
Investments	1,491,001	1,144,704
Beneficial interest in perpetual trust	<u>541,138</u>	<u>504,838</u>
	\$ <u>24,655,149</u>	\$ <u>21,514,286</u>
 <u>Liabilities and Net Assets</u> 		
Current liabilities:		
Line of credit	\$ -	\$ 52,953
Current installments of long-term debt	259,166	104,308
Current installments of capital lease obligation	24,067	23,289
Accounts payable	520,874	275,426
Accrued expenses	<u>835,565</u>	<u>684,043</u>
Total current liabilities	1,639,672	1,140,019
Long-term debt, excluding current installments	4,395,130	4,297,848
Capital lease obligation, excluding current installments	6,691	32,910
Fair value of interest rate swap agreement	<u>523,945</u>	<u>575,154</u>
Total liabilities	<u>6,565,438</u>	<u>6,045,931</u>
Net assets:		
Unrestricted	15,770,256	13,473,074
Temporarily restricted	1,778,317	1,490,443
Permanently restricted	<u>541,138</u>	<u>504,838</u>
Total net assets	<u>18,089,711</u>	<u>15,468,355</u>
	\$ <u>24,655,149</u>	\$ <u>21,514,286</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Activities

Years ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Changes in unrestricted net assets:		
Public support and revenue:		
Patient service revenue, net	\$ 23,206,041	\$ 19,020,187
Contributions	314,463	282,371
Investment income	28,047	1,071
Other	<u>394,138</u>	<u>332,825</u>
Total public support and revenue	23,942,689	19,636,454
Satisfaction of restrictions	<u>1,057,472</u>	<u>1,158,418</u>
Total unrestricted public support and revenue	<u>25,000,161</u>	<u>20,794,872</u>
Expenses:		
Program services:		
Clinical services	11,088,878	9,363,168
Ancillary services	<u>3,687,673</u>	<u>3,374,589</u>
Total program services	14,776,551	12,737,757
Supporting services:		
Administrative and fiscal	5,226,638	4,550,187
Marketing and public relations	<u>2,750,999</u>	<u>2,630,033</u>
Total supporting services	7,977,637	7,180,220
(Gain) loss on interest rate swap agreement	<u>(51,209)</u>	<u>92,981</u>
Total expenses	<u>22,702,979</u>	<u>20,010,958</u>
Increase in unrestricted net assets	<u>2,297,182</u>	<u>783,914</u>
Changes in temporarily restricted net assets:		
Contributions	1,233,070	563,422
Investment income (loss), net	91,051	(5,774)
Net assets released from restrictions	<u>(1,036,247)</u>	<u>(1,124,188)</u>
Increase (decrease) in temporarily restricted net assets	<u>287,874</u>	<u>(566,540)</u>
Changes in permanently restricted net assets:		
Investment income (loss), net	57,525	(7,036)
Income distributed	<u>(21,225)</u>	<u>(34,230)</u>
Increase (decrease) in permanently restricted net assets	<u>36,300</u>	<u>(41,266)</u>
Increase in net assets	2,621,356	176,108
Net assets at beginning of year	<u>15,468,355</u>	<u>15,292,247</u>
Net assets at end of year	<u>\$ 18,089,711</u>	<u>\$ 15,468,355</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Cash Flows

Years ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Cash flows from operating activities:		
Change in net assets	\$ 2,621,356	\$ 176,108
Adjustments to reconcile change in net assets to net cash provided (used) by operating activities:		
Depreciation and amortization	1,000,375	996,764
Provision for doubtful accounts	776,608	425,485
Provision for uncollectible pledges	(42,323)	(16,008)
Gain on sale of property and equipment	(1,800)	-
Discount on contributions receivable	-	(13,189)
Net (gain) loss on investments	(148,207)	29,012
(Gain) loss on interest rate swap agreement	(51,209)	92,981
(Increase) decrease in operating assets:		
Accounts receivable for services	(529,335)	(944,959)
Contributions receivable	82,233	317,088
Other current assets	98,207	81,111
Increase (decrease) in operating liabilities:		
Accounts payable	245,448	(65,223)
Accrued expenses	<u>151,522</u>	<u>(69,988)</u>
Total adjustments	<u>1,581,519</u>	<u>833,074</u>
Net cash provided by operating activities	<u>4,202,875</u>	<u>1,009,182</u>
Cash flows from investing activities:		
Proceeds from disposal of property and equipment	1,800	-
Purchases of property and equipment	(2,023,695)	(799,223)
Proceeds from sale of investments	58,406	76,449
Purchases of investments, net	(292,796)	(97,579)
Change in restricted cash	<u>-</u>	<u>940,837</u>
Net cash provided (used) by investing activities	<u>(2,256,285)</u>	<u>120,484</u>
Cash flows from financing activities:		
Repayments on long-term debt	(197,860)	(1,097,844)
Proceeds from long-term debt	450,000	-
Line of credit, net activity	(52,953)	52,953
Principal payments on capital leases	<u>(25,441)</u>	<u>(20,571)</u>
Net cash provided (used) by financing activities	<u>173,746</u>	<u>(1,065,462)</u>
Increase in cash	2,120,336	64,204
Cash at beginning of year	<u>1,063,832</u>	<u>999,628</u>
Cash at end of year	<u>\$ 3,184,168</u>	<u>\$ 1,063,832</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(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, however, still exists as a legal entity for business purposes.

(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.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(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 makes 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 - 7
Machinery and equipment	3 - 10
Buildings and improvements	3 - 39

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.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(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, 2012, 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, 2008.

(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 \$688,000 and \$745,000 in 2012 and 2011, respectively.

Certain cash contributions are recognized as revenue when received.

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.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(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) New accounting pronouncements

In July 2011, the Financial Accounting Standards Board ("FASB") issued accounting standards that require changes in financial statement presentation and enhanced disclosures by health care entities that recognize significant amounts of patient service revenue at the time services are rendered without taking account of patients' ability to pay. These standards require health care entities to change the presentation of their statement of operations by reclassifying the provision for bad debts associated with patient service revenue from an operating expense to a deduction from patient service revenue (net of contractual allowances and discounts). Additionally, these entities will be required to provide enhanced disclosure about their policies for recognizing revenue and assessing bad debts as well as qualitative and quantitative information about changes in the allowance for doubtful accounts. These standards are effective for fiscal years ending after December 15, 2012. The Foundation has evaluated these accounting standards and has determined that the requirements are not applicable to the Foundation as the collectibility of patient service revenue is generally determinable near the time of service.

(l) Fundraising costs

For the years ended December 31, 2012 and 2011, expenses totaling \$364,019 and \$342,598, respectively, were associated with fundraising and are classified in the consolidated statements of activities under marketing and public relations.

(m) Reclassifications

Certain reclassifications have been made to the 2011 consolidated financial statements in order for them to conform to the 2012 presentation. These reclassifications had no effect on net assets or changes in net assets as previously reported.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(n) Events occurring after reporting date

The Foundation has evaluated events and transactions that occurred between December 31, 2011 and May 23, 2013 which is the date that the consolidated financial statements were available to be issued, for possible recognition or disclosure in the consolidated financial statements.

(3) Credit risk and other concentrations

The Foundation generally maintains cash on deposit at banks in excess of federally insured amounts. 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 provides 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, 2012 and 2011, is as follows:

	<u>2012</u>		<u>2011</u>	
	<u>AR</u>	<u>Revenue</u>	<u>AR</u>	<u>Revenue</u>
Other private insurance	38 %	36 %	34 %	46 %
Individuals	30	24	26	29
Blue Cross/Magellan	<u>32</u>	<u>40</u>	<u>40</u>	<u>25</u>
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

(4) Assets and liabilities measured at fair value

FASB 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.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

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, 2012 and 2011.

- (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, 2012 and 2011

The following table sets forth by level, within the fair value hierarchy, the Foundation's assets at fair value as of December 31, 2012 and 2011:

	<u>2012</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Cash held in interest program	\$ <u>104,572</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>104,572</u>
Mutual funds:				
Fixed income	481,680	-	-	481,680
Domestic index	77,188	-	-	77,188
International	<u>86,083</u>	<u>-</u>	<u>-</u>	<u>86,083</u>
	<u>644,951</u>	<u>-</u>	<u>-</u>	<u>644,951</u>
Equity securities:				
Consumer	177,741	-	-	177,741
Industrial and energy	241,091	-	-	241,091
Information	73,002	-	-	73,002
Healthcare	115,864	-	-	115,864
Telecommunications and utilities	57,007	-	-	57,007
Other	<u>76,773</u>	<u>-</u>	<u>-</u>	<u>76,773</u>
	<u>741,478</u>	<u>-</u>	<u>-</u>	<u>741,478</u>
Beneficial trust	<u>541,138</u>	<u>-</u>	<u>-</u>	<u>541,138</u>
Contributions receivable, net	<u>-</u>	<u>-</u>	<u>58,854</u>	<u>58,854</u>
Total	\$ <u>2,032,139</u>	\$ <u>-</u>	\$ <u>58,854</u>	\$ <u>2,090,993</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

	2011			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Cash held in interest program	\$ <u>92,365</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>92,365</u>
Mutual funds:				
Fixed income	402,395	-	-	402,395
Domestic index	67,004	-	-	67,004
International	<u>57,384</u>	<u>-</u>	<u>-</u>	<u>57,384</u>
	<u>526,783</u>	<u>-</u>	<u>-</u>	<u>526,783</u>
Equity securities:				
Consumer	121,046	-	-	121,046
Industrial and energy	158,914	-	-	158,914
Information	54,082	-	-	54,082
Healthcare	81,408	-	-	81,408
Telecommunications and utilities	54,430	-	-	54,430
Other	<u>55,676</u>	<u>-</u>	<u>-</u>	<u>55,676</u>
	<u>525,556</u>	<u>-</u>	<u>-</u>	<u>525,556</u>
Beneficial trust	<u>504,838</u>	<u>-</u>	<u>-</u>	<u>504,838</u>
Contributions receivable, net	<u>-</u>	<u>-</u>	<u>98,764</u>	<u>98,764</u>
Total	\$ <u>1,649,542</u>	\$ <u>-</u>	\$ <u>98,764</u>	\$ <u>1,748,306</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 fair value on a recurring basis.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

The following table provides a summary of changes in fair value of the Foundation's Level 3 assets for the year ended December 31, 2012 and 2011:

Fair Value Measurements Using Significant Unobservable Inputs (Level 3)

	Contributions receivable, net
Balance at December 31, 2010	\$ 386,655
New contributions	32,415
Contributions received	(302,048)
Decrease in allowance for uncollectible pledges	16,008
Decrease in contribution discount	13,189
Write-off of pledges	<u>(47,455)</u>
Balance at December 31, 2011	98,764
New contributions	34,295
Contributions received	(105,094)
Decrease in allowance for uncollectible pledges	42,323
Write-off of pledges	<u>(11,434)</u>
Balance at December 31, 2012	<u>\$ 58,854</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>2012</u>	<u>2011</u>
Receivable in less than one year	\$ 103,900	\$ 149,211
Receivable in one to five years	<u>7,108</u>	<u>44,030</u>
	111,008	193,241
Less allowance for uncollectible pledges	(46,325)	(88,648)
Less discount	<u>(5,829)</u>	<u>(5,829)</u>
	<u>\$ 58,854</u>	<u>\$ 98,764</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(6) Investments

A summary of the fair value of investments as of December 31, 2012 and 2011 is as follows:

	<u>2012</u>	<u>2011</u>
Cash held in interest program	\$ 104,572	\$ 92,365
Mutual funds	644,951	526,783
Equity securities	<u>741,478</u>	<u>525,556</u>
	<u>\$ 1,491,001</u>	<u>\$ 1,144,704</u>

At December 31, 2012, the fair value of invested assets assigned to permanently restricted endowment net asset balances required to be maintained in perpetuity did not have a deficiency. At December 31, 2011 there was a deficiency of \$36,263.

(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 \$541,138 and \$504,838 at December 31, 2012 and 2011, 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 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Interest and dividend income	\$ 51,636	\$ 38,325
Net gain (loss) on investments	148,207	(29,012)
Fees paid	<u>(23,220)</u>	<u>(21,052)</u>
	<u>\$ 176,623</u>	<u>\$ (11,739)</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(9) Property and equipment

A summary of property and equipment as of December 31, 2012 and 2011 is as follows:

	<u>2012</u>	<u>2011</u>
Land	\$ 440,442	\$ 348,442
Buildings and improvements	22,709,807	21,415,559
Machinery and equipment	2,623,713	3,166,884
Transportation equipment	264,062	207,654
Furniture and fixtures	1,096,827	1,038,762
Construction in progress	<u>624,603</u>	<u>440,380</u>
	27,759,454	26,617,681
Accumulated depreciation	<u>(11,467,106)</u>	<u>(11,348,653)</u>
	<u>\$ 16,292,348</u>	<u>\$ 15,269,028</u>

Construction in progress primarily consists of amounts incurred relating to the renovation of certain property. At December 31, 2012, the estimated cost to complete was approximately \$273,000.

(10) Line of credit

At December 31, 2012, the Foundation had a \$950,000 revolving line of credit, payable on demand, which matures August 30, 2013. There were no borrowings on the line at December 31, 2012. There were borrowings of \$52,953 on the line as of December 31, 2011. Borrowings under the line bear interest, payable monthly, at an annual interest rate equal to the one-month LIBOR plus 2.75 percentage points over the index. The line of credit is secured by accounts receivable.

The line of credit agreement is cross-collateralized with the long-term debt (see Note 11). The security agreement with the bank contains certain financial covenants, including requirements for the maintenance of specified current ratios and minimum levels of debt service coverage. The Foundation was in compliance with all debt covenants as of December 31, 2012.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(11) Long-term debt

A summary of long-term debt as of December 31, 2012 and 2011 is as follows:

	<u>2012</u>	<u>2011</u>
Note payable 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 (1.3839% at December 31, 2012) through May 15, 2017.	\$ 4,254,296	\$ 4,402,156
Note payable due in scheduled principal installments of \$12,500 plus interest at a fixed rate of 3.70% per annum through September 4, 2015.	<u>400,000</u>	<u>-</u>
Total	4,654,296	4,402,156
Less current installments	<u>259,166</u>	<u>104,308</u>
Long-term debt, excluding current installments	\$ <u>4,395,130</u>	\$ <u>4,297,848</u>

A summary of future maturities of long-term debt as of December 31, 2012 is as follows:

<u>Year</u>	<u>Amount</u>
2013	\$ 259,166
2014	280,462
2015	252,393
2016	150,006
2017	<u>3,712,269</u>
	\$ <u>4,654,296</u>

The long-term notes payable are secured by a first mortgage of the Foundation's property and a negative pledge, respectively. The loan agreement in connection with the \$9,991,000 Series 2007 Health Facilities Bonds also requires maintenance of certain covenants (see Note 10).

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(12) Capital lease obligation

The Foundation entered into a capital lease arrangement during 2011 to finance the acquisition of certain equipment. The Foundation's obligation as of December 31, 2012 and 2011 is as follows:

	<u>2012</u>	<u>2011</u>
Minimum lease payments payable	\$ 31,395	\$ 58,304
Less: portion representing interest	<u>637</u>	<u>2,105</u>
Capital lease obligation	30,758	56,199
Less: current portion	<u>24,067</u>	<u>23,289</u>
Long-term portion	<u>\$ 6,691</u>	<u>\$ 32,910</u>

Future minimum annual lease payments payable under the capital lease obligation as of December 31, 2012 are as follows:

<u>Year</u>	<u>Amount</u>
2013	\$ 24,667
2014	<u>6,728</u>
Total current minimum lease payments	<u>\$ 31,395</u>

Equipment utilized under capital lease obligation at December 31, 2012 amounted to approximately \$60,319.

(13) 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 \$4,242,694 as of December 31, 2012. 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, 2012 and 2011, the fair value of the agreement was \$523,945 and \$575,154, respectively, and is reported as a long-term liability in the consolidated statements of financial position. The change in the estimated fair value of the interest rate swap agreement of \$(51,209) and \$92,981 during the years ended December 31, 2012 and 2011, respectively, is reported as a (gain) loss in the consolidated statements of activities.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

(14) Net assets

As of December 31, 2012 and 2011, the Board of Directors had designated \$289,499 and \$242,025, 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, 2012 and 2011 were as follows:

	<u>2012</u>	<u>2011</u>
Board-designated endowment net assets,		
beginning of year	\$ 242,025	\$ 234,963
Net change during year	<u>47,474</u>	<u>7,062</u>
Board-designated endowment net assets, end of year	<u>\$ 289,499</u>	<u>\$ 242,025</u>

Endowment net asset composition by type of fund as of December 31, 2012 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	\$ -	\$ 1,402,842	\$ 541,138	\$ 1,943,980
Board-designated				
endowment funds	<u>289,499</u>	<u>-</u>	<u>-</u>	<u>289,499</u>
Total funds	<u>\$ 289,499</u>	<u>\$ 1,402,842</u>	<u>\$ 541,138</u>	<u>\$ 2,233,479</u>
Endowment net assets,				
beginning of year	\$ 242,025	\$ 902,679	\$ 504,838	\$ 1,649,542
Contributions	31,011	438,236	-	469,247
Amounts appropriated for				
expenditure	(8,057)	(29,124)	(21,225)	(58,406)
Investment income, net	<u>24,520</u>	<u>91,051</u>	<u>57,525</u>	<u>173,096</u>
Endowment net assets,				
end of year	<u>\$ 289,499</u>	<u>\$ 1,402,842</u>	<u>\$ 541,138</u>	<u>\$ 2,233,479</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

Endowment net asset composition by type of fund as of December 31, 2011 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	\$ -	\$ 902,679	\$ 504,838	\$ 1,407,517
Board-designated endowment funds	<u>242,025</u>	<u>-</u>	<u>-</u>	<u>242,025</u>
Total funds	<u>\$ 242,025</u>	<u>\$ 902,679</u>	<u>\$ 504,838</u>	<u>\$ 1,649,542</u>
Endowment net assets, beginning of year	\$ 234,963	\$ 876,357	\$ 546,104	\$ 1,657,424
Contributions	17,525	64,846	-	82,371
Amounts appropriated for expenditure	(9,469)	(32,750)	(34,230)	(76,449)
Investment income, net	<u>(994)</u>	<u>(5,774)</u>	<u>(7,036)</u>	<u>(13,804)</u>
Endowment net assets, end of year	<u>\$ 242,025</u>	<u>\$ 902,679</u>	<u>\$ 504,838</u>	<u>\$ 1,649,542</u>

Temporarily restricted net assets as of December 31, 2012 and 2011 are available for the following purposes:

	<u>2012</u>	<u>2011</u>
Patient assistance (including endowment net assets of \$1,402,842 and \$902,679 at December 31, 2012 and 2011, respectively)	\$ 1,529,030	\$ 1,287,415
Other specific operational programs	<u>249,287</u>	<u>203,028</u>
	<u>\$ 1,778,317</u>	<u>\$ 1,490,443</u>

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, 2012 and 2011 is as follows:

	<u>2012</u>	<u>2011</u>
Olcott Foundation	\$ <u>541,138</u>	\$ <u>504,838</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

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.

(15) Natural classification of expenses

A summary of the natural classification of expenses for the years ended December 31, 2012 and 2011 is as follows:

	<u>2012</u>	<u>2011</u>
Salaries and temporary labor	\$ 13,995,712	\$ 12,010,422
Contract services	1,176,279	1,072,576
Provision for doubtful accounts	776,608	425,485
Depreciation and amortization	1,000,375	996,764
Interest, including swap agreement	169,397	321,898
General insurance	461,739	382,929
Utilities	627,004	618,709
Food service	752,333	670,284
Supplies	589,647	473,712
Other	<u>3,153,885</u>	<u>3,038,179</u>
	<u>\$ 22,702,979</u>	<u>\$ 20,010,958</u>

(16) 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. From October 2010 through June 2012 the Foundation discontinued all matching contributions. In July 2012 the Foundation re-instated the employer matching contribution 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 \$96,583 to the Plan in 2012.

(17) Advertising expenses

Advertising costs of \$644,089 and \$766,436 were expensed during 2012 and 2011, respectively.

(18) Lease commitments

The Foundation leases office space and various office equipment under operating leases. Rent expense under these leases amounted to \$382,868 and \$475,266 in 2012 and 2011, respectively.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

A summary of future minimum payments under these leases as of December 31, 2012 is as follows:

<u>Year</u>	<u>Amount</u>
2013	\$ 333,778
2014	199,920
2015	<u>73,784</u>
	<u>\$ 607,482</u>

(19) 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.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2012 and 2011

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 become effective at various dates over the next several years and a number of additional steps are required to implement these requirements. 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 Organization's operations.

Litigation

The Foundation is 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.

(20) 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.

(21) Supplemental disclosures of cash flow statement information

	<u>2012</u>	<u>2011</u>
Interest paid	\$ <u>220,606</u>	\$ <u>228,917</u>
Equipment acquired under capital lease	\$ <u>-</u>	\$ <u>76,770</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidating Statement of Financial Position

December 31, 2012

Assets	Cumberland Heights Foundation, Inc.	Cumberland Heights Professional Associates, Inc.	Eliminating Entries		Consolidated
			Debit	Credit	
Current assets:					
Cash	\$ 3,160,242	\$ 23,926	\$ -	\$ -	\$ 3,184,168
Accounts receivable for services, net	2,797,977	113,251	-	-	2,911,228
Receivable from related parties	25,610	-	(a)	25,610	-
Current portion of contributions receivable, net	57,575	-	-	-	57,575
Other current assets	166,141	10,271	-	-	176,412
Total current assets	6,207,545	147,448	-	25,610	6,329,383
Property and equipment, net	16,292,348	-	-	-	16,292,348
Pledges receivable, excluding current portion	1,279	-	-	-	1,279
Investments	1,491,001	-	-	-	1,491,001
Beneficial interest in perpetual trust	541,138	-	-	-	541,138
Total assets	\$ 24,533,311	\$ 147,448	\$ -	\$ 25,610	\$ 24,655,149
Liabilities and Net Assets					
Current liabilities:					
Current installments of long term debt	\$ 259,166	\$ -	\$ -	\$ -	\$ 259,166
Current installments of capital lease obligation	24,067	-	-	-	24,067
Payable to related parties	-	25,610 (a)	25,610	-	-
Accounts payable	502,407	18,467	-	-	520,874
Accrued expenses	789,337	46,228	-	-	835,565
Total current liabilities	1,574,977	90,305	25,610	-	1,639,672
Long term debt, excluding current installments	4,395,130	-	-	-	4,395,130
Capital lease obligation, excluding current installments	6,691	-	-	-	6,691
Fair market value of interest rate swap agreement	523,945	-	-	-	523,945
Total liabilities	6,500,743	90,305	25,610	-	6,565,438
Net assets					
Unrestricted	15,713,113	57,143	-	-	15,770,256
Temporarily restricted	1,778,317	-	-	-	1,778,317
Permanently restricted	541,138	-	-	-	541,138
Total net assets	18,032,568	57,143	-	-	18,089,711
	\$ 24,533,311	\$ 147,448	\$ 25,610	\$ -	\$ 24,655,149

(a) To eliminate intercompany receivables and payables.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidating Statement of Activities

Year Ended December 31, 2012

	Cumberland Heights Foundation, Inc.	Cumberland Heights Professional Associates, Inc.	Eliminating Entries		
			Debit	Credit	Consolidated
Changes in unrestricted net assets:					
Public support and revenue	\$ 22,473,076	\$ 732,965	\$ -	\$ -	\$ 23,206,041
Patient service revenue, net	314,463	-	-	-	314,463
Contributions	28,047	-	-	-	28,047
Investment income	394,138	240,000	240,000	-	394,138
Other					
Total public support and revenue	23,209,724	972,965	240,000	-	23,942,689
Satisfaction of restrictions	1,057,472	-	-	-	1,057,472
Total unrestricted public support and revenue	24,267,196	972,965	240,000	-	25,000,161
Expenses:					
Program services:					
Clinical services	10,263,204	945,674	-	(a) 120,000	11,088,878
Ancillary services	3,683,373	4,300	-	-	3,687,673
Total program services	13,946,577	949,974	-	120,000	14,776,551
Supporting services:					
Administrative and fiscal	5,215,479	131,159	-	(a) 120,000	5,226,638
Marketing and public relations	2,750,999	-	-	-	2,750,999
Contribution to affiliate	1,573,317	(1,573,317)	-	-	-
Total supporting services	9,539,795	(1,442,158)	-	120,000	7,977,637
Gain on interest rate swap agreement	(51,209)	-	-	-	(51,209)
Total expenses	23,435,163	(492,184)	-	240,000	22,702,979
Increase in unrestricted net assets	832,033	1,465,149	240,000	240,000	2,297,182
Changes in temporarily restricted net assets:					
Contributions	1,233,070	-	-	-	1,233,070
Investment income, net	91,051	-	-	-	91,051
Net assets released from restrictions	(1,036,247)	-	-	-	(1,036,247)
Increase in temporarily restricted net assets	287,874	-	-	-	287,874
Changes in permanently restricted net assets					
Investment loss, net	57,525	-	-	-	57,525
Income distributed	(21,225)	-	-	-	(21,225)
Increase in permanently restricted net assets	36,300	-	-	-	36,300
Increase in net assets	1,156,207	1,465,149	240,000	240,000	2,621,356
Net assets (deficit) at the beginning of the year	16,876,361	(1,408,006)	160,745	160,745	15,468,355
Net assets at the end of the year	\$ 18,032,568	\$ 57,143	\$ 400,745	\$ 400,745	\$ 18,089,711

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