

**ALIVE HOSPICE, INC.**

**Financial Statements**

**December 31, 2015 and 2014**

**(With Independent Auditors' Report Thereon)**

**ALIVE HOSPICE, INC.**

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## INDEPENDENT AUDITORS' REPORT

The Board of Directors of  
Alive Hospice, Inc.:

We have audited the accompanying financial statements of Alive Hospice, Inc. (the "Organization") which comprise the statements of financial position as of December 31, 2015 and 2014, and the related statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

### *Management's Responsibility for the Financial Statements*

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

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these 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 financial statements are free of material misstatement.

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

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

### *Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Alive Hospice, Inc. as of December 31, 2015 and 2014, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*LBMC, PC*

Brentwood, Tennessee  
May 27, 2016

ALIVE HOSPICE, INC.

Statements of Financial Position

December 31, 2015 and 2014

Assets

	<u>2015</u>	<u>2014</u>
Current assets:		
Cash and cash equivalents	\$ 7,760,572	\$ 7,076,840
Patient accounts receivable, net	2,596,553	2,585,139
Pledges receivable, net	455,312	387,493
Prepaid expenses	238,805	426,262
Other current assets	<u>72,424</u>	<u>544,369</u>
Total current assets	11,123,666	11,020,103
 Pledges receivable, net, excluding current portion	244,000	40,134
Investments	1,844,673	1,977,308
Property and equipment, net	10,764,157	10,453,780
Goodwill	554,293	554,293
Investment in joint venture	<u>1,000</u>	<u>101,063</u>
	<u>\$ 24,531,789</u>	<u>\$ 24,146,681</u>

Liabilities and Net Assets

Current liabilities:		
Accounts payable	\$ 509,108	\$ 874,910
Accrued expenses	<u>1,413,928</u>	<u>2,745,575</u>
Total current liabilities	<u>1,923,036</u>	<u>3,620,485</u>
 Net assets:		
Unrestricted		
Undesignated	18,970,280	17,416,774
Board designated	<u>439,122</u>	<u>459,725</u>
Total unrestricted net assets	19,409,402	17,876,499
Temporarily restricted	2,024,228	1,474,574
Permanently restricted	<u>1,175,123</u>	<u>1,175,123</u>
Total net assets	<u>22,608,753</u>	<u>20,526,196</u>
	<u>\$ 24,531,789</u>	<u>\$ 24,146,681</u>

See accompanying notes to the financial statements.

**ALIVE HOSPICE, INC.**

**Statements of Operations and Changes in Net Assets**

**Years ended December 31, 2015 and 2014**

	<u>2015</u>	<u>2014</u>
Unrestricted net assets:		
Revenue:		
Net patient service revenue	\$ 28,026,195	\$ 26,507,595
Contributions and fundraising	1,332,454	1,515,100
Investment income	62,240	33,733
Net realized gain (loss) on investments	(1,514)	9,873
Other revenue	49,489	36,691
Net assets released from restriction used for operations	<u>310,203</u>	<u>212,774</u>
Total operating revenue	<u>29,779,067</u>	<u>28,315,766</u>
Operating expenses:		
Salaries and wages	15,134,115	14,327,314
Employee benefits	2,852,261	2,799,393
Contract labor	493,890	493,843
Purchased services	2,503,232	2,658,394
Pharmacy and medical supplies	2,694,935	2,842,413
Occupancy and equipment	1,710,037	2,037,828
Other	2,113,214	2,081,217
Depreciation	519,729	627,185
Provision for uncollectible accounts	165,906	170,382
Interest	<u>17,932</u>	<u>19,067</u>
Total operating expenses	<u>28,205,251</u>	<u>28,057,036</u>
Operating revenue in excess of operating expenses	1,573,816	258,730
Department of Justice settlement - see Note 19	<u>-</u>	<u>(1,208,295)</u>
Change in unrestricted net assets from continuing operations	1,573,816	(949,565)
Discontinued operations - loss on palliative care	(1,253)	(1,857)
Non-operating revenues and expenses:		
Net unrealized losses on investments	(39,066)	(2,274)
Other expenses - Alive Institute	<u>(594)</u>	<u>(77,047)</u>
Total non-operating expenses	<u>(39,660)</u>	<u>(79,321)</u>
Change in unrestricted net assets	<u>1,532,903</u>	<u>(1,030,743)</u>
Temporarily restricted net assets:		
Contributions	917,612	619,267
Investment income	23,061	25,773
Net realized and unrealized gains (losses) on investments	(80,816)	16,444
Net assets released from restriction used for operations	<u>(310,203)</u>	<u>(212,774)</u>
Change in temporarily restricted net assets	<u>549,654</u>	<u>448,710</u>
Permanently restricted net assets:		
Contributions	<u>-</u>	<u>11,000</u>
Change in permanently restricted net assets	<u>-</u>	<u>11,000</u>
Change in net assets	2,082,557	(571,033)
Net assets at beginning of year	<u>20,526,196</u>	<u>21,097,229</u>
Net assets at end of year	\$ <u>22,608,753</u>	\$ <u>20,526,196</u>

See accompanying notes to the financial statements.

**ALIVE HOSPICE, INC.**

**Statements of Cash Flows**

**Years ended December 31, 2015 and 2014**

	<u>2015</u>	<u>2014</u>
Cash flows from operating activities:		
Change in net assets	\$ 2,082,557	\$ (571,033)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	519,729	627,185
Net realized and unrealized (gain) loss on investments	121,396	(24,043)
Provision for uncollectible accounts	165,906	170,594
Restricted contributions received	-	(11,000)
Changes in assets and liabilities:		
Accounts receivable	(177,320)	(172,338)
Pledges receivable	(271,685)	(79,407)
Prepaid expenses	187,457	26,874
Other current assets	411,854	(391,294)
Accounts payable	(365,802)	141,024
Accrued expenses	<u>(1,331,647)</u>	<u>706,533</u>
Net cash provided by operating activities	<u>1,342,445</u>	<u>423,095</u>
Cash flows from investing activities:		
Investment in joint venture	(1,000)	(963)
Proceeds from sale of investment in joint venture	161,154	-
Proceeds from sale of investments	286,496	1,949,507
Purchases of investments	(275,257)	(1,920,015)
Purchases of property and equipment	<u>(830,106)</u>	<u>(867,017)</u>
Net cash used by investing activities	<u>(658,713)</u>	<u>(838,488)</u>
Cash flows from financing activities -		
Proceeds from restricted contributions	<u>-</u>	<u>11,000</u>
Net cash provided by financing activities	<u>-</u>	<u>11,000</u>
Increase (decrease) in cash and cash equivalents	683,732	(404,393)
Cash and cash equivalents at beginning of year	<u>7,076,840</u>	<u>7,481,233</u>
Cash and cash equivalents at end of year	\$ <u>7,760,572</u>	\$ <u>7,076,840</u>
Supplemental disclosure of cash flow information -		
cash paid for interest	\$ <u>17,932</u>	\$ <u>19,067</u>

See accompanying notes to the financial statements.

# ALIVE HOSPICE, INC.

## Notes to the Financial Statements

December 31, 2015 and 2014

(1) Nature of activities

Alive Hospice, Inc. (the "Organization"), provides medical, psychological, and spiritual care to terminally ill patients and their families, located primarily in Middle Tennessee.

(2) Summary of significant accounting policies

The financial statements of the Organization are presented on the accrual basis. The significant accounting policies followed are described below.

(a) 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 Organization and changes therein are classified and reported as follows:

Unrestricted net assets - Net assets that are not permanently restricted nor temporarily restricted by donor-imposed restrictions. The unrestricted net assets are comprised of Board designated and unrestricted amounts. Board designated net assets are designated for various purposes based on the direction of the Organization's Board of Directors, and are not specified as an endowment.

Temporarily restricted net assets - Net assets resulting from contributions and other inflows of net assets whose use by the Organization is limited by donor-imposed restrictions that either expire by the passage of time or by actions of the Organization. Temporarily restricted net assets at December 31, 2015 and 2014 represent pledges receivable, accumulated earnings on endowment funds, and donor-restricted funds designated for various programs offered by the Organization.

Permanently restricted net assets - Net assets resulting from contributions and other inflows of assets whose use by the Organization is limited by donor-imposed restrictions that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the Organization. Permanently restricted net assets at December 31, 2015 and 2014 represent donor-restricted gifts that have been invested and are to be maintained in perpetuity, the earnings from which are temporarily restricted to support various programs offered by the Organization.

(b) Cash and cash equivalents

Cash and cash equivalents consist of bank deposits in accounts that are federally insured up to \$250,000. The Organization considers all highly liquid investments with original maturities of less than three months to be cash equivalents.

At December 31, 2015 and 2014, and at times during the year, deposits exceeded the federally insured limits. However, management monitors the soundness of the financial institutions and feels the Organization's risk is negligible.

Notes to the Financial Statements

December 31, 2015 and 2014

(c) Accounts receivable

The accounts receivable balance represents the unpaid amounts billed to patients and third-party payors. Contractual adjustments, discounts, and an allowance for uncollectible accounts are recorded to report receivables for patient care services at net realizable value. Past due receivables are determined based on contractual terms. The Organization does not accrue interest on any of its accounts receivable. As of December 31, 2015 and 2014, approximately 89% and 84%, respectively, of the Organization's accounts receivable are from Medicare and Medicaid.

(d) Allowance for uncollectible accounts

The allowance for uncollectible accounts is determined by management based upon the Organization's historical losses, specific patient circumstances, and general economic conditions. Periodically, management reviews patient accounts receivable and records an allowance based on current circumstances, and charges off the receivable against the allowance when all attempts to collect the receivable are deemed to have failed in accordance with the internal collection policy. Management believes the allowance of \$848,627 and \$655,821 as of December 31, 2015 and 2014, respectively, is adequate to cover potential losses from uncollectible accounts.

(e) Pledges receivable

Pledges receivable represent the remaining balance of unconditional promises to give that have not yet been paid. Pledges that are expected to be collected within one year or less are recorded at net realizable value. For pledges that are expected to be collected beyond one year, management has determined the difference between net realizable value and the present value of their estimated future cash flows and recorded a discount on pledges receivable for this amount. Conditional promises to give are recognized only when the conditions on which they depend are substantially met and the promises become unconditional.

(f) Investments

All investments are valued at their fair values in the statements of financial position. Unrealized gains and losses are included in the change in net assets. See Notes 5 and 17 for additional information on the Organization's investments.

(g) Property and equipment

Property and equipment are stated at cost or, if donated to the Organization, at their fair value at the date of gift. Depreciation is provided over the assets' estimated useful lives using the straight-line method. Additions and improvements over \$500 are capitalized; expenditures for routine maintenance are charged to operations. Depreciation is provided over the estimated useful lives of the various classes of assets on the straight-line method (buildings and improvements, 32-40 years; office furniture and equipment, 3-10 years).

Notes to the Financial Statements

December 31, 2015 and 2014

Gifts of long-lived assets such as land, buildings, and equipment are reported as unrestricted support unless explicit donor restrictions specify how the donated assets are to be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash and other assets that must be used to acquire long-lived assets are reported as temporarily restricted support. Absent explicit donor restrictions about how long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

(h) Goodwill

Goodwill represents the excess of the purchase price over the fair value of net assets of businesses acquired. The carrying amount of goodwill is reviewed annually to determine if facts and circumstances suggest that assets may be impaired. As of December 31, 2015 and 2014, management believes that no impairment existed.

(i) Investments in joint ventures

The Organization accounted for an investment in a joint venture using the equity method. Under the equity method, the investment was initially recorded at cost and was increased or decreased by the Organization's share of the net earnings or losses since acquisition. The carrying value was reduced by any distributions received from the joint venture.

During 2015, the Organization obtained a 1% interest in a joint venture and has accounted for the investment using the cost method. Under the cost method, the investment is recorded at cost and subsequent distributions from the joint venture are treated as a reduction of the investment.

(j) Net patient service revenue

Net patient service revenue is reported 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. Approximately 88% and 86% of the Organization's net patient service revenue was derived from the Medicare and Medicaid programs for the years ended December 31, 2015 and 2014, respectively.

Provisions for estimated third-party payor settlements have been made in the financial statements for estimated contractual adjustments, representing the difference between the standard charges for services and estimated total payments to be received from third-party payors. These estimates are adjusted in future periods as final settlements are determined.

Notes to the Financial Statements

December 31, 2015 and 2014

The Organization, like other health care providers, may be subject to investigations, regulatory action, lawsuits, and claims arising out of the conduct of its business, including the interpretation of laws and regulations governing the Medicare and Medicaid programs and other third-party payor agreements. At this time, no specific alleged violations, claims, or assessments have been made. Management intends to fully cooperate with any governmental agencies in requests for information. Noncompliance with laws and regulations can make the Organization subject to regulatory action, including fines, penalties, and exclusion from the Medicare and Medicaid programs.

Hospice organizations are subject to two specific payment limit caps under the Medicare program. One limit relates to inpatient care days that exceed 20% of the total days of hospice care provided for the year. The Organization did not exceed the 20% cap related to inpatient days in 2015 and 2014. The second limit relates to an aggregate Medicare reimbursement cap calculated by the Medicare fiscal intermediary. The Organization did not exceed the Medicare cap for the years ended December 31, 2015 and 2014.

(k) Charity care

The Organization has a policy of providing charity care to patients who are unable to pay. Such patients are identified based on financial information obtained from the patient and subsequent analysis. The estimated cost of charity care was approximately \$701,000 and \$730,000 for the years ended December 31, 2015 and 2014, respectively. The cost estimate was based on the organization-wide cost to charge ratio.

(l) Contributions

Contributions received and unconditional promises to give are recorded as unrestricted, temporarily restricted, or permanently restricted revenue depending on the existence of donor restrictions and the nature of such restrictions, if they exist.

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of operations and changes in net assets as net assets released from restriction.

If a restriction is fulfilled in the same accounting period in which the contribution is received, the contribution is reported as unrestricted.

In-kind contributions are recorded based on their estimated fair value at the date of donation. During 2015 and 2014, the Organization received approximately \$13,000 and \$9,000 in in-kind contributions, respectively.

ALIVE HOSPICE, INC.

Notes to the Financial Statements

December 31, 2015 and 2014

(m) Donated services

The value of time contributed by unpaid volunteers to the Organization has not been included in the financial statements. The value of donated tangible items is recorded at fair value at date of receipt.

(n) Income taxes

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

As of December 31, 2015 and 2014, the Organization has accrued no interest and no penalties related to uncertain tax positions. It is the Organization's policy to recognize interest and/or penalties related to income tax matters in income tax expense.

The Organization files a U.S. Federal information tax return. The Organization is currently open to audit under the statute of limitations by the Internal Revenue Service for the years ended after December 31, 2011.

(o) Long-lived assets

Management evaluates the recoverability of the investment in long-lived assets on an ongoing basis and recognizes any impairment in the year of determination. It is reasonably possible that relevant conditions could change in the near term and necessitate a change in management's estimate of the recoverability of these assets.

(p) Use of estimates

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

Notes to the Financial Statements

December 31, 2015 and 2014

(q) Recently issued accounting pronouncement

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"), which created a global, comprehensive revenue recognition model. This accounting standard amends substantially all current revenue recognition guidance by providing a single framework for addressing revenue recognition issues and improving comparability of application across all entities and industries. The standard affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets. Under the standard, an entity should follow a five step model in order to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In August 2015, Accounting Standards Update No. 2015-04, *Revenue from Contracts with Customers* ("ASU 2015-04"), was issued which deferred the effective date of ASU 2014-09 by one year. This standard is now effective for financial statements for fiscal years beginning after December 15, 2018. Therefore, the Organization expects to adopt this standard at the beginning of fiscal year 2019.

The FASB's new lease accounting standard, ASU No. 2016-02, *Leases*, which was issued on February 25, 2016, will generally require on-balance sheet recognition for all leases with terms that exceed twelve months. The new lease accounting model will continue to reflect two types of leases. Under the new rules, a lessee would account for most existing capital leases as finance leases (that is, recognizing amortization of the right-of-use ("ROU") asset, as well as separately recognizing interest on the lease liability in the statement of operations). Most existing operating leases will remain as operating leases (that is, recognizing a single total lease expense). Both finance leases and operating leases will result in the lessee recognizing a ROU asset and a lease liability. The new leasing standard is effective for nonpublic companies for fiscal years beginning after December 15, 2019, with required retrospective application to prior years.

The Organization is currently assessing the impact of adopting these accounting standards.

(r) Events occurring after reporting date

The Organization has evaluated events and transactions that occurred between December 31, 2015 and May 27, 2016 which is the date that the financial statements were available to be issued, for possible recognition or disclosure in the financial statements.

**ALIVE HOSPICE, INC.**

**Notes to the Financial Statements**

**December 31, 2015 and 2014**

**(3) Accounts receivable**

At December 31, 2015 and 2014, accounts receivable consists of the following by payor type:

	<u>2015</u>	<u>2014</u>
Medicare	\$ 4,702,043	\$ 2,943,650
Medicaid	1,264,119	1,024,730
Commercial and other	<u>837,337</u>	<u>934,446</u>
	6,803,499	4,902,826
Allowance for doubtful accounts	(848,627)	(655,821)
Medicare periodic interim payment program	<u>(3,358,319)</u>	<u>(1,661,866)</u>
	\$ <u>2,596,553</u>	\$ <u>2,585,139</u>

**(4) Pledges receivable**

The Organization recognizes unconditional promises to give at fair value in the period the promise is made. Pledges receivable are scheduled to be received over the following periods at December 31, 2015 and 2014:

	<u>2015</u>	<u>2014</u>
Less than one year	\$ 476,621	\$ 394,242
One to five years	<u>255,000</u>	<u>40,134</u>
Total pledges receivable	731,621	434,376
Allowance for uncollectible pledges	(17,749)	(6,749)
Discount on pledges	<u>(14,560)</u>	<u>-</u>
	\$ <u>699,312</u>	\$ <u>427,627</u>

For 2015, a rate of 1.60% was used to determine the estimated discount on the pledges receivable. Management has determined that any discount on pledges would be immaterial at December 31, 2014.

ALIVE HOSPICE, INC.

Notes to the Financial Statements

December 31, 2015 and 2014

(5) Investments

Investments are recorded at fair value and consisted of the following at December 31, 2015 and 2014:

	<u>2015</u>	<u>2014</u>
Money market funds	\$ 24,028	\$ 87,376
Bond funds	447,010	472,469
Equity mutual funds	878,738	845,244
Other mutual funds	<u>494,897</u>	<u>572,219</u>
	<u>\$ 1,844,673</u>	<u>\$ 1,977,308</u>

The following schedule summarizes the investment income for 2015 and 2014:

	<u>2015</u>	<u>2014</u>
Interest and dividend income	\$ 103,676	\$ 80,619
Investment expenses	(18,375)	(21,113)
Realized gain (loss) on investments	(3,614)	33,517
Unrealized losses on investments	<u>(117,782)</u>	<u>(9,474)</u>
	<u>\$ (36,095)</u>	<u>\$ 83,549</u>

Investment securities are exposed to various risks, such as interest rate, market, and credit. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risks in the near term would result in material changes in the fair value of investments and net assets of the Organization.

(6) Fair value measurements

U.S. GAAP defines fair value as the price that would be received for an asset or paid to transfer a liability (an exit price) in the Organization's principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

A fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date. The fair values of money market funds, bond funds, and equity mutual funds that are readily marketable are determined by obtaining quoted prices on nationally recognized securities exchanges.

**ALIVE HOSPICE, INC.**

**Notes to the Financial Statements**

**December 31, 2015 and 2014**

**Level 2:** Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data. The Organization has no assets or liabilities measured at fair value using Level 2 inputs.

**Level 3:** Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability. The Organization has no assets or liabilities measured at fair value using Level 3 inputs.

In many cases, a valuation technique used to measure fair value includes inputs from multiple levels of the fair value hierarchy. The lowest level of significant input determines the placement of the entire fair value measurement in the hierarchy.

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 Organization'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.

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

**Fair Value Measurements as of  
December 31, 2015 using the following inputs**

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Money market funds	\$ 24,028	\$ -	\$ -	\$ 24,028
Bond funds	447,010	-	-	447,010
Equity mutual funds	878,738	-	-	878,738
Other mutual funds	<u>494,897</u>	<u>-</u>	<u>-</u>	<u>494,897</u>
<b>Total</b>	<b>\$ <u>1,844,673</u></b>	<b>\$ <u>-</u></b>	<b>\$ <u>-</u></b>	<b>\$ <u>1,844,673</u></b>

**Fair Value Measurements as of  
December 31, 2014 using the following inputs**

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Money market funds	\$ 87,376	\$ -	\$ -	\$ 87,376
Bond funds	472,469	-	-	472,469
Equity mutual funds	845,244	-	-	845,244
Other mutual funds	<u>572,219</u>	<u>-</u>	<u>-</u>	<u>572,219</u>
<b>Total</b>	<b>\$ <u>1,977,308</u></b>	<b>\$ <u>-</u></b>	<b>\$ <u>-</u></b>	<b>\$ <u>1,977,308</u></b>

# ALIVE HOSPICE, INC.

## Notes to the Financial Statements

December 31, 2015 and 2014

### (7) Investment in joint venture

During 2013, the Organization entered into a joint venture with another entity to form a practice management company. The Organization contributed approximately \$100,000 in cash to the joint venture during 2013 and had a 50% ownership interest as of December 31, 2014. The joint venture used the contributions by investors to help fund operations of a palliative care medical practice. As of December 31, 2014, the investment in joint venture amounted to \$101,063. During 2015 the Organization sold their interest in this investment for \$161,154.

Summary information for the management company (unaudited) as of December 31, 2014 and for the year then ended is as follows:

Total assets	\$	192,812
Total liabilities	\$	-
Net loss	\$	(2,991)

During 2015 the Organization entered into a participation agreement with Music City Kidney Care Alliance, LLC. The Organization paid \$1,000 in cash for a 1% ownership interest. The investment is accounted for under the cost method of accounting. No distributions were made from the joint venture during 2015.

### (8) Fund with Community Foundation of Middle Tennessee

The Organization has an agency endowment fund with the Community Foundation of Middle Tennessee (the "Community Foundation"). Earnings on this fund are designated for general operations and programs of the Organization. Total funds held by the Community Foundation, which are excluded from the assets of the Organization, amounted to \$96,792 and \$102,563 at December 31, 2015 and 2014, respectively. The Organization receives a 5% distribution annually from the fund.

### (9) Property and equipment

Property and equipment at December 31, 2015 and 2014 consisted of the following:

	<u>2015</u>	<u>2014</u>
Land and improvements	\$ 3,592,836	\$ 3,592,836
Buildings and improvements	11,371,841	11,283,811
Office furniture and equipment	3,659,859	3,355,571
Projects in progress	<u>491,202</u>	<u>53,428</u>
Total	19,115,738	18,285,646
Accumulated depreciation	<u>(8,351,581)</u>	<u>(7,831,866)</u>
Property and equipment, net	\$ <u>10,764,157</u>	\$ <u>10,453,780</u>

ALIVE HOSPICE, INC.

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Depreciation expense for the years ended December 31, 2015 and 2014 was \$519,729 and \$627,185, respectively.

Construction in progress at December 31, 2015 relates to construction of an inpatient facility in Murfreesboro, Tennessee as well as various other minor projects. The Murfreesboro project is expected to be complete in 2017, with an estimated cost to complete of \$8,000,000. The various other projects were completed in March 2016.

(10) Line of credit

The Organization maintains a \$2,500,000 line of credit with a financial institution which matures in June 2016. Interest only monthly payments are required, and any outstanding principal amounts drawn against the line would be due at maturity. The line of credit is secured by property of the Organization and carries an interest rate of 0.75% above the financial institution's prime rate resulting in a rate of 4.25% at December 31, 2015. The Organization had no borrowings outstanding on the line of credit at December 31, 2015 or 2014.

(11) Temporarily restricted net assets

Temporarily restricted net assets are either donor-restricted for specific purposes, or for use in a specified period of time. At December 31, 2015 and 2014, the restricted purposes are as follows:

	<u>2015</u>	<u>2014</u>
Endowment	\$ 474,175	\$ 531,930
Pledges	699,420	501,664
Other	<u>850,633</u>	<u>440,980</u>
	<u>\$ 2,024,228</u>	<u>\$ 1,474,574</u>

Temporarily restricted net assets were released from restriction for the years ended December 31, 2015 and 2014 for the following purposes:

	<u>2015</u>	<u>2014</u>
Pledges	\$ 50,335	\$ 173,421
Community education	-	9,177
Other	<u>259,868</u>	<u>30,176</u>
	<u>\$ 310,203</u>	<u>\$ 212,774</u>

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(12) Lease commitments

The Organization leases various office space, vehicles, and equipment under operating leases. Rent expense under these leases amounted to \$724,777 and \$990,395 in 2015 and 2014, respectively. A summary of approximate future minimum payments under these operating leases as of December 31, 2015 is as follows:

<u>Year</u>	<u>Amount</u>
2016	\$ 690,000
2017	256,000
2018	92,000
2019	<u>31,000</u>
	<u>\$ 1,069,000</u>

(13) Discontinued operations

During 2013, the Organization decided to discontinue providing palliative care services. GAAP requires that all components of an entity that have been disposed of and whose cash flows can be clearly distinguished from the rest of the entity be presented as discontinued operations. As such, the palliative care services have been presented in discontinued operations within the accompanying statements of operations and changes in net assets. No revenue was generated in 2015 and 2014 related to the palliative care operations.

(14) Retirement plan

The Organization sponsors a defined contribution 403(b) retirement plan. Employees meeting certain eligibility requirements can participate in the plan to the extent allowed under ERISA. The plan also provides for discretionary contributions by the Organization. Participants are immediately vested in their voluntary contributions plus related earnings; whereas, participants are fully vested in the Organization contributions plus related earnings after four years of service. The Organization made contributions of \$131,578 and \$126,878 to the plan in 2015 and 2014, respectively.

(15) Functional expenses

Expenses by functional classification for the years ended December 31, 2015 and 2014 are as follows:

	<u>2015</u>	<u>2014</u>
Program services	\$ 21,967,015	\$ 21,941,910
General and administrative	5,756,643	5,696,385
Fundraising	<u>481,593</u>	<u>418,741</u>
	<u>\$ 28,205,251</u>	<u>\$ 28,057,036</u>

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(16) Alive Institute

The non-operating expenses of \$594 and \$77,047 for the years ended December 31, 2015 and 2014, respectively, are associated with the Alive Institute. The Alive Institute is an initiative launched by the Organization to promote excellence and advance the field of hospice and palliative care. Through the Institute, the Organization shares its considerable gifts with the health care community and the community-at-large through education, research and advocacy with an initial focus on education and training.

(17) Endowment

Overview: The Organization's endowments consist of one fund that holds investments in securities traded on the public markets. The endowments are made up of temporarily restricted and permanently restricted assets. As required by GAAP, net assets associated with these endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law: The Organization's Board of Directors has determined the requirements of Tennessee's version of the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") to center around the preservation of the fair value of the original investment as of the date of the asset transfers. Investments resulting from donations directing that they be invested in perpetuity are classified as permanently restricted. The earnings generated by these investments are classified as unrestricted or temporarily restricted depending on the donors' stipulations. The temporarily restricted net assets are reclassified as unrestricted upon their appropriation for expenditure by the Organization in a manner consistent with the standard of prudence prescribed by Tennessee's version of UPMIFA. The Organization considers the following factors in making a determination to appropriate or accumulate its endowment funds:

- (1) The duration and preservation of the fund
- (2) The purposes of the Organization and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The expected total return from income and the appreciation of investments
- (6) Other resources of the Organization
- (7) The investment policies of the Organization

Return Objectives and Risk Parameters: The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowments while seeking to maintain the purchasing power of the endowment assets. Endowment assets include assets of donor-restricted funds that the Organization must hold in perpetuity. Under this policy, the endowment assets are invested in a manner that is intended to produce a moderate return while assuming a moderate level of investment risk.

ALIVE HOSPICE, INC.

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**Strategies Employed for Achieving Objectives:** To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

**Spending Policy and How the Investment Objectives Relate to Spending Policy:** The Organization disburses funds as needed within the guidelines of the endowments. Disbursements to the Organization are used to assist with its programs and services according to donor restrictions.

**Fund with Deficiencies:** From time to time, the fair value of assets associated with the individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Organization to retain as a fund of perpetual duration. Cumulative deficiencies of this nature that are in excess of related temporarily restricted amounts are reported in unrestricted net assets. There were no such deficiencies as of December 31, 2015 and 2014.

**Endowment Net Asset Composition by Type of Fund:** The Organization's composition of endowment assets for the years ended December 31, 2015 and 2014 is as follows:

<u>2015</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted	\$ <u>-</u>	\$ <u>474,175</u>	\$ <u>1,175,123</u>	\$ <u>1,649,298</u>
<u>2014</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted	\$ <u>-</u>	\$ <u>531,930</u>	\$ <u>1,175,123</u>	\$ <u>1,707,053</u>

Changes in endowment net assets for the years ended December 31, 2015 and 2014 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance at December 31, 2013	\$ -	\$ 489,713	\$ 1,164,123	\$ 1,653,836
Interest and dividends	-	25,773	-	25,773
Net gains	-	16,444	-	16,444
Additions	<u>-</u>	<u>-</u>	<u>11,000</u>	<u>11,000</u>
Balance at December 31, 2014	-	531,930	1,175,123	1,707,053
Interest and dividends	-	23,061	-	23,061
Net losses	<u>-</u>	<u>(80,816)</u>	<u>-</u>	<u>(80,816)</u>
Balance at December 31, 2015	\$ <u>-</u>	\$ <u>474,175</u>	\$ <u>1,175,123</u>	\$ <u>1,649,298</u>

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**(18) Related party transactions**

The Organization had a receivable of approximately \$72,000 at December 31, 2014, due from an affiliate related to an employee lease agreement. This receivable is included in other current assets on the statement of financial position at December 31, 2014. During 2015 and in conjunction with the sale of the investment in joint venture, the employee lease agreement was terminated and the receivable was collected.

At December 31, 2015, the Organization has pledges receivable of \$470,000 due from related parties.

**(19) Department of Justice settlement**

The Organization was served with a qui tam complaint which alleged the Organization violated the False Claims Act by improperly providing patients with a general inpatient level of care who did not qualify for the general inpatient level of care. In September 2015, the Organization reached a settlement agreement with the Department of Justice regarding these allegations. Based upon the terms of the settlement agreement, the Organization paid approximately \$1,600,000 in September 2015, which has been included within accrued expenses in the accompanying statement of financial position as of December 31, 2014. The Organization also recorded a receivable of \$400,000, at December 31, 2014, related to the settlement which represents the agreed upon insurance reimbursement. The receivable is included with other current assets in the accompanying statement of financial position as of December 31, 2014 and was collected in 2015.

**(20) 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 Organization is insured with respect to medical malpractice risk on a claims-made basis. The Organization also maintains insurance for general liability, director and officer liability and property. Certain policies are subject to deductibles. Management is not aware of any claims against the Organization which would have a material financial impact.

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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, and Medicare 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 repayments for patient services previously billed. Management continues to implement policies, procedures, and compliance overview organizational structure to enforce and monitor compliance with the Health Insurance Portability and Accountability Act of 1996 and other government statutes and regulations. The Organization's compliance with such laws and regulations is subject to future government review and interpretations, as well as regulatory actions which are unknown or unasserted at this time. Management believes that the Organization is in compliance with fraud and abuse statutes, as well as other applicable government laws and regulations.

*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 Organization is subject to legal proceedings and claims that arise in the ordinary course of business. However, management believes the amount of potential liability with respect to these actions will not have a material impact on the Organization's financial position, results of operations or cash flows.