

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

Consolidated Financial Statements and Schedules

December 31, 2017 and 2016

(With Independent Auditors' Report Thereon)



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 - 22
Schedules:	
Consolidating Statement of Financial Position	23
Consolidating Statement of Activities	24

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, 2017 and 2016, 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, 2017 and 2016, 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 and statements of activities 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.

LBMC, PC

Brentwood, Tennessee
May 16, 2018

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Financial Position

December 31, 2017 and 2016

	<u>Assets</u>	
	<u>2017</u>	<u>2016</u>
Current assets:		
Cash and cash equivalents, including cash designated for debt service of \$3,588,966 in 2016	\$ 10,102,563	\$ 11,588,328
Accounts receivable for services, less allowance for doubtful accounts of \$906,872 in 2017 and \$832,048 in 2016	4,678,325	5,104,894
Contributions receivable, less allowance for uncollectible pledges of \$18,000 in 2017 and \$16,250 in 2016	101,662	138,170
Other current assets	<u>320,398</u>	<u>230,418</u>
Total current assets	15,202,948	17,061,810
Property and equipment, net	20,323,917	19,966,301
Contributions receivable, excluding current portion	79,450	151,920
Investments	3,572,361	2,721,052
Beneficial interest in perpetual trust	<u>562,261</u>	<u>509,279</u>
	<u>\$ 39,740,937</u>	<u>\$ 40,410,362</u>
	<u>Liabilities and Net Assets</u>	
Current liabilities:		
Current installments of long-term debt	\$ 866,750	\$ 4,449,740
Fair value of interest rate swap agreement	-	43,698
Accounts payable	330,708	612,340
Accrued expenses	<u>1,299,476</u>	<u>1,091,052</u>
Total current liabilities	2,496,934	6,196,830
Long-term debt, excluding current installments	<u>1,647,398</u>	<u>2,548,184</u>
Total liabilities	<u>4,144,332</u>	<u>8,745,014</u>
Net assets:		
Unrestricted	31,950,244	28,610,981
Temporarily restricted	3,084,100	2,545,088
Permanently restricted	<u>562,261</u>	<u>509,279</u>
Total net assets	<u>35,596,605</u>	<u>31,665,348</u>
	<u>\$ 39,740,937</u>	<u>\$ 40,410,362</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Activities

Years ended December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Changes in unrestricted net assets:		
Public support and revenue:		
Patient service revenue, net	\$ 31,419,169	\$ 31,850,480
Contributions	237,500	288,167
Investment income	81,131	45,377
Other	<u>655,139</u>	<u>466,775</u>
Total public support and revenue	32,392,939	32,650,799
Satisfaction of restrictions	<u>896,272</u>	<u>1,023,653</u>
Total unrestricted public support and revenue	<u>33,289,211</u>	<u>33,674,452</u>
Expenses:		
Program services:		
Clinical services	16,741,506	15,102,453
Ancillary services	<u>5,370,276</u>	<u>5,287,321</u>
Total program services	22,111,782	20,389,774
Supporting services:		
Administrative and fiscal	5,305,940	4,846,749
Marketing and public relations	<u>2,575,924</u>	<u>2,747,015</u>
Total supporting services	7,881,864	7,593,764
Gain on interest rate swap agreement	<u>(43,698)</u>	<u>(109,359)</u>
Total expenses	<u>29,949,948</u>	<u>27,874,179</u>
Increase in unrestricted net assets	<u>3,339,263</u>	<u>5,800,273</u>
Changes in temporarily restricted net assets:		
Contributions	1,173,964	1,134,379
Investment income	243,908	137,065
Net assets released from restrictions	<u>(878,860)</u>	<u>(999,426)</u>
Increase in temporarily restricted net assets	<u>539,012</u>	<u>272,018</u>
Changes in permanently restricted net assets:		
Investment income	70,394	28,924
Income distributed	<u>(17,412)</u>	<u>(24,227)</u>
Increase in permanently restricted net assets	<u>52,982</u>	<u>4,697</u>
Increase in net assets	3,931,257	6,076,988
Net assets at beginning of year	<u>31,665,348</u>	<u>25,588,360</u>
Net assets at end of year	\$ <u>35,596,605</u>	\$ <u>31,665,348</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidated Statements of Cash Flows

Years ended December 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities:		
Increase in net assets	\$ 3,931,257	\$ 6,076,988
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	1,362,034	1,224,398
Provision for doubtful accounts	1,379,985	749,613
Provision for uncollectible pledges	1,750	2,750
Loss on sale of property and equipment	(650)	21,843
Net gain on investments	(350,232)	(178,618)
Gain on interest rate swap agreement	(43,698)	(109,359)
(Increase) decrease in operating assets:		
Accounts receivable for services	(953,416)	(2,102,842)
Contributions receivable	107,228	(261,794)
Other current assets	(89,980)	(19,359)
Increase (decrease) in operating liabilities:		
Accounts payable	(281,632)	212,644
Accrued expenses	<u>208,424</u>	<u>339,228</u>
Total adjustments	<u>1,339,813</u>	<u>(121,496)</u>
Net cash provided by operating activities	<u>5,271,070</u>	<u>5,955,492</u>
Cash flows from investing activities:		
Proceeds from disposal of property and equipment	650	-
Purchases of property and equipment	(1,719,650)	(4,914,304)
Proceeds from sale of investments	56,653	67,951
Purchases of investments	<u>(610,712)</u>	<u>(333,627)</u>
Net cash used by investing activities	<u>(2,273,059)</u>	<u>(5,179,980)</u>
Cash flows from financing activities:		
Repayments on long-term debt	(4,483,776)	(593,755)
Proceeds from long-term debt	<u>-</u>	<u>2,542,000</u>
Net cash provided (used) by financing activities	<u>(4,483,776)</u>	<u>1,948,245</u>
Increase (decrease) in cash and cash equivalents	(1,485,765)	2,723,757
Cash and cash equivalents at beginning of year	<u>11,588,328</u>	<u>8,864,571</u>
Cash and cash equivalents at end of year	\$ <u>10,102,563</u>	\$ <u>11,588,328</u>
Supplemental disclosure of cash flow information:		
Cash paid during the year for:		
Interest	\$ <u>130,704</u>	\$ <u>243,180</u>

See accompanying notes to the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

(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.

(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, 2017 and 2016

(c) Investments

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

(d) Receivables and credit policies

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

(e) Property and equipment

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

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

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

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

(f) Income taxes

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

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

As of December 31, 2017 and 2016, 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.

(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 \$611,000 and \$495,000 in 2017 and 2016, respectively.

Cash contributions are generally recognized as revenue when received.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

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

(h) Advertising and promotion costs

Advertising and promotion costs are expensed as incurred and amounted to \$510,599 and \$483,620 during 2017 and 2016, respectively.

(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

During 2016 and through May 2017, the Foundation used 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 was to stabilize cash flow requirements by maintaining interest rate swap contracts to convert variable-rate debt to a fixed rate. The interest rate swap agreement matured in May 2017.

(k) Fundraising costs

For the years ended December 31, 2017 and 2016, expenses totaling \$353,795 and \$299,865, respectively, were associated with fundraising and are classified in the consolidated statements of activities under marketing and public relations.

(l) Events occurring after reporting date

The Organizations have evaluated events and transactions that occurred between December 31, 2017 and May 16, 2018 which is the date that the consolidated financial statements were available to be issued, for possible recognition or disclosure in the consolidated financial statements.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

(3) Credit risk and other concentrations

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

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

The Foundation provides rehabilitation treatment for individuals with alcohol and other chemical dependencies under various payor programs. Accordingly, the concentration of accounts receivable and revenue as of and for the years ended December 31, 2017 and 2016, is summarized as follows:

	<u>2017</u>		<u>2016</u>	
	<u>Accounts Receivable</u>	<u>Revenue</u>	<u>Accounts Receivable</u>	<u>Revenue</u>
Blue Cross/Magellan	33 %	43 %	42 %	52 %
Other private insurance	37	44	34	35
Individuals	<u>30</u>	<u>13</u>	<u>24</u>	<u>13</u>
	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>	<u>100 %</u>

(4) Assets and liabilities measured at fair value

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

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

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

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, 2017 and 2016.

- (i) *Mutual funds*: Valued at the net asset value of shares held by the Foundation at year end based on quoted prices in an active market.
- (ii) *Equity securities*: Valued at the closing price reported on the active market on which the individual securities are traded.

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, 2017 and 2016

The following table sets forth by level, within the fair value hierarchy, the Foundation's assets at fair value as of December 31, 2017 and 2016:

	<u>2017</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Cash held in interest program	\$ <u>22,309</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>22,309</u>
Mutual funds:				
Fixed income	1,180,879	-	-	1,180,879
Domestic index	147,977	-	-	147,977
International	<u>187,345</u>	<u>-</u>	<u>-</u>	<u>187,345</u>
	<u>1,516,201</u>	<u>-</u>	<u>-</u>	<u>1,516,201</u>
Equity securities:				
Consumer	623,939	-	-	623,939
Industrial and energy	499,441	-	-	499,441
Information	238,246	-	-	238,246
Healthcare	307,020	-	-	307,020
Telecommunications and utilities	60,109	-	-	60,109
Other	<u>305,096</u>	<u>-</u>	<u>-</u>	<u>305,096</u>
	<u>2,033,851</u>	<u>-</u>	<u>-</u>	<u>2,033,851</u>
Beneficial interest in perpetual trust	<u>562,261</u>	<u>-</u>	<u>-</u>	<u>562,261</u>
Total	\$ <u>4,134,622</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>4,134,622</u>
	<u>2016</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Cash held in interest program	\$ <u>145,667</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>145,667</u>
Mutual funds:				
Fixed income	747,939	-	-	747,939
Domestic index	130,762	-	-	130,762
International	<u>100,467</u>	<u>-</u>	<u>-</u>	<u>100,467</u>
	<u>979,168</u>	<u>-</u>	<u>-</u>	<u>979,168</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

Equity securities:

Consumer	514,832	-	-	514,832
Industrial and energy	410,932	-	-	410,932
Information	157,142	-	-	157,142
Healthcare	284,086	-	-	284,086
Telecommunications and utilities	57,738	-	-	57,738
Other	<u>171,487</u>	<u>-</u>	<u>-</u>	<u>171,487</u>
	<u>1,596,217</u>	<u>-</u>	<u>-</u>	<u>1,596,217</u>
 Beneficial interest in perpetual trust	 <u>509,279</u>	 <u>-</u>	 <u>-</u>	 <u>509,279</u>
 Total	 <u>\$ 3,230,331</u>	 <u>\$ -</u>	 <u>\$ -</u>	 <u>\$ 3,230,331</u>

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

(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>2017</u>	<u>2016</u>
Receivable in less than one year	\$ 119,662	\$ 154,420
Receivable in one to five years	<u>85,279</u>	<u>157,749</u>
	204,941	312,169
Less allowance for uncollectible pledges	(18,000)	(16,250)
Less discount	<u>(5,829)</u>	<u>(5,829)</u>
	<u>\$ 181,112</u>	<u>\$ 290,090</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

(6) Investments

A summary of the fair value of investments as of December 31, 2017 and 2016 is as follows:

	<u>2017</u>	<u>2016</u>
Cash held in interest program	\$ 22,309	\$ 145,667
Mutual funds	1,516,201	979,168
Equity securities	<u>2,033,851</u>	<u>1,596,217</u>
	<u>\$ 3,572,361</u>	<u>\$ 2,721,052</u>

As of December 31, 2016, the fair value of invested assets assigned to permanently restricted endowment net asset balances required to be maintained in perpetuity had a deficiency of \$31,823. There was no deficiency at December 31, 2017.

(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 and receives annual cash distributions from the trust. 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 \$562,261 and \$509,279 at December 31, 2017 and 2016, 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 in the consolidated statements of activities for 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Interest and dividend income	\$ 90,066	\$ 69,244
Net gain on investments	350,232	178,618
Fees paid	<u>(44,865)</u>	<u>(36,496)</u>
	<u>\$ 395,433</u>	<u>\$ 211,366</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

(9) Property and equipment

A summary of property and equipment as of December 31, 2017 and 2016 is as follows:

	<u>2017</u>	<u>2016</u>
Land	\$ 1,150,857	\$ 1,118,957
Buildings and improvements	30,260,708	26,411,376
Machinery and equipment	2,181,336	2,111,431
Transportation equipment	289,190	249,393
Furniture and fixtures	925,936	910,831
Construction in progress	<u>425,638</u>	<u>2,714,828</u>
	35,233,665	33,516,816
Accumulated depreciation and amortization	<u>(14,909,748)</u>	<u>(13,550,515)</u>
	<u>\$ 20,323,917</u>	<u>\$ 19,966,301</u>

Depreciation and amortization expense amounted to approximately \$1,362,000 and \$1,225,000 for the years ended December 31, 2017 and 2016, respectively.

Construction in progress primarily consists of amounts incurred relating to the ARCH Academy project. At December 31, 2017, the estimated cost to complete all projects was approximately \$7,100,000.

(10) Lines of credit

At December 31, 2017, the Foundation had a \$950,000 revolving line of credit, payable on demand, which matures August 25, 2018. There were no borrowings on the line at December 31, 2017 and 2016. Borrowings under the line bear interest, payable monthly, at an annual interest rate equal to the one-month LIBOR plus 1.50 percentage points over the index. The line of credit is secured by accounts receivable.

The Foundation converted a non-revolving line of credit arrangement to a note payable on July 1, 2016, with a principal balance of \$1,167,000 (see Note 11).

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

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

(11) Long-term debt

A summary of long-term debt as of December 31, 2017 and 2016 is as follows:

	<u>2017</u>	<u>2016</u>
Note payable to bank in connection with \$9,991,000 Series 2007 Health Facilities Bonds issued by the Metropolitan Government of Nashville and Davidson County, Tennessee; due in monthly principal installments ranging from \$9,818 to \$13,208 plus interest at a variable rate based on the 30-day LIBOR rate (1.35% at December 31, 2016) through May 15, 2017, at which time the note payable was paid in full.	\$ -	\$ 3,641,340
Note payable to bank due in monthly installments of \$8,333 plus interest at a fixed rate of 2.68% per annum through May 28, 2019.	141,666	241,666
Note payable to bank due in monthly installments of \$16,333 plus interest at a fixed rate of 2.96% per annum through August 1, 2020.	533,334	733,333
Note payable to bank due in monthly installments of \$16,667 plus interest at a fixed rate of 2.75% per annum through August 1, 2020.	899,564	1,167,000
Note payable to bank due in monthly installments of \$22,917 plus interest at a fixed rate of 2.90% per annum through April 1, 2021.	<u>939,584</u>	<u>1,214,585</u>
Total	2,514,148	6,997,924
Less current installments	<u>866,750</u>	<u>4,449,740</u>
Long-term debt, excluding current installments	\$ <u><u>1,647,398</u></u>	\$ <u><u>2,548,184</u></u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

A summary of future maturities of long-term debt as of December 31, 2017 is as follows:

<u>Year</u>	<u>Amount</u>
2018	\$ 866,750
2019	750,067
2020	641,734
2021	<u>255,597</u>
	\$ <u>2,514,148</u>

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

(12) Interest rate swap agreement

In May 2007, the Foundation entered into an interest rate swap agreement with a commercial bank to reduce the impact of changes in interest rates on its taxable revenue bond Series 2007. Under the interest rate swap agreement, which was classified as a cash flow hedge, the Foundation paid interest at a fixed rate of 3.39% and received interest at 70% of the one-month LIBOR plus 1.24%. The agreement terminated and was settled in May 2017 and had an original notional amount of \$9,991,000. 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, 2016, the settlement value, which approximates fair value, of the agreement was \$43,698. The change in the estimated settlement value of the interest rate swap agreement of \$43,698 and \$109,359 during the years ended December 31, 2017 and 2016, respectively, is reported as a gain in the consolidated statements of activities.

(13) Net assets

As of December 31, 2017 and 2016, the Board of Directors had designated \$882,177 and \$711,997, 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%).

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

Composition of and changes in endowment net assets by type of fund as of December 31, 2017 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	\$ -	\$ 2,690,183	\$ 562,261	\$ 3,252,444
Board-designated endowment funds	<u>882,178</u>	<u>-</u>	<u>-</u>	<u>882,178</u>
Total funds	<u>\$ 882,178</u>	<u>\$ 2,690,183</u>	<u>\$ 562,261</u>	<u>\$ 4,134,622</u>
Endowment net assets, beginning of year	\$ 711,997	\$ 2,009,055	\$ 509,279	\$ 3,230,331
Contributions	109,590	501,372	-	610,962
Amounts appropriated for expenditure	(20,540)	(64,152)	(17,412)	(102,104)
Gain on investment, net	<u>81,131</u>	<u>243,908</u>	<u>70,394</u>	<u>395,433</u>
Endowment net assets, end of year	<u>\$ 882,178</u>	<u>\$ 2,690,183</u>	<u>\$ 562,261</u>	<u>\$ 4,134,622</u>

Composition of and changes in endowment net assets by type of fund as of December 31, 2016 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	\$ -	\$ 2,009,055	\$ 509,279	\$ 2,518,334
Board-designated endowment funds	<u>711,997</u>	<u>-</u>	<u>-</u>	<u>711,997</u>
Total funds	<u>\$ 711,997</u>	<u>\$ 2,009,055</u>	<u>\$ 509,279</u>	<u>\$ 3,230,331</u>
Endowment net assets, beginning of year	\$ 516,634	\$ 1,764,821	\$ 504,582	\$ 2,786,037
Contributions	178,587	155,040	-	333,627
Amounts appropriated for expenditure	(28,601)	(47,871)	(24,227)	(100,699)
Gain on investment, net	<u>45,377</u>	<u>137,065</u>	<u>28,924</u>	<u>211,366</u>
Endowment net assets, end of year	<u>\$ 711,997</u>	<u>\$ 2,009,055</u>	<u>\$ 509,279</u>	<u>\$ 3,230,331</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

Temporarily restricted net assets as of December 31, 2017 and 2016 are available for the following purposes:

	<u>2017</u>	<u>2016</u>
Patient assistance (including endowment net assets of \$2,690,183 and \$2,009,055 at December 31, 2017 and 2016, respectively)	\$ 2,885,097	\$ 2,228,518
Other specific operational programs	<u>199,003</u>	<u>316,570</u>
	<u>\$ 3,084,100</u>	<u>\$ 2,545,088</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, 2017 and 2016 is as follows:

	<u>2017</u>	<u>2016</u>
Olcott Foundation	\$ <u>562,261</u>	\$ <u>509,279</u>

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

(14) Natural classification of expenses

A summary of the natural classification of expenses for the years ended December 31, 2017 and 2016 is as follows:

	<u>2017</u>	<u>2016</u>
Salaries and temporary labor	\$ 18,718,731	\$ 18,012,006
Contract services	1,293,079	1,060,583
Provision for doubtful accounts	1,379,985	749,613
Depreciation and amortization	1,362,034	1,224,398
Interest, including swap agreement	87,005	133,822
General insurance	494,218	560,758
Utilities	695,700	653,467
Food service	971,524	985,730
Supplies	678,322	686,894
Other	<u>4,269,350</u>	<u>3,806,908</u>
	<u>\$ 29,949,948</u>	<u>\$ 27,874,179</u>

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

(15) Profit-sharing plan

Eligible employees of the Foundation may participate in the Cumberland Heights 401(k) Retirement Plan (the "Plan"). Employees are generally eligible after they reach age 20 1/2 and are employed for three months. The Foundation matches salary deferral contributions equal to 100% of salary contributions up to 5% of compensation. The Foundation made contributions of \$355,131 and \$317,886 to the Plan in 2017 and 2016, respectively.

(16) Lease commitments

The Foundation leases office space and various office equipment under operating leases. Rent expense under these leases amounted to \$429,357 and \$391,257 in 2017 and 2016, respectively.

A summary of approximate future minimum payments under these leases as of December 31, 2017 is as follows:

<u>Year</u>	<u>Amount</u>
2018	\$ 425,000
2019	260,000
2020	119,000
2021	56,000
2022	<u>52,000</u>
	<u>\$ 912,000</u>

(17) 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.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

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.

Healthcare Reform

The health care industry in the United States is subject to fundamental changes due to ongoing health care reform efforts and related political, economic and regulatory influences. Notably, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 ("collectively, the "Affordable Care Act") resulted in expanded health care coverage to millions of previously uninsured people beginning in 2014 and has resulted in significant changes to the U.S. health care system. To help fund this expansion, the Affordable Care Act outlines certain reductions in Medicare reimbursements for various health care providers, as well as certain other changes to Medicare payment methodologies. This comprehensive health care legislation has resulted and will continue to result in extensive rulemaking by regulatory authorities, and also may be altered, amended, repealed, or replaced. It is difficult to predict the full impact of the Affordable Care Act due to the complexity of the law and implementing regulations, as well as the Foundation's inability to foresee how CMS and other participants in the health care industry will respond to the choices available to them under the law. The Foundation also cannot accurately predict whether any new or pending legislative proposals will be adopted or, if adopted, what effect, if any, these proposals would have on the Foundation's business. Similarly, while the Foundation can anticipate that some of the rulemaking that will be promulgated by regulatory authorities will affect the Foundation's business and the manner in which the Foundation is reimbursed by the federal health care programs, the Foundation cannot accurately predict today the impact of those regulations on the Foundation's business. The provisions of the legislation and other regulations implementing the provisions of the Affordable Care Act or any amended or replacement legislation may increase costs, decrease revenues, expose the Foundation to expanded liability or require the Foundation to revise the ways in which it conducts business.

In addition to its impact on the delivery and payment for health care, the Affordable Care Act and the implementing regulations have resulted in and may continue to result in increases to the Foundation's costs to provide health care benefits to its employees. The Foundation also may be required to make additional employee-related changes to its business as a result of provisions in the Affordable Care Act or any amended or replacement legislation impacting the provision of health insurance by employers, which could result in additional expense and adversely affect the Foundation's results of operations and cash flow.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Notes to the Consolidated Financial Statements

December 31, 2017 and 2016

Litigation

The Foundation and Affiliate are involved in various legal actions arising in the normal course of business. In the opinion of management, such matters will not have a material adverse effect on the Foundation's consolidated financial position or consolidated 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.

(18) 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.

(19) Subsequent event

In March 2018, the Foundation entered into a note payable to a bank in connection with \$6,000,000 Series 2018 Revenue Bonds issued by the Industrial Development Board of Cheatham County for the purpose of constructing a recovery treatment and rehabilitation center in Pegram, Tennessee.

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidating Statement of Financial Position

December 31, 2017

Assets	Cumberland Heights Foundation, Inc.	Cumberland Heights Professional Associates, Inc.	Eliminating Entries		Consolidated
			Debit	Credit	
Current assets:					
Cash and cash equivalents	\$ 9,756,832	\$ 345,731	\$ -	\$ -	\$ 10,102,563
Accounts receivable for services, net	4,526,628	151,697	-	-	4,678,325
Receivable from related parties	(6,173)	-	6,173 (a)	-	-
Contributions receivable, net	101,662	-	-	-	101,662
Other current assets	311,225	9,173	-	-	320,398
Total current assets	14,690,174	506,601	6,173	-	15,202,948
Property and equipment, net	20,323,917	-	-	-	20,323,917
Contributions receivable, excluding current portion	79,450	-	-	-	79,450
Investments	3,572,361	-	-	-	3,572,361
Beneficial interest in perpetual trust	562,261	-	-	-	562,261
	<u>\$ 39,228,163</u>	<u>\$ 506,601</u>	<u>\$ 6,173</u>	<u>\$ -</u>	<u>\$ 39,740,937</u>
Liabilities and Net Assets					
Current liabilities:					
Current installments of long term debt	\$ 866,750	\$ -	\$ -	\$ -	\$ 866,750
Accounts payable	287,555	36,980	- (a)	6,173	330,708
Accrued expenses	1,268,788	30,688	-	-	1,299,476
Total current liabilities	2,423,093	67,668	-	6,173	2,496,934
Long-term debt, excluding current installments	1,647,398	-	-	-	1,647,398
Total liabilities	4,070,491	67,668	-	6,173	4,144,332
Net assets					
Unrestricted	31,511,311	438,933	-	-	31,950,244
Temporarily restricted	3,084,100	-	-	-	3,084,100
Permanently restricted	562,261	-	-	-	562,261
Total net assets	35,157,672	438,933	-	-	35,596,605
	<u>\$ 39,228,163</u>	<u>\$ 506,601</u>	<u>\$ -</u>	<u>\$ 6,173</u>	<u>\$ 39,740,937</u>

(a) To eliminate intercompany receivables and payables.

See independent auditors' report

CUMBERLAND HEIGHTS FOUNDATION, INC. AND AFFILIATE

Consolidating Statement of Activities

Year ended December 31, 2017

	Cumberland Heights Foundation, Inc.	Cumberland Heights Professional Associates, Inc.	Eliminating Entries		Consolidated
			Debit	Credit	
Changes in unrestricted net assets:					
Public support and revenue:					
Patient service revenue, net	\$ 30,648,581	\$ 770,588	\$ -	\$ -	\$ 31,419,169
Contributions	237,500	-	-	-	237,500
Investment income	81,131	-	-	-	81,131
Other	655,139	120,000 (a)	120,000	-	655,139
Total public support and revenue	31,622,351	890,588	120,000	-	32,392,939
Satisfaction of restrictions	896,272	-	-	-	896,272
Total unrestricted public support and revenue	32,518,623	890,588	120,000	-	33,289,211
Expenses:					
Program services:					
Clinical services	15,955,473	786,033	-	-	16,741,506
Ancillary services	5,366,269	4,007	-	-	5,370,276
Total program services	21,321,742	790,040	-	-	22,111,782
Supporting services:					
Administrative and fiscal	5,420,559	5,381	- (a)	120,000	5,305,940
Marketing and public relations	2,575,924	-	-	-	2,575,924
Total supporting services	7,996,483	5,381	-	120,000	7,881,864
Gain on interest rate swap agreement	(43,698)	-	-	-	(43,698)
Total expenses	29,274,527	795,421	-	120,000	29,949,948
Increase in unrestricted net assets	3,244,096	95,167	120,000	120,000	3,339,263
Changes in temporarily restricted net assets:					
Contributions	1,173,964	-	-	-	1,173,964
Investment income	243,908	-	-	-	243,908
Net assets released from restrictions	(878,860)	-	-	-	(878,860)
Increase in temporarily restricted net assets	539,012	-	-	-	539,012
Changes in permanently restricted net assets					
Investment income	70,394	-	-	-	70,394
Income distributed	(17,412)	-	-	-	(17,412)
Increase in permanently restricted net assets	52,982	-	-	-	52,982
Increase in net assets	3,836,090	95,167	120,000	120,000	3,931,257
Net assets at beginning of year	31,321,582	343,766	-	-	31,665,348
Net assets at end of year	\$ 35,157,672	\$ 438,933	\$ 120,000	\$ 120,000	\$ 35,596,605

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

See independent auditors' report