

**ALIVE HOSPICE, INC.
FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT
YEARS ENDED DECEMBER 31, 2005 AND 2004**

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BLANKENSHIP CPA GROUP, PLLC
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Alive Hospice, Inc.

We have audited the accompanying statements of financial position of Alive Hospice, Inc. (a Tennessee not for profit organization) as of December 31, 2005 and 2004, and the related statements of financial position, changes in net assets, functional expenses and cash flows for the years then ended. These financial statements are the responsibility of Alive Hospice, Inc.'s management. 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our 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, 2005 and 2004, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Blankenship CPA Group, PLLC

February 2, 2006

ALIVE HOSPICE, INC.
STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2005 AND 2004

ASSETS	2005	2004
Cash and cash equivalents:		
Unrestricted	\$ 3,767,589	\$ 2,676,930
Endowment	51,289	37,747
Board designated	-	160,980
Board restricted	963,158	830,524
Donor restricted	46,870	50,474
Total cash and cash equivalents	<u>4,828,906</u>	<u>3,756,655</u>
Investments:		
Permanently restricted	1,000,000	1,000,000
Endowment	80,440	73,141
Board designated	277,398	273,468
Total investments	<u>1,357,838</u>	<u>1,346,609</u>
Accounts receivable, less allowance for doubtful accounts of \$446,776 in 2005 and \$342,785 in 2004	4,274,848	3,108,925
Contributions receivable:		
Unrestricted	167,426	-
Board designated	-	81,897
Donor restricted	115,000	169,394
Total contributions receivable	<u>282,426</u>	<u>251,291</u>
Prepaid expenses	147,003	29,124
Other current assets	143,462	38,157
Land, buildings and equipment, net	9,953,448	9,936,611
Goodwill	623,093	-
Total assets	<u>\$ 21,611,024</u>	<u>\$ 18,467,372</u>
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable	\$ 825,073	\$ 579,322
Accrued expenses	1,597,885	1,182,883
Bonds interest payable	9,018	13,426
Bonds payable	2,200,000	2,200,000
Total liabilities	<u>4,631,976</u>	<u>3,975,631</u>
Net assets:		
Unrestricted:		
Undesignated	15,408,051	12,644,640
Board designated	277,398	516,345
Total unrestricted net assets	<u>15,685,449</u>	<u>13,160,985</u>
Temporarily restricted	293,599	330,756
Permanently restricted	1,000,000	1,000,000
Total net assets	<u>16,979,048</u>	<u>14,491,741</u>
Total liabilities and net assets	<u>\$ 21,611,024</u>	<u>\$ 18,467,372</u>

The accompanying notes are an integral part of these financial statements.

ALIVE HOSPICE, INC.
STATEMENTS OF CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2005 AND 2004

	2005	2004
Unrestricted net assets:		
Revenue, gains and other support:		
Net patient service revenue	\$ 20,659,343	\$ 17,158,313
Contributions	1,490,877	808,716
United Way	324,588	305,318
Investment income	2,968	52,183
Other	106,297	109,596
Net assets released from restrictions	<u>379,992</u>	<u>251,312</u>
Total revenue, gains and other support	<u>22,964,065</u>	<u>18,685,438</u>
Expenses:		
Program services	16,089,238	13,925,894
Management and general	3,826,165	3,071,030
Fundraising	<u>524,198</u>	<u>487,702</u>
Total expenses	<u>20,439,601</u>	<u>17,484,626</u>
Change in unrestricted net assets	2,524,464	1,200,812
Unrestricted net assets, beginning of year	<u>13,160,985</u>	<u>11,960,173</u>
Unrestricted net assets, end of year	<u>15,685,449</u>	<u>13,160,985</u>
Temporarily restricted net assets:		
Contributions	259,122	314,604
Investment income, net	83,713	36,265
Net assets released from restriction	<u>(379,992)</u>	<u>(251,312)</u>
Change in temporarily restricted net assets	(37,157)	99,557
Temporarily restricted net assets, beginning of year	<u>330,756</u>	<u>231,199</u>
Temporarily restricted net assets, end of year	<u>293,599</u>	<u>330,756</u>
Change in net assets	2,487,307	1,300,369
Net assets, beginning of year	<u>14,491,741</u>	<u>13,191,372</u>
Net assets, end of year	<u><u>\$ 16,979,048</u></u>	<u><u>\$ 14,491,741</u></u>

The accompanying notes are an integral part of these financial statements.

ALIVE HOSPICE, INC.
STATEMENTS OF FUNCTIONAL EXPENSES
YEARS ENDED DECEMBER 31, 2005 AND 2004

	2005			2004
	Program Services	Management and General	Fund -raising	Total
Salaries	\$ 6,537,096	\$ 1,966,392	\$ 137,967	\$ 8,641,455
Direct patient care	5,783,399	-	-	5,783,399
Benefits and workers comp	1,226,411	321,235	-	1,547,646
Payroll taxes	466,478	139,954	10,169	616,601
Depreciation	240,646	231,098	35	471,779
Mileage	427,699	43,570	460	471,729
Facility and grounds maintenance	388,090	67,814	1,328	457,232
Medical supplies	331,124	-	-	331,124
Professional fees	6,896	281,352	-	288,248
Office and program supplies	45,179	104,121	47,979	197,279
Telephone	126,554	70,600	-	197,154
Utilities	140,179	40,337	-	180,516
Advertising	-	32,807	146,619	179,426
Equipment rental and maintenance	-	154,073	-	154,073
Interest, fees, and bond expense	-	176	143,547	143,723
Conferences and workshops	34,817	90,589	5,270	130,676
Bad debt expense	33,606	86,472	-	120,078
Insurance	76,899	32,395	24	109,318
Printing and publications	36,932	37,537	17,392	91,861
Dietary supplies	82,977	-	-	82,977
Rent	71,722	7,591	1,246	80,559
Dues and licenses	9,441	58,097	940	68,478
Other operating expenses	16,823	38,364	20	55,207
Postage	6,270	21,591	11,202	39,063
Total expenses	<u>\$ 16,089,238</u>	<u>\$ 3,826,165</u>	<u>\$ 524,198</u>	<u>\$ 20,439,601</u>
				<u>\$ 17,484,626</u>

The accompanying notes are an integral part of these financial statements.

ALIVE HOSPICE, INC.
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2005 AND 2004

	2005	2004
Cash flows from operating activities:		
Change in net assets	\$ 2,487,307	\$ 1,300,369
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	471,779	417,240
Net realized and unrealized losses (gains) on investments	6,796	(45,181)
Loss on disposal of land, buildings and equipment	-	356
(Increase) decrease in:		
Accounts receivable	(1,165,923)	(496,700)
Contributions receivable	(31,135)	54,173
Prepaid expenses	(117,879)	(355)
Other current assets	(105,305)	-
Increase (decrease) in:		
Accounts payable	245,751	41,240
Accrued expenses	415,002	199,882
Bonds interest payable	(4,408)	1,916
Net cash provided by operating activities	<u>2,201,985</u>	<u>1,472,940</u>
Cash flows from investing activities:		
Purchases of investments	(301,314)	(590,796)
Proceeds from sales of investments	283,289	482,671
Capital expenditures and purchase of goodwill	(1,111,709)	(359,200)
Net cash used in investing activities	<u>(1,129,734)</u>	<u>(467,325)</u>
Cash flows from financing activities:		
Payments on bonds	-	(240,000)
Net cash used in financing activities	<u>-</u>	<u>(240,000)</u>
Net increase in cash and cash equivalents	1,072,251	765,615
Cash and cash equivalents, beginning of year	<u>3,756,655</u>	<u>2,991,040</u>
Cash and cash equivalents, end of year	<u>\$ 4,828,906</u>	<u>\$ 3,756,655</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest	<u>\$ 114,029</u>	<u>\$ 134,273</u>

The accompanying notes are an integral part of these financial statements.

ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2005 AND 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

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

Basis of Presentation

The Organization is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted, and permanently restricted net assets. The financial statements are prepared using the accrual method of accounting in accordance with accounting principles generally accepted in the United States of America.

Reclassifications

Certain prior year amounts have been reclassified to conform with current year presentation.

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Organization considers highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Accounts are insured by the Federal Deposit Insurance Corporation up to \$100,000. At December 31, 2005 and 2004, the Company exceeded the insured limit by \$4,723,475 and \$3,763,672, respectively.

Promises to Give

Unconditional promises to give, less an allowance for uncollectible amounts, are recognized as revenues in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

Investments

Investments are stated in the aggregate at market value. Investment income is comprised of realized and unrealized gains and losses and interest income.

Land, Buildings and Equipment

Land, buildings and equipment are stated at cost or fair market value at date of gift. Depreciation is provided over the estimated useful lives of the respective assets on a straight-line basis. When depreciable assets are disposed of, the cost and related accumulated depreciation are removed from the accounts, and any gain (except on trade-in) or loss is included in income for the period. A gain on trade-in is applied to reduce the cost of the new acquisition.

ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEARS ENDED DECEMBER 31, 2005 AND 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Goodwill

Goodwill is recognized for the excess of the purchase price over the fair market of tangible and identifiable intangible net assets of businesses acquired. Goodwill is reviewed annually for impairment under the policy for long-lived assets.

Patient Service Revenue Recognition

The Organization recognizes revenue for patient care when services are performed. The Organization provides an allowance for estimated losses on accounts receivable in the period deemed uncollectible. The allowance for doubtful accounts is \$446,776 and \$342,785 at December 31, 2005 and 2004, respectively.

Contributions

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. All donor-restricted support is reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restriction. When a 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 changes in net assets as net assets released from restrictions.

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.

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. Since the Organization does not expect payment, estimated charges for charity care are not included in revenue.

Funds Held By Others

The Nashville Community Foundation holds funds for the benefit of Alive Hospice, Inc. Alive Hospice, Inc. receives the earnings related to these funds; however, the Organization does not own the funds.

Income Tax

The Organization is exempt from income tax under Section 501(c)(3) of the Internal Revenue Code. Accordingly, no provision for income tax has been made. The Organization has also been classified as an entity that is not a private foundation within the meaning of Section 509(a) of the Internal Revenue Code.

ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEARS ENDED DECEMBER 31, 2005 AND 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the financial statements and disclosures. Accordingly, actual results could differ from those estimates.

Advertising

The Organization's advertising is non-direct, and the costs are expensed as incurred. The Organization incurred \$179,425 and \$128,805 of advertising expense in 2005 and 2004, respectively.

NOTE 2 - INVESTMENTS

Investments at December 31, 2005 and 2004 are summarized as follows:

	2005		2004	
	Cost or Donated Value	Market Value	Cost or Donated Value	Market Value
Corporate bonds and notes	\$ 286,313	\$ 280,836	\$ 337,028	\$ 353,087
Equity securities	784,658	894,056	742,840	848,422
U.S. Governmental securities	<u>179,337</u>	<u>182,946</u>	<u>127,512</u>	<u>145,100</u>
	<u>\$1,250,308</u>	<u>\$1,357,838</u>	<u>\$1,207,380</u>	<u>\$1,346,609</u>

Investment gain amounted to \$86,681 and \$88,448, respectively, for the years ended December 31, 2005 and 2004. Included in these totals are net realized and unrealized losses of \$6,796 for 2005 and net realized and unrealized gains of \$45,181 for 2004.

NOTE 3 - LAND, BUILDINGS AND EQUIPMENT

The balances of the major classes of land and depreciable assets are summarized as follows:

	2005	2004
Land	\$ 2,608,751	\$ 2,608,751
Building and building improvements	\$ 8,192,935	7,992,603
Office furniture and equipment	<u>1,770,290</u>	<u>1,482,007</u>
	12,571,976	12,083,361
Less accumulated depreciation	<u>(2,618,528)</u>	<u>(2,146,750)</u>
	<u>\$ 9,953,448</u>	<u>\$ 9,936,611</u>

ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEARS ENDED DECEMBER 31, 2005 AND 2004

NOTE 4 - CONTRIBUTIONS RECEIVABLE

Contributions receivable are summarized as follows:

	2005	2004
Receivable in less than one year	\$ 82,894	\$ 344,145
Receivable in one to five years	<u>199,532</u>	<u>98,334</u>
Total unconditional promises to give	282,426	442,479
Less discounts to net present value	-	12,458
Less allowance for uncollectible promises	<u>-</u>	<u>178,730</u>
Net unconditional promises to give	<u>\$ 282,426</u>	<u>\$ 251,291</u>
Conditional promises consist of the following:		
Bequests and life insurance policies	<u>\$ 1,475,000</u>	<u>\$ 1,425,000</u>

NOTE 5 - GOODWILL

On August 15, 2005, the Organization purchased all the assets, liabilities and net assets of Hospice of Murfreesboro, Inc. The purchase price of \$950,000 was allocated to identifiable assets including restricted cash reserves (\$300,000), furnishings and equipment (\$26,907) with the remainder of \$623,093 allocated to goodwill.

NOTE 6 - LINE OF CREDIT

The Organization has a \$250,000 line of credit with a local bank with a variable interest rate. There was no amount outstanding on this line of credit as of December 31, 2005 or 2004.

NOTE 7 - BONDS PAYABLE

In 2001, the Organization, through a loan agreement with The Health and Educational Facilities Board of the Metropolitan Government of Nashville and Davidson County, Tennessee issued revenue bonds in the amount of \$8,100,000. The proceeds were used to finance (1) the acquisition, construction and equipping of a 30-bed in-patient hospice facility located at 1710 Patterson Street in Davidson County, (2) the renovation of the offices of the Organization located at 1718 Patterson Street in Davidson County, (3) the retirement of existing indebtedness of the Organization which was incurred to finance an addition to its office facilities at 1718 Patterson Street, and (4) the provision of updated computer equipment for use in both the in-patient facility and the office facility. The term of the loan agreement extends to July 15, 2019, at which time the principal must be repaid in full. Interest is payable monthly at a variable rate on the outstanding bonds. In conjunction with this agreement, the Organization entered an interest rate swap agreement to swap a part of the fixed rate obligation as floating. Payments for swap agreement of \$60,544 and \$104,294 are included in interest expense for the years ended December 31, 2005 and 2004, respectively. Bonds interest payable was \$9,018 and \$13,426 at December 31, 2005 and 2004, respectively. Payments of \$240,000 were made in 2004. The balance of the bonds payable at December 31, 2005 was \$2,200,000. This loan agreement contains, among other things, certain financial covenants and ratios. As of December 31, 2005, the Organization was in compliance with the aforementioned financial covenants and ratios.

ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEARS ENDED DECEMBER 31, 2005 AND 2004

NOTE 8 - NET ASSETS

Temporarily Restricted Net Assets

Funds temporarily restricted by the donors are designated for capital projects, debt service, and various programs offered by the Organization. The total at December 31, 2005 and 2004 was \$293,599 and \$330,756, respectively.

Permanently Restricted Net Assets

Funds donated with permanent restrictions as to use by the Organization totaled \$1,000,000 as of December 31, 2005 and 2004. The donors have stipulated that the investment income be temporarily restricted to support the construction or maintenance of the hospice facilities.

Unrestricted – Board Designated Net Assets

Funds internally designated by the Board of Directors represent non-permanently restricted investments and large contribution receivable balances for which the Board exercises discretion as to the final allocation of these funds. The balance was \$277,398 and \$516,345 at December 31, 2005 and 2004, respectively.

NOTE 9 - THIRD-PARTY RATE ADJUSTMENTS AND REVENUE

Approximately 85% and 86% of net patient service revenue in 2005 and 2004, respectively, was derived under federal and state third-party reimbursement programs. These revenues are based, in part, on cost reimbursement principles and are subject to audit and retroactive adjustment by the respective third-party fiscal intermediaries. In the opinion of management, retroactive adjustments, if any, would not be material to the financial position or results of operations of the Organization.

The Organization grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables at December 31, 2005 and 2004 was as follows:

	2005	2004
Medicare	67%	68%
TennCare	18%	18%
Other third-party payors	15%	14%
	<u>100%</u>	<u>100%</u>

ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEARS ENDED DECEMBER 31, 2005 AND 2004

NOTE 10 - EMPLOYEE BENEFIT PLANS

The Organization has a simplified employee pension plan (SEP) whereby the Organization makes discretionary contributions on behalf of all employees who are at least 18 years old with one year of service. The discretionary contributions, based on annual operating results, were \$639,296 and \$373,967 during 2005 and 2004, respectively. While this plan does not provide for employee contributions, the Organization also maintains a 403(b) defined contribution pension plan whereby employees can contribute a portion of their earnings on a pre-tax basis, up to the allowable legal limits. The Organization does not provide matching contributions to this plan.

NOTE 11 - LEASES

The Organization leases office space and certain office equipment under various noncancellable operating leases. Total rental expense for all operating leases for the years ended December 31, 2005 and 2004, amounted to \$160,874 and \$95,459, respectively.

As of December 31, 2005, future minimum rental payments remaining under these lease obligations were as follows:

2006	\$ 213,465
2007	206,153
2008	170,950
2009	128,277
2010	<u>56,310</u>
	<u>\$ 775,155</u>