

**ALIVE HOSPICE, INC.
FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT
YEARS ENDED DECEMBER 31, 2006 AND 2005**

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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, 2006 and 2005, and the related statements of 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, 2006 and 2005, 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 9, 2007

ALIVE HOSPICE, INC.
STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2006 AND 2005

ASSETS		2006	2005
Cash and cash equivalents:			
Unrestricted	\$	5,713,823	\$ 3,767,589
Endowment		137,995	51,289
Board restricted		978,793	963,158
Donor restricted		51,790	46,870
Total cash and cash equivalents		<u>6,882,401</u>	<u>4,828,906</u>
Investments:			
Endowment		997,530	1,080,440
Board designated		311,866	277,398
Total investments		<u>1,309,396</u>	<u>1,357,838</u>
Accounts receivable, less allowance for doubtful accounts of \$438,816 in 2006 and \$446,776 in 2005		3,738,433	4,274,848
Contributions receivable:			
Unrestricted		144,718	167,426
Donor restricted		702,000	115,000
Total contributions receivable		<u>846,718</u>	<u>282,426</u>
Prepaid expenses		160,817	147,003
Other current assets		56,325	143,462
Land, buildings and equipment, net		10,866,355	9,953,448
Goodwill		623,093	623,093
Total assets		<u>\$ 24,483,538</u>	<u>\$ 21,611,024</u>
LIABILITIES AND NET ASSETS			
Liabilities:			
Accounts payable	\$	753,856	\$ 825,073
Accrued expenses		1,909,667	1,597,885
Mortgage payable		696,111	-
Bonds interest payable		1,821	9,018
Bonds payable		1,720,000	2,200,000
Total liabilities		<u>5,081,455</u>	<u>4,631,976</u>
Net assets:			
Unrestricted:			
Undesignated		17,200,902	15,408,051
Board designated		311,866	277,398
Total unrestricted net assets		<u>17,512,768</u>	<u>15,685,449</u>
Temporarily restricted		889,315	293,599
Permanently restricted		1,000,000	1,000,000
Total net assets		<u>19,402,083</u>	<u>16,979,048</u>
Total liabilities and net assets		<u>\$ 24,483,538</u>	<u>\$ 21,611,024</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, 2006 AND 2005

	2006	2005
Unrestricted net assets:		
Revenue, gains and other support:		
Net patient service revenue	\$ 24,826,067	\$ 20,659,343
Contributions	1,696,533	1,815,465
Investment income	132,687	2,968
Other	354,318	106,297
Net assets released from restrictions	<u>268,773</u>	<u>379,992</u>
Total revenue, gains and other support	<u>27,278,378</u>	<u>22,964,065</u>
Expenses:		
Program services	20,420,950	16,089,238
Management and general	4,458,458	3,826,165
Fundraising	<u>571,651</u>	<u>524,198</u>
Total expenses	<u>25,451,059</u>	<u>20,439,601</u>
Change in unrestricted net assets	1,827,319	2,524,464
Unrestricted net assets, beginning of year	<u>15,685,449</u>	<u>13,160,985</u>
Unrestricted net assets, end of year	<u>17,512,768</u>	<u>15,685,449</u>
Temporarily restricted net assets:		
Contributions	760,390	259,122
Investment income, net	104,099	83,713
Net assets released from restriction	<u>(268,773)</u>	<u>(379,992)</u>
Change in temporarily restricted net assets	595,716	(37,157)
Temporarily restricted net assets, beginning of year	<u>293,599</u>	<u>330,756</u>
Temporarily restricted net assets, end of year	<u>889,315</u>	<u>293,599</u>
Change in net assets	2,423,035	2,487,307
Net assets, beginning of year	<u>16,979,048</u>	<u>14,491,741</u>
Net assets, end of year	<u>\$ 19,402,083</u>	<u>\$ 16,979,048</u>

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

ALIVE HOSPICE, INC.
STATEMENTS OF FUNCTIONAL EXPENSES
YEARS ENDED DECEMBER 31, 2006 AND 2005

	2006				2005
	Program Services	Management and General	Fund -raising	Total	Total
Salaries	\$ 8,592,772	\$ 2,261,751	\$ 150,906	\$ 11,005,429	\$ 8,641,455
Direct patient care	6,871,315	-	-	6,871,315	5,783,399
Benefits and workers comp	1,493,472	410,346	-	1,903,818	1,547,646
Payroll taxes	609,056	157,872	11,311	778,238	616,601
Depreciation	297,691	285,890	2,856	586,437	471,779
Facility and grounds maintenance	443,001	80,806	2,631	526,438	457,232
Mileage	471,573	45,747	1,947	519,267	471,729
Medical supplies	443,260	-	-	443,260	331,124
Rent	275,945	35,179	15,015	326,139	80,559
Professional fees	32,981	235,689	44,181	312,851	288,248
Equipment rental and maintenance	86,044	214,213	-	300,257	154,073
Office and program supplies	82,269	170,489	42,175	294,933	197,279
Telephone	165,520	82,388	1,515	249,423	197,154
Utilities	166,734	40,386	1,454	208,573	180,516
Advertising	-	43,609	146,337	189,946	179,426
Conferences and workshops	62,103	116,830	4,769	183,701	130,676
Dietary supplies	135,972	-	-	135,972	82,977
Insurance	96,447	34,079	-	130,526	109,318
Interest, fees, and bond expense	-	3,713	123,308	127,021	143,723
Printing and publications	36,331	40,393	11,551	88,275	91,861
Dues and licenses	15,415	63,246	1,187	79,848	68,478
Bad debt expense	18,767	59,632	-	78,400	120,078
Other operating expenses	14,685	45,407	22	60,116	55,207
Postage	9,597	30,793	10,486	50,876	39,063
Total expenses	<u>\$ 20,420,950</u>	<u>\$ 4,458,458</u>	<u>\$ 571,651</u>	<u>\$ 25,451,059</u>	<u>\$ 20,439,601</u>

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

ALIVE HOSPICE, INC.
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2006 AND 2005

	2006	2005
Cash flows from operating activities:		
Change in net assets	\$ 2,423,035	\$ 2,487,307
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	586,437	471,779
Net realized and unrealized losses (gains) on investments	(123,206)	6,796
(Increase) decrease in:		
Accounts receivable	536,415	(1,165,923)
Contributions receivable	(564,292)	(31,135)
Prepaid expenses	(13,814)	(117,879)
Other current assets	87,137	(105,305)
Increase (decrease) in:		
Accounts payable	(71,217)	245,751
Accrued expenses	311,782	415,002
Bonds interest payable	(7,197)	(4,408)
Net cash provided by operating activities	<u>3,165,080</u>	<u>2,201,985</u>
Cash flows from investing activities:		
Purchases of investments	(238,331)	(301,314)
Proceeds from sales of investments	409,979	283,289
Capital expenditures and purchase of goodwill	(1,499,344)	(1,111,709)
Net cash used in investing activities	<u>(1,327,696)</u>	<u>(1,129,734)</u>
Cash flows from financing activities:		
Mortgage borrowings	700,000	-
Payments on mortgage	(3,889)	-
Payments on bonds	(480,000)	-
Net cash provided by financing activities	<u>216,111</u>	<u>-</u>
Net increase in cash and cash equivalents	2,053,495	1,072,251
Cash and cash equivalents, beginning of year	<u>4,828,906</u>	<u>3,756,655</u>
Cash and cash equivalents, end of year	<u>\$ 6,882,401</u>	<u>\$ 4,828,906</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest	<u>\$ 109,213</u>	<u>\$ 114,029</u>

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

**ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2006 AND 2005**

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 statements 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, 2006 and 2005, the Company exceeded the insured limit by \$6,895,469 and \$4,723,475, 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, 2006 AND 2005

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 \$438,816 and \$446,776 at December 31, 2006 and 2005, 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, 2006 AND 2005

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 \$189,946 and \$179,426 of advertising expense in 2006 and 2005, respectively.

NOTE 2 - INVESTMENTS

Investments at December 31, 2006 and 2005 are summarized as follows:

	2006		2005	
	Cost or Donated Value	Market Value	Cost or Donated Value	Market Value
Fixed income securities	\$ 411,903	\$ 407,296	\$ 465,650	\$ 463,782
Equity securities	<u>707,972</u>	<u>902,100</u>	<u>784,658</u>	<u>894,056</u>
	<u>\$1,119,875</u>	<u>\$1,309,396</u>	<u>\$1,250,308</u>	<u>\$1,357,838</u>

Investment income amounted to \$236,786 and \$86,681, respectively, for the years ended December 31, 2006 and 2005. Included in these totals are net realized and unrealized gains of \$123,206 and losses of \$6,796, in 2006 and 2005, respectively.

NOTE 3 - LAND, BUILDINGS AND EQUIPMENT

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

	2006	2005
Land	\$ 2,878,251	\$ 2,608,751
Building and building improvements	8,983,144	8,192,935
Office furniture and equipment	<u>2,207,968</u>	<u>1,770,290</u>
	14,069,363	12,571,976
Less accumulated depreciation	<u>(3,203,008)</u>	<u>(2,618,528)</u>
	<u>\$10,866,355</u>	<u>\$ 9,953,448</u>

ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEARS ENDED DECEMBER 31, 2006 AND 2005

NOTE 4 - CONTRIBUTIONS RECEIVABLE

Contributions receivable are summarized as follows:

	2006	2005
Receivable in less than one year	\$ 690,000	\$ 82,894
Receivable in one to five years	156,718	199,532
Total unconditional promises to give	<u>\$ 846,718</u>	<u>\$ 282,426</u>

Conditional promises consist of the following:

Bequests and life insurance policies	<u>\$ 1,475,000</u>	<u>\$ 1,475,000</u>
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As of December 31, 2006, contributions receivable in less than one year includes a promised in-kind donation of computers, software, and training in the amount of \$600,000. This amount has also been included in the temporarily restricted contributions on the statements of changes in net assets and in the temporarily restricted net assets on the statements of financial position.

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 - MORTGAGE PAYABLE

Mortgage payable consists of a note payable to Bank of America, bearing interest at the LIBOR fixed rate (6.35% at December 31, 2006), secured by real property of the Organization, with monthly principal payments of \$3,889 plus interest. The loan matures on November 21, 2021. The balance at December 31, 2006 was \$696,111.

Scheduled repayments on the mortgage are as follows:

Year End December 31,

2007	\$ 46,668
2008	46,668
2009	46,668
2010	46,668
2011	46,668
Thereafter	<u>462,771</u>
Total	<u>\$ 696,111</u>

**ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEARS ENDED DECEMBER 31, 2006 AND 2005**

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 \$30,025 and \$60,544 are included in interest expense for the years ended December 31, 2006 and 2005, respectively. Bonds interest payable was \$1,821 and \$9,018 at December 31, 2006 and 2005, respectively. Payments of \$480,000 were made in 2006. The balance of the bonds payable at December 31, 2006 was \$1,720,000.

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, 2006 and 2005 was \$889,315 and \$293,599, respectively.

Permanently Restricted Net Assets

Funds donated with permanent restrictions as to use by the Organization totaled \$1,000,000 as of December 31, 2006 and 2005. 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 \$311,866 and \$277,398 at December 31, 2006 and 2005, respectively.

ALIVE HOSPICE, INC.
NOTES TO FINANCIAL STATEMENTS (CONTINUED)
YEARS ENDED DECEMBER 31, 2006 AND 2005

NOTE 9 - THIRD-PARTY RATE ADJUSTMENTS AND REVENUE

Approximately 87% and 85% of net patient service revenue in 2006 and 2005, 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, 2006 and 2005 was as follows:

	2006	2005
Medicare	58%	67%
TennCare	25%	18%
Other third-party payors	17%	15%
	<u>100%</u>	<u>100%</u>

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 \$783,949 and \$639,296 during 2006 and 2005, 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, 2006 and 2005, amounted to \$428,164 and \$160,874, respectively.

As of December 31, 2006, future minimum rental payments remaining under these lease obligations were as follows:

2007	\$ 573,077
2008	500,614
2009	455,257
2010	<u>338,222</u>
	<u>\$1,867,170</u>