

North Country HealthCare, Inc.

**Financial Statements, Supplementary Information
and Single Audit Reports**

**Year Ended June 30, 2018
(with comparative totals for 2017)**

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Independent Auditors' Report

To the Board of Directors of
North Country HealthCare, Inc.
Flagstaff, Arizona

Report on the Financial Statements

We have audited the accompanying financial statements of North Country HealthCare, Inc. (the Center, a nonprofit organization), which comprise the statement of financial position as of June 30, 2018, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of North Country HealthCare, Inc. as of June 30, 2018, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited the Center's 2017 financial statements, and we expressed an unmodified opinion on those audited financial statements in our report dated October 25, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2017 is consistent, in all material respects, with the audited financial statements from which it has been derived.

Other Matters

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the 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 financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the 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 financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 18, 2018, on our consideration of the Center's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Center's internal control over financial reporting and compliance.

Fester & Chapman, PLLC

October 18, 2018

North Country HealthCare, Inc.

STATEMENT OF FINANCIAL POSITION

June 30, 2018

(with comparative financial information as of June 30, 2017)

	<u>2018</u>	<u>2017</u>
ASSETS		
Current assets:		
Cash	\$ 1,348,102	\$ 2,853,979
Investments	2,652,252	2,482,676
Accounts receivable, patient revenues, net	6,074,080	4,277,559
Grants receivable	982,971	1,006,281
Other receivables	386,506	459,725
Inventory	484,443	417,004
Prepaid expenses	<u>307,660</u>	<u>296,248</u>
Total current assets	12,236,014	11,793,472
Property and equipment:		
Medical equipment	2,000,226	2,350,975
Furniture, fixtures and office equipment	4,348,097	4,122,474
Leasehold improvements	1,353,100	1,353,100
Buildings and improvements	16,660,814	16,651,423
Land	<u>2,061,430</u>	<u>2,061,430</u>
	26,423,667	26,539,402
Less accumulated depreciation and amortization	<u>(9,759,511)</u>	<u>(9,261,949)</u>
Total property and equipment	<u>16,664,156</u>	<u>17,277,453</u>
Total assets	<u>\$ 28,900,170</u>	<u>\$ 29,070,925</u>
LIABILITIES AND NET ASSETS		
Current liabilities:		
Accounts payable	\$ 1,103,536	\$ 954,953
Accrued wages and benefits	998,676	932,702
Accrued vacations	1,331,118	1,383,663
Refundable advances	678,437	909,961
Current portion of long-term debt	<u>383,319</u>	<u>5,394,403</u>
Total current liabilities	4,495,086	9,575,682
Long-term debt, net of current maturities	<u>4,905,047</u>	<u>144,796</u>
Total liabilities	9,400,133	9,720,478
Net assets:		
Unrestricted	19,067,533	18,945,885
Temporarily restricted	119,757	101,278
Permanently restricted	<u>312,747</u>	<u>303,284</u>
Total net assets	<u>19,500,037</u>	<u>19,350,447</u>
Total liabilities and net assets	<u>\$ 28,900,170</u>	<u>\$ 29,070,925</u>

The accompanying notes are an integral part of these statements.

North Country HealthCare, Inc.

STATEMENT OF ACTIVITIES

Year Ended June 30, 2018

(with comparative financial information for the year ended June 30, 2017)

	Unrestricted	Temporarily	Permanently	Totals	
		Restricted	Restricted	2018	2017
Revenue, support and gains:					
Patient revenue, net	\$ 27,053,270			\$ 27,053,270	\$ 24,168,434
Health Centers Cluster grant	6,536,221			6,536,221	6,465,934
Other grants and contracts	7,239,824			7,239,824	7,661,629
Pharmacy sales	8,529,677			8,529,677	7,855,219
Other income	57,052	\$ 131,416	\$ 9,463	197,931	564,422
Net investment income	121,290	14,383		135,673	266,509
In-kind contributions	762,002			762,002	569,046
Net assets released from restrictions:					
Satisfaction of donor requirements	<u>127,320</u>	<u>(127,320)</u>			
Total revenue, support and gains	<u>50,426,656</u>	<u>18,479</u>	<u>9,463</u>	<u>50,454,598</u>	<u>47,551,193</u>
Expenses:					
Wages and salaries	26,581,459			26,581,459	25,428,296
Payroll taxes and fringe benefits	4,872,705			4,872,705	4,704,774
Professional services - locums	2,726,941			2,726,941	1,692,896
Professional services - other	1,772,935			1,772,935	1,454,155
Pharmaceuticals	3,978,442			3,978,442	3,921,591
Supplies	1,147,217			1,147,217	1,336,436
Repairs and maintenance	897,335			897,335	848,907
Telephone and internet	917,122			917,122	835,096
Marketing	535,515			535,515	533,014
Occupancy	1,521,547			1,521,547	1,277,915
Travel and training	886,115			886,115	831,437
Depreciation and amortization	1,049,505			1,049,505	1,022,812
Patient screening and assistance	612,779			612,779	625,837
Interest expense	204,502			204,502	196,571
Software maintenance	1,399,948			1,399,948	1,341,073
Recruitment, licensing and dues	314,273			314,273	291,993
Miscellaneous	124,666			124,666	156,628
In-kind expense	<u>762,002</u>			<u>762,002</u>	<u>569,046</u>
Total expenses	<u>50,305,008</u>			<u>50,305,008</u>	<u>47,068,477</u>
Change in net assets	121,648	18,479	9,463	149,590	482,716
Net assets, beginning of year	<u>18,945,885</u>	<u>101,278</u>	<u>303,284</u>	<u>19,350,447</u>	<u>18,867,731</u>
Net assets, end of year	<u>\$ 19,067,533</u>	<u>\$ 119,757</u>	<u>\$ 312,747</u>	<u>\$ 19,500,037</u>	<u>\$ 19,350,447</u>

The accompanying notes are an integral part of these statements.

North Country HealthCare, Inc.

STATEMENT OF CASH FLOWS

Year Ended June 30, 2018

(with comparative financial information for the year ended June 30, 2017)

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Change in net assets	\$ 149,590	\$ 482,716
Adjustments to reconcile change in net assets to net cash (used) provided by operating activities:		
Depreciation and amortization	1,049,505	1,022,812
Net gains on investments	(21,042)	(191,993)
Gain on asset disposal	(25,095)	
Change in:		
Accounts receivable, patient revenues, net	(1,796,521)	(636,373)
Grants receivable	23,310	(269,508)
Other receivables	73,219	(289,169)
Inventory	(67,439)	(521)
Prepaid expenses	(11,412)	(27,612)
Accounts payable	148,583	(152,204)
Accrued wages and benefits	65,974	125,076
Accrued vacations	(52,545)	89,673
Refundable advances	<u>(231,524)</u>	<u>305,952</u>
Net cash (used) provided by operating activities	(695,397)	458,849
Cash flows from investing activities:		
Acquisition of property and equipment	(532,403)	(591,313)
Proceeds from the sales of fixed assets	121,290	
Proceeds from the sales of investments	412,495	113,159
Acquisition of investments	<u>(561,029)</u>	<u>(224,206)</u>
Net cash used by investing activities	(559,647)	(702,360)
Cash flows from financing activities:		
Principal payments on long-term debt	<u>(250,833)</u>	<u>(352,776)</u>
Net cash used by financing activities	<u>(250,833)</u>	<u>(352,776)</u>
Net change in cash	(1,505,877)	(596,287)
Cash, beginning of year	<u>2,853,979</u>	<u>3,450,266</u>
Cash, end of year	<u>\$ 1,348,102</u>	<u>\$ 2,853,979</u>
<u>Supplemental disclosure of cash flow information:</u>		
Cash paid for interest	\$ 204,502	\$ 196,571

The accompanying notes are an integral part of these statements.

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 1 - BACKGROUND AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

North Country HealthCare, Inc. (the Center) is a nonprofit corporation formed in Arizona under Section 501(c)(3) of the Internal Revenue Code. The Center has sixteen service sites including three sites in Flagstaff, Arizona, with satellite clinics in Ash Fork, Seligman, Winslow, Holbrook, St. Johns, Round Valley/Springerville, Kingman, Grand Canyon, Show Low, Lake Havasu, Williams, Bullhead City and Payson, Arizona. The Center's objective is to provide accessible, affordable, comprehensive, quality primary health care in northern Arizona, through direct services, training, outreach and advocacy.

The Center's operations are in an area where a significant number of the target population is uninsured and below 200% of the Federal Poverty Level (FPL). In addition, there are a limited number of providers serving this target population in the service area.

The Center received Federal funding through the U.S. Department of Health and Human Services (DHHS) totaling \$8,482,190 and \$8,450,297, for the years ended June 30, 2018 and 2017, respectively. The Center receives other operating funds from Arizona Health Care Cost Containment System (AHCCCS), Medicare, private insurance, self-pay parties and various third party payers. Training and outreach programs are funded through a variety of grants and contracts.

The significant accounting policies of the Center follow:

Basis of Presentation: Financial statement presentation follows the recommendations of the Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) topic of *Not-for-Profit Entities*. The Center is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. See Note 13 for details regarding restrictions on net assets.

Use of Estimates: In preparing financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP), management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 1 - BACKGROUND AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES -
CONTINUED

Investments: Investments primarily consist of shares in mutual funds, and are stated at fair value. Unrealized and realized losses and gains are accounted for as investment (losses) income. The Center estimates the fair value of its investments using available market information and other valuation methodologies (See Note 3). Accordingly, the estimates presented are not necessarily indicative of the amounts that the Center could realize in a current market exchange. The use of different assumptions and/or estimation methods may have a material effect on the estimated fair value amounts. The estimates are based on pertinent information available to management as of June 30, 2018 and 2017. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, current estimates of fair value may differ significantly from the statements presented.

Grants Receivable: The Center recognizes grants as support when eligible costs are incurred or revenues are earned. Grants receivable are recorded when grant expenses are incurred or contracted services have been provided, but reimbursement has not been received by the Center.

Inventory: Inventory, which is comprised of pharmaceuticals and medical supplies, is stated at cost (which approximates fair value) for purchased items, and at estimated fair value for donated items. Cost for items on hand at year-end is determined using the first-in, first-out method.

Property and Equipment: Property and equipment costing \$5,000 or more are recorded at cost, or at their estimated fair value at the date of gift if donated. The cost or value is allocated to current and future periods through depreciation and amortization.

Depreciation and amortization is computed using the straight-line method based on estimated economic lives of the assets as follows:

Buildings and improvements	10 - 40 years
Medical equipment	5 - 7 years
Leasehold improvements	Lesser of the estimated useful life or remaining term of applicable lease
Furniture, fixtures and office equipment	5 - 7 years

DHHS and the State of Arizona retain reversionary interests in property and equipment purchased with their funds, as well as proceeds from the sale of such assets.

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 1 - BACKGROUND AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES -
CONTINUED

Refundable Advances: The Center records funds received from grant awards classified as exchange transactions as refundable advances until the related funds are expended and/or the services related to the awards are performed, at which time funds are recognized as revenue.

Uncompensated Care: The Center provides health care and other related services to patients who meet certain criteria under its charity care policy. Because the Center does not pursue collection of amounts which qualify as charity care, they are not reported as net patient service fees. Uncompensated care provided by the Center under its policy amounted to \$1,699,306 and \$1,315,922 for the years ended June 30, 2018 and 2017, respectively.

In-kind Contributions/Expenses: Donated goods and services are recorded at their estimated fair value at the date of contribution, and shown as revenues and expenses in the financial statements. Donated services are recognized in the financial statements at their estimated fair value if the following criteria are met:

- i) The services require specialized skills and the services are provided by individuals possessing those skills, and the services would typically need to be purchased if not donated; or
- ii) The services enhance or create an asset.

Expense Allocation: The costs of providing various programs and other activities have been summarized on a functional basis in Note 12. Accordingly, certain costs have been allocated to the programs and supporting services benefited.

Income Taxes: The Organization is exempt from federal and state income taxes as an organization other than a private foundation under Section 501(c)(3) of the Internal Revenue Code and similar state provisions.

Prior Year Summarized Information: The financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should only be read in conjunction with the Center's financial statements for the year ended June 30, 2017, from which the summarized information was derived.

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 2 - CONCENTRATIONS

The Center maintains cash and investments at several financial institutions located in northern Arizona. Accounts at each institution are insured in limited amounts by the Federal Deposit Insurance Corporation (FDIC), or covered under the Securities Investor Protection Corporation (SIPC). The Center has not experienced material losses in such accounts and believes it is not exposed to significant credit risks.

NOTE 3 - INVESTMENTS AND FAIR VALUE MEASUREMENT

GAAP establishes a framework for measuring fair value and expands disclosures about fair value measurements, which are determined based on assumptions that market participants would use in pricing assets and liabilities. GAAP also establishes a fair value hierarchy that distinguishes between market participant assumptions and the Center's own assumptions about market participant assumptions.

Observable inputs are assumptions based on market data obtained from independent sources, while unobservable inputs are the Center's own assumptions about what market participants would assume based on the best information available in the circumstance.

Level 1 inputs – A quoted price in an active market for an identical asset or liability is considered to be the most reliable evidence of fair value.

Level 2 inputs – These are observable inputs, either directly or indirectly, other than quoted prices included within Level 1. The Center does not have any financial instruments it values based on Level 2 inputs.

Level 3 inputs – These inputs are unobservable and are used to measure fair value only when observable inputs are not available. The Center does not have any financial instruments it values based on Level 3 inputs.

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 3 - INVESTMENTS AND FAIR VALUE MEASUREMENT - CONTINUED

Fair value of assets measured on a recurring basis at June 30, 2018 were as follows:

	<u>Level 1</u>
Equities:	
U.S. large cap	\$ 513,453
U.S. mid cap	109,205
U.S. open-end funds	214,147
Non-U.S. equities	<u>737,927</u>
Total equities	1,574,732
Bonds:	
Core fixed income	462,700
High-yield fixed income	162,881
Short U.S. government funds	354,444
Emerging market local currency debt	<u>48,646</u>
Total bonds	1,028,671
Other	<u>48,849</u>
Totals	<u><u>\$ 2,652,252</u></u>

Fair value of assets measured on a recurring basis at June 30, 2017 were as follows:

	<u>Level 1</u>
Equities:	
U.S. large cap	\$ 471,355
U.S. mid cap	98,761
U.S. open-end funds	198,144
Non-U.S. equities funds	<u>742,834</u>
Total equities	1,511,094
Bonds:	
Core fixed income	413,894
High-yield fixed income	147,551
Short U.S. government funds	314,437
Emerging market local currency debt	<u>50,100</u>
Total bonds	925,982
Other	<u>45,600</u>
Totals	<u><u>\$ 2,482,676</u></u>

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 3 - INVESTMENTS AND FAIR VALUE MEASUREMENT - CONTINUED

Net investment income (losses) is comprised of the following for the years ended June 30,

	<u>2018</u>	<u>2017</u>
Interest and dividends	\$ 114,631	\$ 74,516
Realized gains (losses)	16,461	(16,313)
Unrealized gains	<u>4,581</u>	<u>208,306</u>
Net investment income	<u>\$ 135,673</u>	<u>\$ 266,509</u>

NOTE 4 - ACCOUNTS RECEIVABLE, PATIENT REVENUES - NET

Accounts receivable consist of charges to patients for services provided to them. Settled charges have been adjusted by a sliding fee schedule based on each patient's ability to pay. Management provides for uncollectible amounts through a provision for bad debt and contractual allowances, and based on its assessment of the current status of individual accounts.

The Center's due from AHCCCS receivable balance is included in accounts receivable, net, and it represents amounts due from Arizona Health Care Cost Containment System (AHCCCS) for the unreimbursed cost of providing primary health care to AHCCCS members. As of April 1, 2015, AHCCCS replaced the Prospective Payment System, and now FQHCs primarily receive their all-inclusive per visit cost for each AHCCCS encounter by directly billing the contracted third party AHCCCS insurance plans. The Center completes annual reconciliations between actual costs of providing healthcare services to AHCCCS members and the payments received from the third party AHCCCS insurance plans.

The following is a summary at June 30,

	<u>2018</u>	<u>2017</u>
Accounts receivable, patient revenues	\$ 6,165,243	\$ 3,965,938
Pharmacy revenue	814,618	732,348
Medicare Cost Report	278,483	273,000
Due from AHCCCS	2,279,736	1,126,224
Allowance for doubtful accounts and contractual allowances	<u>(3,464,000)</u>	<u>(1,819,951)</u>
Accounts receivable, patient revenues, net	<u>\$ 6,074,080</u>	<u>\$ 4,277,559</u>

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 5 - REFUNDABLE ADVANCES

Refundable advances consist primarily of grant funds received that are unspent as of the end of the fiscal year. The following is a summary of refundable advances for the years ended June 30,

	<u>2018</u>	<u>2017</u>
Health Choice Integrated Care	\$ 252,812	\$ 225,772
Scottsdale Healthcare		169,848
Other grants	<u>425,625</u>	<u>514,341</u>
Total refundable advances	<u>\$ 678,437</u>	<u>\$ 909,961</u>

NOTE 6 - LINE-OF-CREDIT

The Center has a revolving line-of-credit with J.P. Morgan Chase Bank in the amount of \$2,000,000, secured by the Center's assets, maturing in January 2019. Borrowings under the line bear interest at LIBOR plus 3.0%, which was 5.76% and 4.73% at June 30, 2018 and 2017, respectively. The outstanding balance on the line-of-credit was \$0 at June 30, 2018 and 2017.

NOTE 7 - LONG-TERM DEBT

Long-term debt at June 30 consisted of the following:

	<u>2018</u>	<u>2017</u>
\$5,481,278 note payable to J.P. Morgan Chase Bank dated June 26, 2012, secured by the Center's land and the clinic in Flagstaff. The note is due in monthly installments of \$32,207, including interest at 3.65%, maturing on March 10, 2018, with remaining principal and unpaid interest due at maturity. The note was refinanced in August 2018. See Note 16.	\$ 4,271,011	\$ 4,456,501
\$1,105,000 note payable to J.P. Morgan Chase Bank dated August 28, 2012, secured by the Show Low clinic. The note is due in monthly installments of \$6,681, including interest at 3.9%, maturing on March 1, 2018, with remaining principal and unpaid interest due at maturity. The note was retired in August 2018. See Note 16.	872,570	916,892

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 7 - LONG-TERM DEBT - CONTINUED

	<u>2018</u>	<u>2017</u>
\$211,500 note payable to White Mountain Communities Special Health Care District for the purchase of land in Springerville, Arizona, dated May 26, 2010, secured by the Center's Springerville clinic. The note is due in monthly installments of \$1,282, including 4.00% interest, maturing April 2030.	144,785	154,179
Capital lease obligations, see Note 8		<u>11,627</u>
Total	<u>5,288,366</u>	<u>5,539,199</u>
Less current maturities	<u>383,319</u>	<u>5,394,403</u>
Long-term debt, net of current maturities	<u>\$ 4,905,047</u>	<u>\$ 144,796</u>

Future maturities of long-term debt are as follows for the years ending June 30,

2019	\$ 383,319
2020	445,968
2021	467,727
2022	489,940
2023	513,209
Thereafter	<u>2,988,203</u>
	<u>\$ 5,288,366</u>

The Center is required to comply with the following financial covenants on the debt from J.P. Morgan Chase Bank: current ratio not less than 1.50 to 1.00 (quarterly), debt service coverage ratio of not less than 1.30 to 1.00 (annually), and a minimum ratio of debt to net assets not in excess of 1.75 to 1.00 (quarterly). At June 30, 2018 and 2017 the Center was in compliance with these requirements.

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 8 - LEASES

Capital Leases:

The Center had capital leases for equipment and data infrastructure costing \$311,854. Amortization of the leased assets is included with depreciation expense. Accumulated amortization was \$311,854 and \$249,483 at June 30, 2018 and 2017, respectively. The outstanding balance on the capital leases was \$0 and \$11,627 at June 30, 2018 and 2017, respectively.

Operating Leases:

The Center leases facilities and equipment under several operating lease agreements expiring through 2025. Rent expense for the years ended June 30, 2018 and 2017 was \$916,942 and \$735,148, respectively. Future minimum payments on noncancellable operating leases at June 30, 2018 are as follows:

Years ending June 30,	
2019	\$ 805,306
2020	757,624
2021	590,688
2022	521,081
2023	330,993
Thereafter	465,112
	<u>\$ 3,470,804</u>

NOTE 9 - PATIENT REVENUE, NET

Patient revenue consists of gross charges to patients for services rendered. The charges are comparable to what other health service facilities would charge for the same services. The charges are then decreased by a sliding scale subsidy adjustment (charity care) based on each patient's ability to pay. The Center also receives fees for services provided that are adjusted based on a negotiated fee schedule with the patient's insurer.

The following summarizes patient revenue for the years ended June 30,

	2018	2017
Patient service charges	\$ 42,536,585	\$ 38,244,539
Disallowed insurance, sliding scale subsidy, bad debt, and other contractual adjustments	<u>(15,483,315)</u>	<u>(14,076,105)</u>
Patient revenue, net	<u>\$ 27,053,270</u>	<u>\$ 24,168,434</u>

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 10 - OTHER GRANTS AND CONTRACTS

The Center received the following grants and contracts revenue from various federal and non-federal sources during the years ended June 30,

	<u>2018</u>	<u>2017</u>
Arizona Department of Health Services:		
Health Start	\$ 388,775	\$ 452,809
Well Woman Health Check	711,233	668,494
Ryan White HIV Care Formula Grants	279,182	296,810
Affordable Care Act programs and other grants	673,467	606,552
University of Arizona - Model Area Health Education Center	626,954	593,354
University of Arizona - Family Medicine Education Center	90,764	217,809
National Park Service contract	670,692	649,620
Arizona Alliance of Community Health Centers	68,773	371,563
Clark County Social Service - Ryan White	171,133	183,265
United Way of Northern Arizona	32,346	25,889
Susan G. Komen Foundation	41,732	125,477
Northern Arizona Center Against Sexual Assault (NACASA)	323,688	277,738
A.T. Still University	361,805	375,304
Williams Hospital District	1,032,913	1,108,490
Health Choice Integrated Care	608,626	628,117
Other grants and contracts	<u>1,157,741</u>	<u>1,080,338</u>
Total other grants and contracts	<u>\$ 7,239,824</u>	<u>\$ 7,661,629</u>

NOTE 11 - IN-KIND CONTRIBUTIONS AND EXPENSES

During the years ended June 30, 2018 and 2017, the Center recognized in-kind contributions and expenses of \$667,649 and \$428,214, respectively, for donated vaccines, and \$94,353 and \$140,832, respectively, for donated medical services.

NOTE 12 - FUNCTIONAL EXPENSE ALLOCATION

The following is a summary of the Center's expenses by function for the years ended June 30,

	<u>2018</u>	<u>2017</u>
Primary health care and education	\$37,665,084	\$34,966,258
General and administrative	12,458,022	11,997,594
Fundraising	<u>191,902</u>	<u>104,625</u>
Total expenses	<u>\$50,315,008</u>	<u>\$47,068,477</u>

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 13 - RESTRICTED NET ASSETS

The Center maintains its John H. Caskey endowment fund in accordance with Arizona's Uniform Prudent Management of Institutional Funds Act (UPMIFA), which governs the handling of endowment funds. Under UPMIFA, institutions may spend or accumulate as much as they determine to be prudent, taking into account the donor's intent, the duration and preservation of the endowment fund, and the purposes of the institution and the endowment fund. Assets in an endowment fund are donor restricted until appropriated for expenditure by the Center's governing Board.

Contributions to the endowment fund are classified as permanently restricted net assets, with investment income available for distribution, after the Board has appropriated such earnings for expenditure.

Asset Allocation, Return Objectives and Spending Policy

The Board has authorized the finance committee to review the endowment fund's asset allocation periodically. Endowment fund assets include investments in equity securities, bonds and money market accounts based on a Board-approved percentage range for each type of investment. Each year the Board may appropriate endowment funds to be available for expenditure. This distribution is calculated as 5% of the average balance of the endowment fund for the previous four quarters. The Board's finance committee may adjust the spending rate percentage as it deems appropriate, based on market conditions and other factors.

Distributions made from the endowment fund are transferred into the Center's Angel Fund and classified as temporarily restricted net assets. The Angel Fund includes amounts which are donor restricted to benefit patients in certain service areas or for specific purposes.

Activity of the endowment fund for the year ended June 30, 2018 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year		\$ 101,278	\$ 303,284	\$ 404,562
Investment income		14,383		14,383
Contributions		131,416	9,463	140,879
Appropriated for expenditure	\$ 127,320	(127,320)		
Expenditures	(127,320)			(127,320)
Endowment net assets, end of year	<u>\$</u>	<u>\$ 119,757</u>	<u>\$ 312,747</u>	<u>\$ 432,504</u>

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 13 - RESTRICTED NET ASSETS - CONTINUED

Activity of the endowment fund for the year ended June 30, 2017 is as follows:

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 57,062	\$ 207,027	\$ 283,358	\$ 547,447
Investment income		8,854		8,854
Contributions		103,544	19,926	123,470
Appropriated for expenditure	218,147	(218,147)		
Expenditures	<u>(275,209)</u>			<u>(275,209)</u>
Endowment net assets, end of year	<u>\$</u>	<u>\$ 101,278</u>	<u>\$ 303,284</u>	<u>\$ 404,562</u>

NOTE 14 - DEFINED CONTRIBUTION RETIREMENT PLAN

The Center has a 401(k) defined contribution retirement plan which allows employees with one year of service to participate. Under the plan, the Center provides matching contributions of up to 4 percent of each participating employee's salary. The Center's contributions to the plan were \$600,990 and \$552,235 for the years ended June 30, 2018 and 2017, respectively.

NOTE 15 - CONTINGENT LIABILITIES

Compliance: The Center participates in federally-funded and state-funded programs administered by various government agencies. The programs included in these financial statements may be subject to program compliance and/or financial monitoring by the granting agencies or their representatives. The amount, if any, of expenses which may be disallowed by the granting agencies cannot be determined at this time.

Healthcare regulation: The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not limited to, matters such as licensure, accreditation, program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Center is in compliance with all applicable laws and regulations. Compliance with such laws and regulations can be subject to future review and interpretation as well as regulatory actions unknown or unasserted at this time.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 15 - CONTINGENT LIABILITIES - CONTINUED

The Health Insurance Portability and Accountability Act of 1996 (HIPAA) broadened the scope of certain fraud and abuse laws by adding several criminal provisions for fraud offenses that apply to all health benefit programs. HIPAA also added a prohibition against incentives intended to influence decisions by Medicare beneficiaries as to the provider from which they receive services. HIPAA was followed by the Balanced Budget Act of 1997, which created additional fraud and abuse provisions, including civil penalties for contractors.

HIPAA developed standards to protect the privacy and security of individually identifiable health-related information. The privacy standards regulate the use and disclosure of health-related information, whether communicated electronically, on paper or orally. Also, additional security regulations became mandatory on April 20, 2005, and require health care providers to implement administrative, physical and technical practices to protect the security of individually identifiable health-related information that is maintained or transmitted electronically. In February 2010, HIPAA requirements were updated by the Health Information Technology for Economic and Clinical Health Act (HITECH Act). Under the HITECH Act, violations of HIPAA requirements could now result in civil penalties of up to \$50,000 per incident, and up to \$1.5 million in total for each type of violation in a calendar year.

Professional liability insurance: The Federally Supported Health Centers Assistance Act of 1992 authorizes the Public Health Service to assume responsibility for medical malpractice claims involving approved grantees and certain other health care providers under the Federal Tort Claims Act (FTCA). The Center is currently covered under the FTCA.

Litigation: Periodically, the Center is involved in litigation and claims arising in the normal course of operations. In the opinion of management, based on consultation with legal counsel, losses, if any, from these matters are covered by insurance or are immaterial.

Other matters: During the year ending June 30, 2017, the Center's management became aware of a potential loss of funding related to Universal Service Administrative Company (USAC) credits related to a contract with a third-party telecommunications vendor. These credits helped to offset the Center's telecommunication expenses during the year ended June 30, 2017. The Center is currently appealing the denial of the USAC credits with the Federal Communications Commission, as well as reviewing other options available to it; therefore, the amount, if any, of the potential impact to these financial statements or to future years covered under the contract with this vendor are unknown.

North Country HealthCare, Inc.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

(with comparative financial information as of and for the year ended June 30, 2017)

NOTE 16 - SUBSEQUENT EVENTS

Subsequent events have been evaluated through October 18, 2018, which was the date the Center's financial statements were available to be issued.

The Center refinanced its note payable (secured by the Flagstaff Clinic) and retired another note payable (secured by the Show Low clinic) in August 2018. The new note is secured by the Center's Flagstaff clinic, with monthly payments due of \$54,135, including 4.60% interest, with a balloon payment of \$2,335,227 due at maturity in September 2023.

SUPPLEMENTARY INFORMATION

North Country HealthCare, Inc.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2018

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Grantor's Number</u>	<u>Expenditures</u>	<u>Amounts Provided to Subrecipients</u>
U.S. Department of Health and Human Services:				
Health Centers Cluster: Health Center Program	93.224	N/A	\$ 6,536,221	\$
Substance Abuse and Mental Health Services_Opioid State Targeted Response, passed through Health Choice Integrated Care	93.788	None	278,960	
Grants for Education, Prevention, and Early Detection of Radiogenic Cancers and Diseases	93.257	N/A	189,195	
Cancer Prevention and Control Programs for State, Territorial and Tribal Organizations financed in part by Prevention and Public Health Funds, passed through Arizona Department of Health Services	93.752	ADHS14-069425	711,233	
HIV Emergency Relief Project Grants, passed through Clark County, Nevada	93.914	4800008177-004	171,133	
HIV Care Formula Grants, passed through Arizona Department of Health Services	93.917	ADHS13-050870	279,182	
Block Grants for Prevention and Treatment of Substance Abuse, passed through Health Choice Integrated Care	93.959	None	70,151	
Area Health Education Centers, passed through University of Arizona	93.107	PO 292602, U77HP03034	69,218	
PPHF Cooperative Agreement to Support Navigators in Federally-facilitated and State Partnership Exchanges, passed through Arizona Alliance for Community Health Centers	93.750	CA-NAV-130007-01-00	26,758	
Assistance Programs for Chronic Disease Prevention and Control, passed through Arizona Department of Health Services	93.945	ADHS 15-094090	<u>150,139</u>	<u> </u>
Total U.S. Department of Health and Human Services			8,482,190	

The accompanying notes are an integral part of this schedule.

North Country HealthCare, Inc.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS - CONTINUED

Year Ended June 30, 2018

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-through Grantor's Number</u>	<u>Expenditures</u>	<u>Amounts Provided to Subrecipients</u>
U.S. Department of Agriculture:				
State Administrative Matching Grants for the Supplemental Nutrition Assistance Program, passed through Arizona Community Action Association	10.561	None	164,514	
U.S. Department of Justice:				
Rural Domestic Violence, Dating Violence, Sexual Assault, and Stalking Assistance Program, passed through Arizona Alliance for Community Health Centers	16.589	DOJ#2007-WR-AX-0010	<u>42,015</u>	<u> </u>
Total expenditures of federal awards			<u>\$ 8,688,719</u>	<u>\$</u>

The accompanying notes are an integral part of this schedule.

North Country HealthCare, Inc.

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2018

NOTE 1 - BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of North Country HealthCare, Inc. and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic financial statements.

NOTE 2 - CATALOG OF FEDERAL DOMESTIC ASSISTANCE (CFDA) NUMBERS

The program titles and CFDA numbers were obtained from federal or pass-through grantors or the 2018 *Catalog of Federal Domestic Assistance*.

NOTE 3 - INDIRECT COST RATE

The Center has selected not to use the 10 percent de minimis indirect cost rate as allowed under the Uniform Guidance.

NOTE 4 - SUBRECIPIENTS

The Center did not pass on any federal funds to subrecipients during the fiscal year ended June 30, 2018.

SINGLE AUDIT REPORTS



Independent Auditors' Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance with *Government Auditing Standards*

The Board of Directors of
North Country HealthCare, Inc.
Flagstaff, Arizona

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of North Country HealthCare, Inc. (the Center, a nonprofit organization), which comprise the statement of financial position as of June 30, 2018, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated October 18, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Center's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Center's internal control. Accordingly, we do not express an opinion on the effectiveness of the Center's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Center's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the organization's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Center's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Fester & Chapman, PLLC

October 18, 2018



Independent Auditors' Report on Compliance For Each Major Federal Program and
on Internal Control over Compliance Required by the Uniform Guidance

The Board of Directors of
North Country HealthCare, Inc.
Flagstaff, Arizona

Report on Compliance for Each Major Federal Program

We have audited North Country HealthCare, Inc. (the Center)'s compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Center's major federal programs for the year ended June 30, 2018. The Center's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of the Center's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Center's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Center's compliance.

Opinion on Each Major Federal Program

In our opinion, the Center complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2018.

Report on Internal Control over Compliance

Management of the Center is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Center's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Center's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Fester & Chapman, PLLC

October 18, 2018

North Country HealthCare, Inc.

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended June 30, 2018

Section I - Summary of Auditors' Results

Financial Statements:

Type of auditors' report issued: Unmodified

Internal control over financial reporting:

Material weakness(es) identified in internal control over financial reporting?	<u> </u> yes	<u> X </u> no
Significant deficiency(ies) identified that are not considered to be material weaknesses?	<u> </u> yes	<u> X </u> none reported
Noncompliance material to financial statements noted?	<u> </u> yes	<u> X </u> no

Federal Awards:

Internal control over major programs:

Material weakness(es) identified?	<u> </u> yes	<u> X </u> no
Significant deficiency(ies) identified that are not considered to be material weakness(es)?	<u> </u> yes	<u> X </u> none reported

Type of auditors' report on compliance for major programs: Unmodified

Any audit findings disclosed that are required to be reported in accordance with section 2 CFR 200.516(a)?	<u> </u> yes	<u> X </u> no
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Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Programs or Cluster</u>
93.224	Heath Centers Cluster: Health Center Program
93.788	Substance Abuse and Mental Health Services_Opioid State Targeted Response

Dollar threshold used to distinguish between type A and type B programs:	<u>\$750,000</u>
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Auditee qualified as low-risk auditee?	<u> X </u> yes	<u> </u> no
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Other Matters:

Auditee's Summary Schedule of Prior Audit Findings required to be reported in accordance with 2 CFR 200.511(b)?	<u> </u> yes	<u> X </u> no
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Section II - Financial Statement Findings

None noted.

Section III - Federal Award Findings and Questioned Costs

None noted.