

St. John's Well Child and Family Center, Inc.

Independent Auditor's Report and Financial Statements

December 31, 2013 and 2012

St. John's Well Child and Family Center, Inc.
December 31, 2013 and 2012

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Independent Auditor's Report

Board of Directors
St. John's Well Child and Family Center, Inc.
Los Angeles, California

We have audited the accompanying financial statements of St. John's Well Child and Family Center, Inc. (the "Organization"), which comprise the balance sheets as of December 31, 2013 and 2012, and the related statements of operations, changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the 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 auditor's 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.

Board of Directors
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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of St. John's Well Child and Family Center, Inc. as of December 31, 2013 and 2012, and the results of its operations, the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

BKD, LLP

Springfield, Missouri
September 29, 2014

St. John's Well Child and Family Center, Inc.

Balance Sheets

December 31, 2013 and 2012

Assets

	<u>2013</u>	<u>2012</u>
Current Assets		
Cash	\$ 792,206	\$ 2,675,217
Assets limited as to use - current	3,385,268	-
Patient accounts receivable, net	3,526,990	2,361,017
Grants and other receivables	1,249,405	1,846,461
Contributions receivable - current	1,215,915	1,257,228
Estimated amounts due from third-party payers - current	7,679	294,542
Supplies	218,468	214,213
Prepaid expenses and other	170,988	175,888
	<u>10,566,919</u>	<u>8,824,566</u>
Assets Limited As To Use		
Held internally under debt agreement	3,385,268	-
Held by trustee	368,956	368,956
	<u>3,754,224</u>	<u>368,956</u>
Less amount required to meet current obligations	3,385,268	-
	<u>368,956</u>	<u>368,956</u>
Contributions Receivable	<u>27,608</u>	<u>242,481</u>
Estimated Amounts Due From Third-Party Payers	225,892	623,842
Less current portion	7,679	294,542
	<u>218,213</u>	<u>329,300</u>
Property and Equipment, At Cost		
Land and land improvements	2,647,884	2,647,884
Buildings and leasehold improvements	13,866,088	12,320,048
Equipment	2,602,300	2,517,620
Furniture and fixtures	970,681	868,469
Construction in progress	5,383,041	2,649,429
	<u>25,469,994</u>	<u>21,003,450</u>
Less accumulated depreciation	3,840,395	3,617,176
	<u>21,629,599</u>	<u>17,386,274</u>
Other Assets		
Deferred financing costs	634,923	552,722
	<u>634,923</u>	<u>552,722</u>
Total assets	<u>\$ 33,446,218</u>	<u>\$ 27,704,299</u>

Liabilities and Net Assets

	<u>2013</u>	<u>2012</u>
Current Liabilities		
Current maturities of long-term debt	\$ 4,332,390	\$ 1,118,343
Accounts payable	3,739,748	2,840,213
Accrued expenses	856,827	1,306,853
Deferred grant revenue	-	2,000
	<u>8,928,965</u>	<u>5,267,409</u>
Long-Term Debt	5,786,965	6,053,245
Accrued Rent Payable	<u>17,341</u>	<u>18,881</u>
Total liabilities	<u>14,733,271</u>	<u>11,339,535</u>
Net Assets		
Unrestricted	15,721,607	12,933,681
Temporarily restricted	<u>2,991,340</u>	<u>3,431,083</u>
	<u>18,712,947</u>	<u>16,364,764</u>
Total liabilities and net assets	<u>\$ 33,446,218</u>	<u>\$ 27,704,299</u>

St. John's Well Child and Family Center, Inc.
Statements of Operations
Years Ended December 31, 2013 and 2012

	2013	2012
Unrestricted Revenues, Gains and Other Support		
Net patient service revenue less provision for uncollectible accounts	\$ 17,296,587	\$ 14,211,690
Premium revenue	1,661,541	1,753,714
Grant revenue	7,724,870	6,196,968
Contributions	1,333,856	1,653,829
Other	378,116	218,635
Net assets released from restrictions used for operations	2,216,681	1,897,329
Total unrestricted revenues, gains and other support	30,611,651	25,932,165
Expenses and Losses		
Salaries and wages	15,035,305	12,750,061
Employee benefits	3,018,970	2,438,258
Purchased services and professional fees	6,216,797	4,253,150
Supplies and other	5,495,681	5,590,961
Rent	266,941	263,412
Depreciation and amortization	1,445,890	1,332,955
Interest	402,852	403,593
Loss on disposal of property and equipment	10,833	1,649
Total expenses and losses	31,893,269	27,034,039
Deficiency of Revenues Over Expenses	(1,281,618)	(1,101,874)
Contributions of or for acquisition of property and equipment	30,000	205,294
Grants for acquisition of property and equipment	3,703,764	5,955,565
Net assets released from restrictions used for purchase of property and equipment	335,780	222,128
Increase in Unrestricted Net Assets	\$ 2,787,926	\$ 5,281,113

St. John's Well Child and Family Center, Inc.
Statements of Changes in Net Assets
Years Ended December 31, 2013 and 2012

	2013	2012
Unrestricted Net Assets		
Deficiency of revenues over expenses	\$ (1,281,618)	\$ (1,101,874)
Contributions of or for acquisition of property and equipment	30,000	205,294
Grants for acquisition of property and equipment	3,703,764	5,955,565
Net assets released from restrictions used for purchase of property and equipment	335,780	222,128
Increase in unrestricted net assets	2,787,926	5,281,113
Temporarily Restricted Net Assets		
Contributions	2,112,718	2,460,072
Net assets released from restriction	(2,552,461)	(2,119,457)
Increase (decrease) in temporarily restricted net assets	(439,743)	340,615
Change in Net Assets	2,348,183	5,621,728
Net Assets, Beginning of Year	16,364,764	10,743,036
Net Assets, End of Year	\$ 18,712,947	\$ 16,364,764

St. John's Well Child and Family Center, Inc.
Statements of Cash Flows
Years Ended December 31, 2013 and 2012

	<u>2013</u>	<u>2012</u>
Operating Activities		
Change in net assets	\$ 2,348,183	\$ 5,621,728
Items not requiring (providing) cash		
Loss on disposal of property and equipment	10,833	1,649
Depreciation and amortization	1,445,890	1,332,955
Contributions of or for acquisition of property and equipment	(30,000)	(205,294)
Grants for acquisition of property and equipment	(3,703,764)	(5,955,565)
Change in contributed supplies	30,074	104,309
Accrued rent payable	(1,540)	841
Changes in		
Patient accounts receivable, net	(1,165,973)	(511,218)
Grants and other receivables	597,056	(164,899)
Contributions receivable	256,186	(400,664)
Estimated amounts due from third-party payers	397,950	186,158
Prepaid expenses and other	4,900	(37,287)
Supplies	(34,329)	14,213
Accounts payable and accrued expenses	(307,509)	590,155
Deferred grant revenue	(2,000)	2,000
	<u>(154,043)</u>	<u>579,081</u>
Investing Activities		
Purchase of assets limited as to use	(3,385,268)	-
Purchase of property and equipment	(4,893,916)	(6,950,548)
	<u>(8,279,184)</u>	<u>(6,950,548)</u>
Financing Activities		
Proceeds from contributions for acquisition of property and equipment	-	200,000
Proceeds from grants for acquisition of property and equipment	3,703,764	5,955,565
Payment of deferred financing costs	(101,315)	-
Proceeds from issuance of long-term debt	3,450,000	800,000
Principal payments on long-term debt	(502,233)	(382,126)
Proceeds from issuance of notes payable to bank	550,000	700,000
Principal payments on notes payable to bank	(550,000)	(700,000)
	<u>6,550,216</u>	<u>6,573,439</u>

St. John's Well Child and Family Center, Inc.
Statements of Cash Flows
Years Ended December 31, 2013 and 2012

	2013	2012
Increase (Decrease) in Cash	\$ (1,883,011)	\$ 201,972
Cash, Beginning of Year	2,675,217	2,473,245
Cash, End of Year	\$ 792,206	\$ 2,675,217
Supplemental Cash Flows Information		
Interest paid (net of amount capitalized)	\$ 402,852	\$ 403,593
Property and equipment acquisitions in accounts payable	\$ 1,989,512	\$ 1,232,494
Capital lease obligation incurred for property and equipment	\$ -	\$ 109,900
Equipment acquired through noncash contribution	\$ 30,000	\$ 5,294

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

St. John's Well Child and Family Center, Inc. (the "Organization") is a community health center that primarily earns revenues by providing physician and related health care services through clinics located in Los Angeles, California.

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 reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash

At December 31, 2013, the Organization's cash accounts exceeded federally insured limits by approximately \$980,000. This amount includes bank balances available to pay checks issued prior to year-end but not yet presented for payment prior as of December 31, 2013.

Assets Limited As To Use

Assets limited as to use include a money market account held by trustee under an indenture agreement and a lender and a restricted cash account which contains funds obtained under a financing agreement with NCB Capital Impact (*Note 8*).

Patient Accounts Receivable

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, the Organization analyzes its past history and identifies trends for each of its major payer sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for uncollectible accounts. Management regularly reviews data about these major payer sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

For receivables associated with services provided to patients who have third-party coverage, the Organization analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for uncollectible accounts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payer has not yet paid, or for payers who are known to be having financial difficulties that make the realization of amounts due unlikely).

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

For receivables associated with self-pay patients (which includes both patients without insurance and patients with deductible and copayment balances due for which third-party coverage exists for part of the bill), the Organization records a provision for doubtful accounts in the period of service on the basis of its past experience, which indicates that many patients are unable or unwilling to pay the portion of their bill for which they are financially responsible. The difference between the standard rates (or the discounted rates if negotiated or provided by policy) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

No significant provision for uncollectible accounts was recorded for the years ended December 31, 2013 and 2012. No allowance for uncollectible accounts was needed at December 31, 2013 and 2012.

Supplies

The Organization states supply inventories at the lower of cost, determined using the first-in, first-out method, or market.

Property and Equipment

Property and equipment acquisitions are recorded at cost and are depreciated on a straight-line basis over the estimated useful life of each asset. Assets under capital lease obligations and leasehold improvements are depreciated over the shorter of the lease term or their respective estimated useful lives.

Donations of property and equipment are reported at fair value as an increase in unrestricted net assets unless use of the assets is restricted by the donor. Monetary gifts that must be used to acquire property and equipment are reported as restricted support. The expiration of such restrictions is reported as an increase in unrestricted net assets when the donated asset is placed in service.

Certain property and equipment have been purchased with grant funds received from the U.S. Department of Health and Human Services. Such items may be reclaimed by the federal government if not used to further the grant's objectives.

The Organization capitalizes interest costs as a component of construction in progress, based on the weighted-average rates paid for long-term borrowing. Total interest incurred was:

	2013	2012
Interest costs capitalized	\$ 93,263	\$ 70,542
Interest costs charged to expense	402,852	403,593
Total interest incurred	<u>\$ 496,115</u>	<u>\$ 474,135</u>

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Effective January 1, 2012, the estimated useful service lives of the Organization's Hoover building and related leasehold improvements were decreased due to the Williams/Hoover Campus renovation project and the demolition of the Hoover building in March 2013. The effect of this change was to increase depreciation expense for 2012 by \$501,657.

Long-Lived Asset Impairment

The Organization evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimate future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value.

No impairment loss was recognized for the years ended December 31, 2013 and 2012.

Deferred Financing Costs

Deferred financing costs represent costs incurred in connection with the issuance of long-term debt. Such costs are being amortized over the term of the respective debt using the straight-line method.

Temporarily Restricted Net Assets

Temporarily restricted net assets are those whose use by the Organization has been limited by donors to a specific time period or purpose.

Net Patient Service Revenue

The Organization has agreements with third-party payers that provide for payments to the Organization at amounts different from its established rates. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers and others for services rendered and includes estimated retroactive revenue adjustments. Retroactive adjustments are considered in the recognition of revenue on an estimated basis in the period the related services are rendered and such estimated amounts are revised in future periods as adjustments become known.

Premium Revenue

The Organization has agreements with various Medi-Cal Managed Care Organizations (MCOs) to provide medical services to subscribing participants. Under these agreements, the Organization receives monthly capitation payments based on the number of each MCO's participants, regardless of the services actually performed by the Organization. In addition, the MCOs make fee-for-service payments to the Organization for certain covered services based upon discounted fee schedules.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Contributions

Unconditional gifts expected to be collected within one year are reported at their net realizable value. Unconditional gifts expected to be collected in future years are initially reported at fair value determined using the discounted present value of estimated future cash flows technique. The resulting discount is amortized using the level-yield method and is reported as contribution revenue.

Gifts received with donor stipulations are reported as either temporarily or permanently restricted net assets. When a donor restriction expires, that is, when a time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified and reported as an increase in unrestricted net assets. Conditional contributions are reported as liabilities until the condition is eliminated or the contributed assets are returned to the donor.

Government Grant Revenue

Support funded by grants is recognized as the Organization performs the contracted services or incurs outlays eligible for reimbursement under the grant agreements. Grant activities and outlays are subject to audit and acceptance by the granting agency and, as a result of such audit, adjustments could be required.

In-Kind Contributions

In addition to receiving cash contributions, the Organization receives in-kind contributions of rent and pharmaceutical supplies. For the years ended December 31, 2013 and 2012, \$821,828 and \$1,312,550 was received in in-kind contributions, respectively.

Income Taxes

The Organization has been recognized as exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, the Organization is subject to federal income tax on any unrelated business taxable income.

Electronic Health Records Incentive Program

The Electronic Health Records Incentive Program, enacted as part of the *American Recovery and Reinvestment Act of 2009*, provides for one-time incentive payments under both the Medicare and Medicaid programs to eligible federally qualified health centers that demonstrate meaningful use of certified electronic health records technology (EHR). Payments under the Medicare program are generally made for up to four years based on a statutory formula. Payments under the Medicaid program are generally made for up to six years based upon a statutory formula, as determined by the State, which is approved by the Centers for Medicare and Medicaid Services. Payment under both programs are contingent on the Organization continuing to meet escalating meaningful use criteria and any other specific requirements that are applicable for the reporting period. The final amount for any payment year is determined based upon an audit by the State, fiscal intermediary or Medicare Administrative Contractor. Events could occur that would cause the final amounts to differ materially from the initial payments under the program.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

The Organization recognizes revenue ratably over the reporting period starting at the point when management is reasonably assured it will meet all of the meaningful use objectives and any other specific grant requirements applicable for the reporting period.

For the years ended December 31, 2013 and 2012, \$289,000 and \$159,750, respectively, was recorded as revenue, which is included in other revenue in the statements of operations.

Excess (Deficiency) of Revenues Over Expenses

The statements of operations include excess (deficiency) of revenues over expenses. Changes in unrestricted net assets which are excluded from excess (deficiency) of revenues over expenses, consistent with industry practice, include contributions or grants of long-lived assets (including assets acquired using contributions or grants which by donor or granting agency restriction are to be used for the purpose of acquiring such assets).

Subsequent Events

Subsequent events have been evaluated through the date of the Independent Auditor's Report, which is the date the financial statements were available to be issued.

Note 2: Grant Revenue

The Organization is the recipient of a Consolidated Health Centers (CHC) grant from the U.S. Department of Health and Human Services. The general purpose of the grant is to provide expanded health care service delivery for residents of Los Angeles, California, and surrounding areas. Terms of the grant generally provide for funding of the Organization's operations based on an approved budget. Grant revenue is recognized as qualifying expenditures are incurred over the grant period. During the years ended December 31, 2013 and 2012, the Organization recognized \$4,553,288 and \$3,748,705 in CHC grant revenue, respectively. The Organization's present CHC grant awards covers the grant period ended February 28, 2014, and is authorized at \$4,608,525. Funding for the grant year ending February 28, 2015, is also authorized at \$5,151,388.

The federal government passed legislation appropriating grant dollars to community health centers for construction and renovation projects under the *Affordable Care Act (ACA)*. The Organization was awarded \$9,482,804 under the ACA-Capital Development Grants program for the period of October 1, 2010, to September 30, 2013, for facility construction and renovation and \$500,000 under the ACA-School-Based Health Centers Capital Program for the period of July 1, 2011, to June 30, 2013, for school-based facility construction and renovation. During the years ended December 31, 2013 and 2012, the Organization recognized \$3,203,241 and \$225,680 in ACA grant revenue, respectively.

In addition to the aforementioned grants, the Organization receives financial support from other federal, state and private sources. Generally, such support requires compliance with terms and conditions specified in grant agreements and must be renewed on an annual basis.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Note 3: Net Patient Service Revenue

The Organization recognizes patient service revenue associated with services provided to patients who have third-party payer coverage on the basis of contractual rates for the services rendered. For uninsured patients that do not qualify for the sliding fee program, the Organization recognizes revenue on the basis of its standard rates for service provided. On the basis of historical experience, a significant portion of the Organization's uninsured patients who do not qualify for the sliding fee program will be unable or unwilling to pay for the services provided. Thus the Organization records a provision for uncollectible accounts related to uninsured patients who do not qualify for the sliding fee program in the period the services are provided. This provision for uncollectible accounts is presented on the statement of operations as a component of net patient service revenue.

The Organization is approved as a Federally Qualified Health Center (FQHC) for both Medicare and Medi-Cal reimbursement purposes. The Organization has agreements with third-party payers that provide for payments to the Organization at amounts different from its established rates. These payment arrangements include:

Medicare. Covered FQHC services rendered to Medicare program beneficiaries are paid based on a cost reimbursement methodology. The Organization is reimbursed for cost reimbursable items at a tentative rate with final settlement determined after submission of an annual cost report by the Organization and audit thereof by the Medicare fiscal intermediary. Services not covered under the FQHC benefit are paid based on established fee schedules.

Medi-Cal. Covered FQHC services rendered to Medi-Cal program beneficiaries are paid based on a prospective reimbursement methodology. The Organization is reimbursed a set encounter rate for all services provided. Services not covered under the FQHC benefit are paid based on established fee schedules.

The Organization is required to submit an annual Medi-Cal Reconciliation Request Form to the California Department of Health Care Services (the "Department") for purposes of determining whether it was paid appropriately for certain Medi-Cal visits. These annual reconciliations result in the determination of any underpayment or overpayment by the Medi-Cal program for the affected visits. The Organization has recorded a receivable for estimated settlements expected to be received for Medi-Cal Reconciliation Request Forms for the years ended December 31, 2006 through 2013. Such amounts are recorded on the balance sheets as amounts due from third-party payers. Following submission of the Medi-Cal Reconciliation Request Form, the Organization will generally receive a tentative settlement from the Medi-Cal program with a final settlement made within three years of the date of submission. Due to the timing of the interim and final settlement processes, the Organization has classified a portion of the amount as a noncurrent asset.

Laws and regulations governing the Medicare and Medicaid programs are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

The Organization is a partner in the Healthy Way LA (HWLA) Program with the County of Los Angeles, which replaced the Public/Private Partnership (PPP) Program. Covered primary care services rendered to HWLA beneficiaries are paid by the County of Los Angeles to the extent of the County's contracted maximum obligation.

The Organization has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations and preferred provider organizations. The basis for payment to the Organization under these agreements includes prospectively determined rates and discounts from established charges.

There was no significant provision for uncollected accounts recorded for the years ended December 31, 2013 and 2012. Patient service revenue, net of contractual allowances and discounts, recognized in the years ended December 31, 2013 and 2012, respectively, was:

	2013	2012
Medi-Cal	\$ 7,626,082	\$ 6,804,325
Medicare	206,974	123,774
County of Los Angeles	9,318,503	7,015,002
Self-pay and other	145,028	268,589
 Total	 \$ 17,296,587	 \$ 14,211,690

Note 4: Concentration of Credit Risk

The Organization grants credit without collateral to its patients, most of whom are area residents and are insured under third-party payer agreements. The mix of receivables from patients and third-party payers at December 31, 2013 and 2012, was:

	2013	2012
Medi-Cal	27%	38%
Medicare	1%	1%
County of Los Angeles	71%	58%
Other third-party payers	1%	3%
	100%	100%

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Note 5: Contributions Receivable

Contributions receivable at December 31, 2013 and 2012, consisted of the following:

	<u>2013</u>	<u>2012</u>
Temporarily restricted		
Due within one year	\$ 1,215,915	\$ 1,257,228
Due in one to five years	<u>28,483</u>	<u>250,000</u>
	1,244,398	1,507,228
Less		
Unamortized discount	<u>875</u>	<u>7,519</u>
	<u>\$ 1,243,523</u>	<u>\$ 1,499,709</u>

The discount rate for both 2013 and 2012 was 3%.

Note 6: Medical Malpractice Claims

The U.S. Department of Health and Human Services deemed the Organization and its practicing physicians covered under the Federal Tort Claims Act (FTCA) for damage for personal injury, including death, resulting from the performance of medical, surgical, dental and related functions. FTCA coverage is comparable to an occurrence policy without a monetary cap.

Claim liabilities are to be determined without consideration of insurance recoveries. Expected recoveries are presented separately. Based upon the Organization's claim experience, no accrual has been made for medical malpractice costs for the years ended December 31, 2013 and 2012. However, because of the risk in providing health care services, it is possible that an event has occurred which will be the basis of a future material claim.

Note 7: Line of Credit

The Organization has a revolving line of credit in the amount of \$1,000,000 which matured on January 1, 2014. Interest is payable monthly at a rate of the greater of 3.50% or the bank's prime rate plus 1% (4.25% at December 31, 2013). The line is collateralized by substantially all of the Organization's assets except real estate. At December 31, 2013 and 2012, the Organization had no outstanding borrowings against this line of credit.

On January 14, 2014, the Organization obtained a new revolving line of credit in the amount of \$700,000 which matures on October 1, 2014. Interest is payable monthly at a rate of the greater of 2.5% or the bank's prime rate plus 1%. The line is collateralized by substantially all of the Organization's assets except real estate.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Note 8: Long-Term Debt

	2013	2012
City National Bank (A)	\$ 752,008	\$ 790,937
City National Bank (B)	613,333	773,333
Series 2011 revenue bonds (C)	5,187,500	5,277,500
NCB Capital Impact (D)	3,450,000	-
GoWest capital lease obligation (E)	115,667	311,444
Avaya financial capital lease obligation (F)	75,827	96,039
	10,194,335	7,249,253
Less current maturities	4,332,390	1,118,343
Less unamortized discount on bonds	74,980	77,665
	\$ 5,786,965	\$ 6,053,245

- (A) Due June 2026; payable \$7,171 monthly, including interest at 6.0%; secured by certain real estate, subordinated to the NCB Capital Impact note.
- (B) Due October 2017; principal payable monthly at \$13,333; interest accrued on the note is payable monthly at a rate of the greater of 3.50% or the bank's prime rate plus 1% (4.25% at December 31, 2013); secured by certain real estate. This note was paid in full subsequent to year-end as part of a conditional requirement of financing related to the NCB Capital Impact note (D). Accordingly, the outstanding balance due under this note has been classified as a current liability at December 31, 2013.

In connection with this note, the Organization is required to maintain a cash flow from operations to debt service ratio of at least 1.5. This covenant was not met for the year ended December 31, 2013. Management has reported the noncompliance to the bank and the bank has decided to take no action against the Organization based solely on the default status of this covenant for the year ended December 31, 2013.

- (C) The Revenue Bonds (Series 2011) consist of Insured Revenue Bonds in the original amount of \$5,370,000 dated November 30, 2011, which bear interest at 4% to 5.625%. The Bonds are payable in annual sinking fund installments and three principal payments. Annual sinking fund installments are payable from November 30, 2012, to November 30, 2041, and fluctuate between \$85,000 and \$330,000, respectively. The three principal payments are \$120,000, \$200,000 and \$345,000 due on November 30, 2021, November 30, 2031 and November 30, 2041, respectively. Bonds maturing on or after December 1, 2020, are subject to redemption prior to their stated maturity at the option of the Organization, in whole or in part by lot on any date, upon at least 45 days prior written notice to the Trustee, on or after December 1, 2019. Bonds redeemed December 1, 2019, through November 30, 2020, are subject to a redemption premium of 2%; bonds redeemed December 1, 2020, through November 30, 2021, are subject to a redemption premium of 1%; bonds redeemed December 1, 2021, and thereafter are not subject to a redemption premium.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

The regulatory agreement requires that certain funds be established with the trustee. Accordingly, these funds are included as assets limited as to use held by trustee in the financial statements. The indenture agreement also requires the Organization to comply with certain restrictive covenants including maintaining a ratio of net income available for debt service to maximum aggregate annual debt service of at least 1.25, maintaining a current ratio of at least 1.5 and maintaining at least 30 days of expenses in cash.

These three covenants were not met for the year ended December 31, 2013. Management has reported the noncompliance to the bond insurer and bank and both parties have decided to take no action against the Organization based solely on the default status of these covenants for the year ended December 31, 2013.

- (D) Construction loan payable in the original amount of \$3,450,000 with a fixed interest rate at 3.94% is due September 2024. Interest only payments began April 2013 and are due monthly for 18 months. Monthly principal and interest payments begin October 2014, in the amount of \$34,831. The construction loan is secured by subordinated deeds of trust on real property.

The loan agreement also requires the Organization to comply with certain restrictive covenants including maintaining a debt service coverage ratio of at least 1.15, maintaining a leverage ratio of less than 1.5 and maintaining a current ratio of at least 1.5. These covenants were not met for the year ended December 31, 2013. Accordingly, the outstanding balance due under this note has been classified as a current liability at December 31, 2013.

- (E) At imputed interest of 8%, due through May 2014; collateralized by equipment.
(F) At imputed interest of 6.27%, due through March 2017; collateralized by equipment.

Property and equipment included the following equipment under capital lease:

	2013	2012
Equipment	\$ 587,801	\$ 587,801
Less accumulated depreciation	<u>268,758</u>	<u>151,198</u>
	<u>\$ 319,043</u>	<u>\$ 436,603</u>

St. John's Well Child and Family Center, Inc.

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Aggregate annual maturities of long-term debt and payments on capital lease obligations at December 31, 2013, are:

	Long-Term Debt (Excluding Capital Lease Obligations)	Capital Lease Obligations
2014	\$ 4,195,205	\$ 145,142
2015	139,465	25,661
2016	147,106	25,661
2017	155,142	7,095
2018	162,836	-
Thereafter	<u>5,203,087</u>	<u>-</u>
	<u>\$ 10,002,841</u>	203,559
Less amount representing interest		<u>12,065</u>
Present value of future minimum lease payments		<u>191,494</u>
Less current maturities		<u>137,185</u>
Noncurrent portion		<u>\$ 54,309</u>

Note 9: Temporarily Restricted Net Assets

Temporarily restricted net assets are available for the following purpose or periods:

	2013	2012
Health care services		
Purchase of equipment	\$ 453,887	\$ 27,000
Indigent care	1,965,119	2,127,357
Health education	403,587	57,645
Pharmaceutical program	136,198	166,271
Time restricted	<u>32,549</u>	<u>1,052,810</u>
	<u>\$ 2,991,340</u>	<u>\$ 3,431,083</u>

During 2013, net assets were released from donor restrictions by incurring expenses, satisfying the restricted purposes of purchase of equipment, indigent care, health care education and pharmaceutical program in the amount of \$2,552,461. During 2012, net assets were released from donor restrictions by incurring expenses, satisfying the restricted purposes of purchase of equipment, indigent care, health care education and pharmaceutical program in the amount of \$2,119,457.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Note 10: Functional Expenses

The Organization provides health care services primarily to residents within its geographic area. Expenses related to providing these services are as follows:

	<u>2013</u>	<u>2012</u>
Health care services	\$ 24,386,537	\$ 21,604,036
General and administrative	6,690,933	4,606,554
Fundraising	<u>815,799</u>	<u>823,449</u>
	<u>\$ 31,893,269</u>	<u>\$ 27,034,039</u>

Note 11: Operating Leases

The Organization has noncancellable operating leases for primary care outpatient offices and equipment which expire in various years through 2020.

Future minimum lease payments at December 31, 2013, were:

2014	\$ 230,471
2015	192,608
2016	108,397
2017	72,598
2018	49,302
Thereafter	<u>33,489</u>
Future minimum lease payments	<u>\$ 686,865</u>

Note 12: Pension Plan

The Organization has a 403(b) defined contribution plan covering substantially all employees. Any employer contributions are discretionary in nature and are subject to reduction or termination. Contributions were suspended after October 31, 2009 and have not yet been reinstated. The Organization did not record retirement plan expense for the years ended December 31, 2013 and 2012.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Note 13: Construction in Progress

At December 31, 2013, the Organization has construction in progress related to the \$13,180,000 Williams/Hoover Campus renovation project. As of December 31, 2013, \$5,157,125 of this work had been completed and is classified as construction in progress on the Organization's balance sheet. This project is primarily funded under an Affordable Care Act grant from the Health Resource Services Administration (HRSA) for \$9,400,000, as well as a \$3,450,000 loan with NCB Capital Impact (see *Note 8*).

At December 31, 2013, the Organization has construction in progress related to the renovation of the Hyde Park Clinic. As of December 31, 2013, \$41,789 of this work has been completed and is classified as construction in progress on the Organization's balance sheet. Continuation of this project is dependent on the availability of additional federal grant and other funding.

During 2012, the Organization began implementing a dental digital x-ray system. As of December 31, 2013, \$184,127 of costs have been incurred for hardware and software purchases related to this project and are classified as construction in progress on the Organization's balance sheet. The Organization plans to complete the installation of digital x-ray and Electronic Dental Record (EDR) software, funded by a Henry Schein grant, in 2014.

Note 14: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

Grant Revenues

Concentration of revenues related to grant awards and other support is described in *Note 2*.

Allowance for Net Patient Service Revenue Adjustments

Estimates of allowances for adjustments included in net patient service revenue are described in *Notes 1* and *3*.

Medical Malpractice Claims

Estimates related to the accrual for medical malpractice claims are described in *Note 6*.

St. John's Well Child and Family Center, Inc.

Notes to Financial Statements

December 31, 2013 and 2012

Litigation

In the normal course of business, the Organization is, from time to time, subject to allegations that may result in litigation. The Organization evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of counsel, management records an estimate of the amount of the ultimate expected loss, if any, for each of these matters. Events could occur that would cause the estimate of loss to differ materially in the near term.

Labor Agreement

The Organization entered into an agreement with Service Employees International Union, Local 721 for the period March 1, 2011, through February 28, 2014. Approximately 61% of employees are covered under this agreement. Management continues operating under this agreement while negotiations are ongoing.

Current Economic Conditions

The current economic environment presents community health centers with difficult circumstances and challenges. As employers make adjustments to health insurance plans or more patients become unemployed, certain patients may find it difficult to pay for services rendered. The continuing implementation of the *Affordable Care Act*, including the health insurance exchanges and the decision by the state regarding Medicaid expansion, will directly impact community health centers' net revenues. Further, the effect of economic conditions on federal and state budgets could adversely impact the grant revenues available to community health centers and the programs they administer. Each of these factors could have an adverse impact on the Organization's future operating results.