

MARRAKECH, INC.

**Consolidated Financial Statements
and Supplementary Information
with Independent Auditor's Report**

June 30, 2018 and 2017

MARRAKECH, INC.

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INDEPENDENT AUDITOR'S REPORT



GUILMARTIN ▪ DIPIRO ▪ SOKOLOWSKI LLC

CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITOR'S REPORT

The Board of Directors
Marrakech, Inc.:

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Marrakech, Inc. (a nonprofit organization), which comprise the consolidated statements of financial position as of June 30, 2018 and 2017, and the related consolidated statements of activities, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of 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 consolidated financial statements based on our audits. We conducted our audits 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 audits to obtain reasonable assurance about whether the consolidated 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 judgement, 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Marrakech, Inc. as of June 30, 2018 and 2017, and 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.

Other Matters

Other Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedules 1 through 3 are presented for purposes of additional analysis and are not a required part of the basic consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 25, 2019 on our consideration of Marrakech, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and 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 Marrakech, Inc.'s internal control over financial reporting and compliance.

Guilmodio D.P. + Sokolowski, LLC

Middletown, Connecticut

January 25, 2019

FINANCIAL STATEMENTS

MARRAKECH, INC.

Consolidated Statements of Financial Position

June 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
<u>Assets</u>		
Current assets:		
Cash	\$ 3,180,234	\$ 1,670,060
Accounts receivable, net of allowance for doubtful accounts of \$309,000 in 2018 and \$393,000 in 2017	1,833,280	2,469,617
Prepaid expenses	<u>584,906</u>	<u>571,255</u>
Total current assets	<u>5,598,420</u>	<u>4,710,932</u>
Property and equipment, net	10,273,128	10,638,956
Other assets:		
Investments - endowment	48,666	27,567
Derivative debt agreements	5,090	-
Other assets	<u>27,426</u>	<u>22,963</u>
	<u>81,182</u>	<u>50,530</u>
Total assets	<u>\$ 15,952,730</u>	<u>\$ 15,400,418</u>
<u>Liabilities and Net Assets</u>		
Current liabilities:		
Accounts payable	\$ 443,266	\$ 286,955
Accrued liabilities	2,406,332	2,093,907
Due to grantors	685,826	467,177
Deferred revenue, current portion	99,758	165,767
Current portion of mortgages and loans payable	<u>879,033</u>	<u>438,870</u>
Total current liabilities	<u>4,514,215</u>	<u>3,452,676</u>
Long-term liabilities:		
Mortgages payable, less current portion	4,355,024	4,689,423
Loans payable, less current portion	493,231	837,922
Derivative debt agreements	-	21,662
Deferred revenue, less current portion	133,989	192,754
DDS cash advances	599,046	429,909
Contingent liabilities (see Note 13)	-	-
Total long-term liabilities	<u>5,581,290</u>	<u>6,171,670</u>
Total liabilities	<u>10,095,505</u>	<u>9,624,346</u>
Net assets:		
Unrestricted	5,754,983	5,678,570
Temporarily restricted	<u>102,242</u>	<u>97,502</u>
Total net assets	<u>5,857,225</u>	<u>5,776,072</u>
Total liabilities and net assets	<u>\$ 15,952,730</u>	<u>\$ 15,400,418</u>

See accompanying notes to financial statements.

MARRAKECH, INC.

Consolidated Statements of Activities

For the years ended June 30, 2018 and 2017

<u>Changes in Unrestricted Net Assets</u>	<u>2018</u>	<u>2017</u>
Revenue and other support:		
Operating revenue (Schedule 1)	\$ 31,258,251	\$ 32,839,752
Donations and fund-raising	444,350	565,669
Net assets released from restrictions	<u>38,344</u>	<u>16,744</u>
Total unrestricted revenue and other support	<u>31,740,945</u>	<u>33,422,165</u>
Operating expenses:		
Salary	20,450,818	21,249,760
Non-salary (Schedule 2)	7,313,632	8,015,207
Employee benefits (Schedule 3)	<u>3,950,730</u>	<u>4,056,950</u>
Total operating expenses	<u>31,715,180</u>	<u>33,321,917</u>
Change in unrestricted net assets before other income	<u>25,765</u>	<u>100,248</u>
Other income (loss):		
Change in fair value of derivative debt agreements	26,752	19,115
Unemployment tax refunds	23,896	151,570
Loss on disposal of operating segment	<u>-</u>	<u>(308,027)</u>
Total other income (loss)	<u>50,648</u>	<u>(137,342)</u>
Change in unrestricted net assets	76,413	(37,094)
Unrestricted net assets, beginning of year	<u>5,678,570</u>	<u>5,715,664</u>
Unrestricted net assets, end of year	<u>\$ 5,754,983</u>	<u>\$ 5,678,570</u>
<u>Changes in Temporarily Restricted Net Assets</u>		
Donations	\$ 43,084	\$ 31,600
Net assets released from restrictions	<u>(38,344)</u>	<u>(16,744)</u>
Change in temporarily restricted net assets	<u>4,740</u>	<u>14,856</u>
Temporarily restricted net assets, beginning of year	<u>97,502</u>	<u>82,646</u>
Temporarily restricted net assets, end of year	<u>\$ 102,242</u>	<u>\$ 97,502</u>
Total change in net assets	<u>\$ 81,153</u>	<u>\$ (22,238)</u>

See accompanying notes to financial statements.

MARRAKECH, INC.

Consolidated Statements of Cash Flows

For the years ended June 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities:		
Change in net assets	\$ <u>81,153</u>	\$ <u>(22,238)</u>
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	779,025	856,001
Unrealized (gain) on investments	(1,235)	(1,191)
(Increase) in fair value of derivative debt agreements	(26,752)	(19,115)
(Gain) loss on disposal of assets	(5,437)	322,750
Decrease (increase) in accounts receivable	665,555	(90,097)
(Increase) decrease in prepaid expenses	(13,651)	276,394
(Increase) in other assets	(4,840)	(3,275)
Increase (decrease) in accounts payable	156,311	(13,128)
Increase (decrease) in accrued liabilities	312,425	(249,892)
Increase (decrease) in due to grantors	218,649	(28,465)
(Increase) in due from others	(29,218)	(17,841)
(Decrease) in deferred revenue	(124,774)	(9,571)
Increase in DDS cash advances	169,137	-
Total adjustments	<u>2,095,195</u>	<u>1,022,570</u>
Net cash provided by operating activities	<u>2,176,348</u>	<u>1,000,332</u>
Cash flows from investing activities:		
Purchase of investments	(19,864)	(26,376)
Purchase of property and equipment	(412,820)	(1,753,470)
Net cash (used) by investing activities	<u>(432,684)</u>	<u>(1,779,846)</u>
Cash flows from financing activities:		
Proceeds of long-term debt	212,899	943,737
Principal payments on loans	(451,826)	(573,696)
Cash proceeds from disposal of property	5,437	469,564
Net cash (used) provided by financing activities	<u>(233,490)</u>	<u>839,605</u>
Net increase in cash	1,510,174	60,091
Cash, beginning of year	<u>1,670,060</u>	<u>1,609,969</u>
Cash, end of year	<u>\$ 3,180,234</u>	<u>\$ 1,670,060</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest expense	<u>\$ 313,403</u>	<u>\$ 387,547</u>
Non-cash investing and financing activities:		
Payoff of loans on sales of properties	<u>\$ -</u>	<u>\$ 1,636,618</u>
Security deposit liabilities assumed by buyer on sales of properties	<u>\$ -</u>	<u>\$ 1,200</u>
Derivative debt liability assumed by buyer on sale of property	<u>\$ -</u>	<u>\$ 231,612</u>

See accompanying notes to financial statements.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

NOTE 1

ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of organization

These consolidated financial statements include Marrakech, Inc. and its sister corporations, Marrakech Housing Options, Inc., Marrakech Day Services, Inc. and Marrakech Residential Services, Inc. (the Agencies).

Marrakech, Inc. operates programs for persons with disabilities in the State of Connecticut. Additionally, it provides management services for Marrakech Housing Options, Inc., Marrakech Day Services, Inc. and Marrakech Residential Services, Inc.

Marrakech Housing Options, Inc. and Marrakech Residential Services, Inc. operate private group homes, community residential supported living arrangements and day programs for persons with disabilities in the State of Connecticut. The operating revenue for the Agencies comes primarily from the Connecticut Departments of Developmental Services (DDS) and Social Services (DSS) and the Social Security Administration (SSA).

Marrakech Day Services, Inc. operates vocational day programs which are licensed by the State of Connecticut for disadvantaged and developmentally disabled persons. It is principally funded through cost reimbursements from the State of Connecticut Department of Mental Health and Addiction Services (DMHAS).

The accounting policies of Marrakech, Inc. and its sister corporations conform to accounting principles generally accepted in the United States of America applicable to nonprofit organizations.

Marrakech, Inc. and its sister corporations, except for Marrakech Residential Services, Inc. fiscal years end on June 30th. Marrakech Residential Services, Inc.'s fiscal year ends on September 30th.

The following is a summary of the more significant policies:

Basis of presentation

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. The Agencies report information regarding their financial position and activities

according to three classes of net assets: unrestricted, temporarily restricted and permanently restricted. They are described as follows:

Unrestricted - Net assets that are not subject to explicit donor-imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of the Board of Directors.

Temporarily restricted - Net assets whose use by the Agencies are subject to either explicit donor-imposed stipulations or by operation of law that can be fulfilled by actions of the Agencies or that expire by the passage of time.

Permanently restricted - Net assets subject to explicit donor-imposed stipulations that they be maintained permanently by the Agencies and stipulate the use of income and/or appreciation as temporarily restricted based on donor-imposed stipulations or by operation of law. The Agencies had no permanently restricted net assets as of June 30, 2018 and 2017.

Use of estimates

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

Income tax status

The Agencies have received exemption from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. The Agencies have also been classified as entities that are not private foundations within the meaning of Section 509(a) and qualify for deductible contributions as provided in Section 170(b)(1)(A)(vi).

Management has reviewed the Agencies' reporting and believe that no tax positions have been taken that are more likely than not to be determined to be incorrect by the Internal Revenue Service and therefore no adjustments or disclosures are required. The Agencies are subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods pending or in progress.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Cash and cash equivalents

For the purpose of the consolidated statements of cash flows, the Agencies consider all highly liquid investments with an original maturity of three months or less to be cash equivalents. The Agencies had no cash equivalents as of June 30, 2018 and 2017.

Accounts receivable

The Agencies have accounts receivable related to grants and third party reimbursements. Based on historical experience, grants are considered fully collectible. Management performs an assessment of collectability related to other receivables and will write off receivables from individuals and other sources after all attempts at collection are exhausted. When appropriate, management maintains an allowance for doubtful accounts, which is based on a review of significant delinquent balances and past collection experience. The allowance for doubtful accounts at June 30, 2018 and 2017 was \$309,000 and \$393,000 respectively.

Property and equipment

The Agencies follow the practice of capitalizing at cost all property and equipment with costs in excess of stated amounts as required by the Agencies' funding sources. Depreciation is computed using the straight-line method over the estimated useful lives of the assets which range from 3 to 30 years. Repairs and maintenance are charged to expense as incurred. For assets sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected in change in net assets for the period.

The Agencies review long-lived assets for impairment using an undiscounted cash flow method whenever events or circumstances indicate the carrying value of an asset may not be recoverable. There were no impairment losses related to long-lived assets as of June 30, 2018 and 2017.

Derivative debt agreements and interest rate risk management

Marrakech, Inc. has entered into variable rate debt agreements (interest rate swap loans) related to mortgages owed on several of its properties. These arrangements enabled Marrakech, Inc. to fix the currently low interest rates on these obligations for ten years. Under the interest rate swap contracts, Marrakech, Inc. agrees to pay an amount equal to a specified fixed rate of interest times a notional principal amount, and to receive in return an amount equal to a specified variable rate of interest times a notional amount.

No other cash payments are made unless the contract is terminated prior to maturity, in which case the amount paid or received in settlement is established by agreement at the time of the termination and usually represents the net present value, at current rates of interest, of the remaining obligations to exchange payments under the term of the contract. Marrakech, Inc. accounts for these swaps as cash flow hedges. Marrakech, Inc. does not issue or hold derivative contracts for speculative purposes.

Grants and contracts

Governmental grants and contracts are generally considered to be exchange transactions rather than contributions. Revenue from cost reimbursement grants and contracts is recognized to the extent of costs incurred. Revenue from performance-based grants and contracts is recognized to the extent of performance achieved. Grant and contract receipts in excess of allowable expenditures are recorded on the consolidated statements of financial position as deferred revenue if the grant extends beyond the Agencies' fiscal year and as due to grantor if the grant was completed within the fiscal year.

Individuals who are provided services receive funds from the Connecticut Department of Social Services (DSS) and other sources which are passed through the Agencies as room and board fees.

Bond revenue

Contributions received under grant-in-aid bonding and other agreements, to finance the acquisition and development of property to be dedicated to a specific use over a required number of years, are recorded as deferred revenue on the Agencies' consolidated statements of financial position. Revenue is then recognized ratably over the restricted use period as the liability for repayment to the donor is reduced by any applicable forgiveness provisions.

Contributions

Unconditional contributions are recognized when pledged or received, as applicable, and are considered to be available for unrestricted use unless specifically restricted by the donor. Contributions receivable expected to be collected in more than one year are discounted to their present value. The Agencies report contributions and grants of cash and other assets as temporarily restricted support if they are received with donor stipulations that limit their use. When a donor restriction expires, that is, when the stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as assets released

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Contributions, continued

from restrictions. If temporarily restricted support is received and the restriction is satisfied within the same fiscal year, the support is reported as unrestricted. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

The Agencies report gifts of property and equipment as unrestricted support unless explicit donor stipulations specify how the assets are to be used. Gifts of long-lived assets with explicit restrictions on how the assets are to be used and gifts of cash or other assets that must be used to acquire property and equipment are reported as restricted support. Absent donor stipulations about how long those assets must be maintained, the Agencies report expirations of donor restrictions when the assets are placed in service.

Contributed services are recognized in the consolidated financial statements if they enhance nonfinancial assets or require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. General volunteer services do not meet these criteria for recognition. However, many volunteers have donated significant amounts of time in supporting the Agencies' mission and fundraising campaigns.

Cost settlement

The Agencies are subject to cost settlement procedures prescribed by various agencies of the State of Connecticut. Management's estimates of all cost settlements due are included as current liabilities on the consolidated statements of financial position in "Due to grantors."

Endowment and spending policy

The Agencies have adopted investment and spending policies for endowment assets that attempt to provide a reasonably predictable stream of funding for programs supported by their endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include an annual allocation of 5% of the Agencies' net fund-raising income subject to the discretion of Marrakech's board of directors. Under this policy, the endowment assets are invested in accordance with sound investment practices that emphasize long-term investment fundamentals. It is recognized that short-term market fluctuations may cause variations in account performance.

To satisfy its long-term rate of return objectives, the Agencies assume a conservative level of investment risk and hold their investments in a professionally managed investment account consisting of global equity and bond funds and private assets. This is consistent with the Agencies' objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return. Under the board of directors' discretion, management may access these funds at any time for the Agencies' use and the endowment is completely revocable.

Fund-raising

Marrakech, Inc. conducts various fund-raising activities during the year including various special events and appeals for donations. The total cost of fund-raising activities was \$154,367 and \$121,762 for the years ended June 30, 2018 and 2017, respectively which included salary and benefits associated with Marrakech, Inc. staff involved in fund-raising activities of \$20,172 in each respective year.

Subsequent events

The Agencies have evaluated events and transactions for potential recognition or disclosure through January 25, 2019, which is the date the consolidated financial statements were available to be issued.

NOTE 2

CONCENTRATIONS

The Agencies maintain their cash balances with high-credit quality financial institutions. At times, such amounts may exceed federal depository insurance limits. At June 30, 2018 the cash balance exceeded the federally insured limit by \$2,679,577.

A substantial portion of the Agencies' revenue is derived from government grants and contracts. Since the contracts are evidenced by signed contracts with government and other agencies, management believes there is nominal credit risk associated with any outstanding grants receivable.

The following tables show the Agencies' highest concentrations of revenues and receivables from these grants and contracts for the years ended June 30, 2018 and 2017:

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Concentrations, continued

2018			<u>2018</u>	<u>2017</u>	
	Percentage of Total				
	<u>Revenue</u>	<u>Receivable</u>			
State of Connecticut Department of Developmental Services	60%	43%	DDS accounts receivable	\$2,334,085	\$1,108,844
State of Connecticut Department of Social Services	11%	9%	Less: DDS advance	<u>1,538,071</u>	<u>-</u>
State of Connecticut Department of Mental Health and Addiction Services	<u>13%</u>	<u>0%</u>	Net DDS receivable	796,014	1,108,844
	<u>84%</u>	<u>52%</u>	Other receivables	1,346,266	1,753,773
			Less: allowance for doubtful accounts	<u>309,000</u>	<u>393,000</u>
			Accounts receivable, net	<u>\$1,833,280</u>	<u>\$2,469,617</u>

2017			<u>2018</u>	<u>2017</u>	
	Percentage of Total				
	<u>Revenue</u>	<u>Receivable</u>			
State of Connecticut Department of Developmental Services	58%	45%	Furniture and equipment	\$ 1,618,918	\$ 1,446,963
State of Connecticut Department of Social Services	13%	12%	Transportation equipment	3,796,488	3,626,315
State of Connecticut Department of Mental Health and Addiction Services	<u>13%</u>	<u>0%</u>	Buildings, land and improvements	15,620,410	15,608,096
	<u>84%</u>	<u>57%</u>	Construction-in-process	<u>66,091</u>	<u>125,589</u>
				21,101,907	20,806,963
			Less: accumulated depreciation	<u>10,828,779</u>	<u>10,168,007</u>
			Total	<u>\$10,273,128</u>	<u>\$10,638,956</u>

NOTE 4
PROPERTY AND EQUIPMENT

Components of property and equipment as of June 30 are as follows:

Depreciation expense was \$778,648 and \$855,552 for the years ended June 30, 2018 and 2017, respectively.

Construction-in-process at June 30, 2018 included costs incurred to build out program and administrative space in various properties throughout the Agencies.

NOTE 3
ACCOUNTS RECEIVABLE/DDS BRIDGE FUNDING ADVANCES

Marrakech Housing Options, Inc. retains bridge funding advances from DDS to fund the cash flow requirements of the Agency's DDS programs in the amount of \$1,538,071 as of June 30, 2018.

As shown below, these advances are offset against DDS accounts receivable on the accompanying consolidated statements of financial position.

NOTE 5
LINES OF CREDIT

Citizens Bank

Marrakech, Inc. has a revolving line of credit with Citizens Bank which expired on July 31, 2018 and was extended to March 31, 2020. Advances on the line of credit are payable on demand and bear interest at a variable rate under the note agreement. The maximum amount which may be withdrawn under the agreement is \$2,500,000. The interest rate was 5.50% and 4.75% as of June 30, 2018 and 2017, respectively and the balances due were \$0 in both years. The obligation has been guaranteed by each Agency.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Lines of credit, continued

Start Community Bank

Marrakech, Inc. had a revolving line of credit agreement with Start Community Bank. Advances on the line of credit bear interest at a variable rate under the agreement, which were payable in full at the maturity date of the agreement unless the advances were converted to a term promissory note with the bank. The maximum amount which could be withdrawn under the agreement was \$600,000. The interest rate and balance due at June 30, 2017 was 5.50% and \$0, respectively. The line of credit was never used during fiscal year June 30, 2018 and was closed at maturity on March 3, 2018.

Key Bank (f/k/a First Niagara Bank)

Revolving credit loan agreement

On October 17, 2013 Marrakech, Inc. entered into a revolving credit loan agreement with Key Bank (f/k/a First Niagara Bank) in order to provide capital on an as needed basis for improvements to the Agency's various properties. The maximum that may be withdrawn under the agreement is \$677,250. Advances on the agreement bear interest, which is payable monthly at the lender's announced prime rate as determined by the lender for calculating interest on certain loans. The agreement matured on September 1, 2018 and was extended to March 15, 2019, at which time the principal balance outstanding and all accrued and unpaid interest and any fees are due. The balances due as of June 30, 2018 and 2017 were \$414,000 in each year. The interest rate on the agreement as of June 30, 2018 and 2017 was 4.25% in both years.

Non-revolving multiple draw term note

On June 26, 2015 Marrakech, Inc. entered in to a non-revolving multiple draw term note with Key Bank (f/k/a First Niagara Bank) to provide capital for equipment purchases. The maximum that may be drawn under the agreement was \$500,000 through June 30, 2016. Advances on the agreement bear interest at the lender's prime rate as determined by the lender for calculating interest on certain loans. After June 30, 2016, the loan became payable in monthly payments of principal and interest through the note's maturity on July 1, 2021. The interest rate during this period will be 2.25% plus the five year advance Federal Home Loan Bank (of New York) rate. As of June 30, 2018 and 2017, the balances owed on the agreement were \$271,460 and \$368,805, respectively and the interest rate was 4.14% in both years.

NOTE 6

LONG-TERM DEBT

Financing for Clinton Harbor facility

Marrakech, Inc.'s debt obligations included two loans of \$1,700,000 and \$1,000,000 during fiscal year 2017, which were obtained to permanently finance prior construction loans for the build-out of their Clinton Harbor property, an intermediate care facility for developmentally disabled individuals. On April 7, 2017, this property was sold and those loans, along with the related additional liabilities under their respective derivative debt agreements (see "interest rate swap loans" below), were assumed by the buyer of the property as part of the sales price. As of June 30, 2018 and 2017, there were no balances owed on the \$1,700,000 and \$1,000,000 loans. The \$1,700,000 and \$1,000,000 loans were payable in equal monthly amounts of principal of \$14,392 and \$2,770, respectively plus interest on each loan's respective monthly balance at 6.88% and 7.17% per annum, respectively. Principal balances on the loans were reset on an annual basis in accordance with each loan's amortization schedule and both loans' scheduled maturities were on January 1, 2021. The \$1,700,000 loan was being amortized on a ten year schedule and the \$1,000,000 loan was amortized over a twenty year time frame. The loans were secured by Marrakech's Clinton Harbor home and Woodbridge main office properties, including all improvements on each.

Interest rate swap loans

The financing for the Clinton Harbor facility discussed above, along with three other loans (which were also received in prior years), have been financed as "interest rate swap loans" as per the terms of a master agreement of the International Swap Dealers Association, Inc. These loans include credit-risk-related contingent features whereby the Agency could incur additional liabilities should the agreements be terminated before maturity by Marrakech, Inc. As discussed above, the Clinton Harbor property was sold on April 7, 2017 and the related two interest rate swap loans under that property's two loan obligations were assumed by the buyer of the property as part of the sales price.

As of the fiscal years ended June 30, 2018 and 2017, the agreements were in net asset and net liability positions totaling \$5,090 and \$21,662, respectively, which is shown on the Agency's consolidated statements of financial position under other assets and long-term liabilities, respectively as "derivative debt agreements." The Agency has recorded net income related to the agreements' changes in fair value of \$26,752 for the fiscal year ended June 30, 2018 and \$19,115 for the fiscal year ended June 30, 2017, as shown on the

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Interest rate swap loans, continued

consolidated statements of activities under “change in fair value of derivative debt agreements”. Please see Note 1 under “Derivative debt agreements and interest rate risk management” for additional information.

Other mortgages and loans

The Agencies have additional mortgages and notes payable as of June 30, 2018 and 2017. Please see the schedule of debt obligations (Table 6.1) and their respective terms at the end of these footnotes.

NOTE 7

DDS CASH ADVANCES

When a facility commences operations, the Agency may receive an operational advance equal to the service revenue for one month based on full capacity. These operational advances are applied against the final reimbursement when a facility ceases their agency relationship with DDS. Total operational advances were \$599,046 and \$429,909 as of the fiscal years ended June 30, 2018 and 2017, respectively.

NOTE 8

OPERATING LEASES

Marrakech, Inc. maintained a lease agreement with an unrelated party to rent property in Milford, Connecticut used for a DCF licensed group home for students enrolled in an academic program sponsored by the lessor. Annual base rent was \$1 plus an annual student rent of \$7,000 per year per student and was due and payable for each full month that a student resided at the premises. Marrakech, Inc. was reimbursed for the annual student rents under the program through the town the student was attending school and, as a result, there is no corresponding expense in the consolidated financial statements for the student rents. This agreement expired March 20, 2018.

Marrakech, Inc. has an informal lease agreement with an unrelated party to rent property in Milford and West Haven, Connecticut on a month-to-month basis. Monthly rent is \$2,564 and \$2,832, respectively. The properties under the lease are used to operate two intermediate care facilities.

Marrakech, Inc. has an operating lease agreement with the State of Connecticut to rent a house in Trumbull, Connecticut for \$1 per year. The lease agreement expired on January 31, 2016 and continues on a month-to-month basis while Marrakech, Inc. awaits approval of a longer term lease from

the State of Connecticut. The house is used to operate a CLA program for DDS.

Marrakech, Inc. has an operating lease agreement with an unrelated party to rent property in Waterbury, Connecticut used for job training programs through December 31, 2019. Monthly rent was \$3,200 as of June 30, 2018 and increases to \$3,300 per month beginning in January 2019.

Marrakech, Inc. has an operating lease agreement with an unrelated party to rent property in Bridgeport, Connecticut used for educational programs, maintenance and vocational rehabilitation programs for \$1,600 per month. The lease agreement expired on May 17, 2018 and continues on a month-to-month basis.

Marrakech, Inc. has an operating lease agreement with an unrelated party to rent property in New Milford, Connecticut used for Day programs through November 30, 2020. Monthly rent is \$6,365 and increases by 3% annually.

Marrakech, Inc. had an informal lease agreement with an unrelated party to rent property in Woodbridge, Connecticut used for a bakery and deli for their employment programs. The lease was terminated on December 15, 2016. Monthly rent was \$500 through the date of termination.

Marrakech, Inc. had an informal lease agreement with an unrelated party to rent property in Clinton, Connecticut used for a Day program. On November 1, 2016 the Day program was transferred to another agency and the lease agreement was terminated. The monthly rent was \$2,000 as of the date of termination.

Marrakech, Inc. had an informal month-to-month lease agreement with an unrelated party to rent property in Middletown, Connecticut used for administrative offices for their Acquired Brain Injury (ABI) program. The month-to-month lease agreement terminated on November 30, 2018. The rent was \$1,100 per month.

Marrakech, Inc. has several other informal lease agreements with unrelated parties to rent houses and apartments for their Young Adult Services Programs through the Connecticut Department of Mental Health and Addiction Services (DMHAS), Community Living Arrangement and Shared Living programs through the Connecticut Department of Developmental Services (DDS) and to provide other services. Rents under these programs are reimbursed by either the state agencies or by Marrakech’s clients and, as a result, there is no corresponding rent expense in the consolidated financial statements.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Operating leases, continued

Related rent expense for the years ended June 30, 2018 and 2017 was \$226,479 and \$286,390, respectively.

At June 30, minimum lease payments due under operating leases for facilities for the next five years ended June 30 are as follows:

2019	\$135,377
2020	100,201
2021	33,659
2022	-
2023	-
Total	<u>\$269,237</u>

NOTE 9

TEMPORARILY RESTRICTED NET ASSETS

At June 30, 2018 and 2017, temporarily restricted net assets are available for the following purposes and amounts:

	<u>2018</u>	<u>2017</u>
Island Lane renovations	\$ 6,170	\$ 6,503
Robbins Street renovations	37,001	39,001
Whalley Avenue renovations	9,885	10,485
106 Sherman Avenue renovations	6,102	9,913
Grant for carpeting	33,800	31,600
Grant for energy efficient windows	<u>9,284</u>	<u>-</u>
	<u>\$102,242</u>	<u>\$97,502</u>

NOTE 10

DEFINED CONTRIBUTION PLAN

The Agencies have adopted a profit sharing plan covering all full-time employees who are at least twenty-one years old and have worked for the Agencies for at least one year. Each participant's interest in the employer's contributions and the earnings thereon are vested 20% after two years of service with an additional 20% vesting for each additional year of service thereafter, up to the maximum vesting of 100%. The Board of Directors determines the amount of the contribution each fiscal year, which is allocated to each participant in the same proportion as his or her compensation bears to the

compensation of all participants. There were no contributions authorized by the Board of Directors for the fiscal years ended June 30, 2018 and 2017.

NOTE 11

ENDOWMENT

The Agencies' endowment may include both donor-restricted endowment funds and funds designated by the Board of Directors to function as endowments. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions. The Board of Directors has interpreted the Connecticut Uniform Prudent Management of Institutional Funds Act (CTUPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Agencies classify as permanently restricted net assets: (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Board of Directors in a manner consistent with the standard of prudence prescribed by CTUPMIFA.

In accordance with CTUPMIFA, the Agencies consider the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund.
2. The purposes of the Agencies and the donor-restricted endowment fund.
3. General economic conditions.
4. The possible effect of inflation and deflation.
5. The expected total return from income and the appreciation (depreciation) of investments.
6. Other resources of the Agencies.
7. The investment policies of the Agencies.

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Endowment, continued

Endowment net asset composition by type of fund as of June 30, 2018 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ -	\$ -	\$ -	\$ -
Board-designated endowment funds	<u>48,666</u>	<u>-</u>	<u>-</u>	<u>48,666</u>
Total funds	<u>\$48,666</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$48,666</u>

Changes in endowment net assets for the year ended June 30, 2018 are as follows:

Endowment net assets, beginning of year	\$27,567	\$ -	\$ -	\$27,567
Board-designated additions	18,500	-	-	18,500
Net realized and unrealized appreciation	2,599	-	-	2,599
Amounts appropriated for expenditure	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Endowment net assets, end of year	<u>\$48,666</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$48,666</u>

From time to time, the fair value of assets associated with donor-restricted endowment funds may fall below the level that the donor or applicable law requires the Agencies to retain as a fund of perpetual duration. As there were no donor-restricted endowment funds, there were no deficiencies as of June 30, 2018.

NOTE 12

BOARD DESIGNATION OF UNRESTRICTED NET ASSETS

The Board of Directors has designated the following unrestricted net assets:

	<u>2018</u>	<u>2017</u>
Endowment	<u>\$48,666</u>	<u>\$27,567</u>

NOTE 13

CONTINGENCIES

Grant funding for acquisition of properties

Certain Marrakech agencies have been awarded grant funding for acquisition of various properties, building improvements and vehicles over several years. These grant awards stipulate that if the Agency were to discontinue usage of the property

for its specified grant purpose, the grant funds would be repayable, either in whole or a ratable portion (depending on years of usage), back to the grantor.

The State of Connecticut has liens on certain properties for the amounts of their respective grants which will terminate on various dates between December 3, 2019 and November 25, 2025. The properties renovated by these state funds continue to be used for their designated purposes as of June 30, 2018.

NOTE 14

DISCONTINUED OPERATIONS

FASB accounting standards update No 2014-08 "Reporting discontinued operations and disclosures of disposals of components of an entity" expands the reporting requirements for disposals which will have a major effect on an entity's results and operations.

On April 7, 2017, Marrakech's Clinton Harbor intermediate care facility and day program were sold to an unrelated entity. The sale price was \$2,145,923 which included cash of \$293,260 plus the buyers' assumption of debt owed on the property including mortgages of \$1,621,051 and the balance on the related derivative debt agreement of \$231,612. Marrakech's depreciated cost of the property and equipment sold was \$2,453,950 and the loss on the disposal was

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Discontinued operations, continued

\$308,027, as shown within other income (loss) on the Agencies' year ended June 30, 2017 consolidated statements of activities.

The Agencies have reported other gains and losses on disposals of assets which do not meet the reporting requirements of ASU No. 2014-08 as part of operating revenue on the consolidated statements of activities.

NOTE 15

FUNCTIONAL EXPENSES

Consolidated functional expenses for the years ended June 30 are as follows:

	<u>2018</u>	<u>2017</u>
Program services	\$29,933,704	\$31,447,035
General and administrative	<u>1,781,476</u>	<u>1,874,882</u>
	<u>\$31,715,180</u>	<u>\$33,321,917</u>

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Table 6.1 - Schedule of Debt Obligations

<u>Lender/Collateral</u>	<u>Interest Rate</u>	<u>Monthly Payment</u>	<u>Maturity Date</u>	<u>2018</u>	<u>2017</u>
<u>Mortgages payable</u>					
CCO Mortgage Corporation 106-108 Sherman Avenue, New Haven, Connecticut	4.25%	\$ 903	05/01/18	\$ -	\$ 8,855
CCO Mortgage Corporation 60 Plainfield Avenue, New Haven, Connecticut	8.25%	270	07/01/30	24,576	25,740
CCO Mortgage Corporation 615-617 Whalley Avenue, New Haven, Connecticut	8.25%	338	08/01/30	30,970	32,407
CCO Mortgage Corporation 106-108 Hobart Street, New Haven, Connecticut	6.50%	484	09/01/31	51,248	53,635
CCO Mortgage Corporation 158R Meetinghouse Road, Durham, Connecticut	5.50%	1,416	03/01/36	191,684	197,939
CCO Mortgage Corporation 27-29 Robbins Street, Waterbury, Connecticut	5.63%	1,151	05/01/36	155,326	160,254
CCO Mortgage Corporation 85 Talmadge Hill Road, Prospect, Connecticut	5.88%	2,395	08/01/36	319,692	329,342
CCO Mortgage Corporation 88-90 Sherman Avenue, New Haven, Connecticut	5.63%	1,891	11/01/36	259,048	266,926
CCO Mortgage Corporation 25 Kreger Drive, Wolcott, Connecticut	5.63%	1,917	06/01/37	267,486	275,207
CCO Mortgage Corporation 32-34 Plant Street, New Haven, Connecticut	4.13%	894	10/01/40	156,069	160,267
Citizens Bank * 514-526 Whalley Avenue, New Haven, Connecticut	5.96%	2,626	05/18/21	81,606	107,402
Citizens Bank * 60 Knollwood Drive, New Haven, Connecticut	4.86%	1,099	12/22/21	166,523	172,252
Citizens Bank * 50 Oak Tree Avenue, Waterbury, Connecticut	4.86%	4,215	12/22/21	513,885	541,251
Connecticut Department of Developmental Services 159 Osborn Avenue, New Haven, Connecticut	6.00%	1,675	06/01/19	17,568	36,010
Connecticut Department of Developmental Services 25 Kreger Drive, Wolcott, Connecticut	6.00%	1,441	07/01/38	201,128	206,185
Connecticut Department of Developmental Services 85 Talmadge Hill Road, Prospect, Connecticut	6.00%	177	07/01/24	10,666	12,101
Connecticut Housing Finance Authority 21 Victor Hill Road, Branford, Connecticut	7.34%	2,017	09/01/26	149,471	162,198
Connecticut Housing Finance Authority 33 Lake Street, West Haven, Connecticut	6.93%	2,343	07/16/27	190,302	204,671
Connecticut Housing Finance Authority 92 Hurd Road, Trumbull, Connecticut	6.63%	1,734	10/01/30	175,034	183,924
Connecticut Housing Finance Authority 92 View Terrace, East Haven, Connecticut	6.63%	1,740	10/01/30	175,658	184,579
Connecticut Housing Finance Authority 2 Anton Circle, Bridgeport, Connecticut	5.75%	2,425	01/01/33	286,808	299,028
Connecticut Housing Finance Authority 29 Briarwood Terrace, Middlebury, Connecticut	3.00%	1,939	01/01/47	446,188	455,909
Connecticut Housing Finance Authority 102 Harwinton Avenue, Plymouth, Connecticut	3.00%	1,783	01/01/47	410,126	419,061

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Table 6.1 - Schedule of Debt Obligations, Continued

<u>Lender/Collateral</u>	<u>Interest Rate</u>	<u>Monthly Payment</u>	<u>Maturity Date</u>	<u>2018</u>	<u>2017</u>
<u>Mortgages payable, continued</u>					
Wells Fargo Bank (f/k/a Wachovia Bank) 615-617 Whalley Avenue, New Haven, Connecticut	7.25%	\$ 1,141	08/01/19	\$ 17,208	\$ 29,154
Wells Fargo Bank (f/k/a Wachovia Bank) 450 Island Lane, West Haven, Connecticut	7.15%	10,957	10/27/21	388,336	487,713
Total mortgages payable				4,686,606	5,012,010
Less: current portion				(331,582)	(322,587)
Total mortgages payable, net of current portion				<u>\$ 4,355,024</u>	<u>\$ 4,689,423</u>
* Mortgage is financed under an interest rate swap agreement. See Note 1 under "Derivative debt agreements and interest rate risk management" and Note 6 under "Interest rate swap loans".					
<u>Loans payable</u>					
Connecticut Department of Developmental Services/Unsecured	6.00%	\$ 129	10/01/18	\$ 382	\$ 1,857
Key Bank revolving credit loan agreement (see Note 5) improvements to property acquired with loan proceeds	4.25%	-	03/15/19	414,000	414,000
Key Bank non-revolving multiple draw term note (see Note 5)/Corporate assets	4.14%	-	07/01/21	271,460	368,805
Connecticut Department of Developmental Services/Unsecured	6.00%	272	04/01/26	19,986	21,981
Connecticut Department of Developmental Services/Unsecured	6.00%	91	04/01/26	6,700	7,369
Connecticut Department of Developmental Services/Unsecured	6.00%	112	04/01/26	8,252	9,076
Connecticut Department of Developmental Services/Unsecured	6.00%	304	04/01/21	8,954	11,961
Connecticut Department of Developmental Services/Unsecured	6.00%	148	04/01/31	15,764	16,572
Connecticut Department of Developmental Services/Unsecured	6.00%	517	04/01/21	15,264	20,388
Connecticut Department of Developmental Services/Unsecured	6.00%	120	04/01/26	8,839	9,720
Connecticut Department of Developmental Services/Unsecured	6.00%	287	04/01/21	8,476	11,320
Connecticut Department of Developmental Services/Unsecured	6.00%	119	07/01/22	5,068	6,156
Connecticut Department of Developmental Services/Unsecured	6.00%	230	07/01/32	26,046	27,200
Connecticut Department of Developmental Services/Unsecured	6.00%	235	07/01/32	26,865	27,800
Connecticut Department of Developmental Services/Unsecured	6.00%	214	09/01/32	24,410	-
Connecticut Department of Developmental Services/Unsecured	6.00%	573	09/01/24	35,348	-
Connecticut Department of Developmental Services/Unsecured	6.00%	143	09/01/37	19,557	-
Connecticut Department of Developmental Services/Unsecured	6.00%	506	09/01/32	57,890	-
Connecticut Department of Developmental Services/Unsecured	6.00%	174	09/01/27	14,697	-
Connecticut Department of Developmental Services/Unsecured	6.00%	445	12/01/32	52,724	-
Total loans payable				1,040,682	954,205
Less: current portion				(547,451)	(116,283)
Total loans payable, net of current portion				<u>\$ 493,231</u>	<u>\$ 837,922</u>

MARRAKECH, INC.

Notes to Consolidated Financial Statements

June 30, 2018 and 2017

Table 6.1 - Schedule of Debt Obligations, Continued

Minimum future principal payments on mortgages and loans for the next five years and thereafter are as follows:

2019	\$ 879,033
2020	462,346
2021	435,763
2022	263,931
2023	231,424
Thereafter	<u>3,454,791</u>
	<u>\$ 5,727,288</u>

Interest expense related to the above mortgages, loans and the lines of credit for the years ended June 30, 2018 and 2017 was \$313,403 and \$387,547, respectively.

SUPPLEMENTARY INFORMATION

MARRAKECH, INC.

Consolidated Supporting Schedule of Operating Revenue

For the years ended June 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Department of Developmental Services	\$ 19,308,771	\$ 19,361,221
Department of Mental Health and Addiction Services	3,971,815	4,005,564
Department of Social Services Room and Board	3,508,742	4,181,083
ABI revenue	1,634,155	1,946,117
DCF Work/Learn and Children Services programs	774,516	1,016,699
Board of Education	516,380	63,456
Other revenue, net of gains and losses on disposals of assets	486,332	509,350
BRS revenue	347,626	900,860
Rental revenue	294,131	424,679
Caning revenue	162,209	102,360
HSTP revenue	136,077	198,220
BESB revenue	<u>117,497</u>	<u>130,143</u>
	<u>\$ 31,258,251</u>	<u>\$ 32,839,752</u>

MARRAKECH, INC.

Consolidated Supporting Schedule of Non-Salary

For the years ended June 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Transportation	\$ 838,466	\$ 865,177
Depreciation and amortization	779,025	856,001
Consultants	896,745	1,050,593
Utilities	760,969	766,321
Interest	313,403	387,547
Plant maintenance and repairs	437,487	444,570
Insurance	624,790	719,204
Food and household supplies	700,463	735,575
Miscellaneous	449,307	476,138
Intermediate care facility State of Connecticut user fees	123,550	160,785
Equipment expenses	136,924	158,680
Rent	226,479	286,390
Program supplies	194,819	213,461
Training	386,051	353,232
Professional fees	236,686	281,184
Property taxes	62,513	73,334
Medical supplies	59,498	80,002
Advertising	31,618	64,184
Dues, fees and licenses	<u>54,839</u>	<u>42,829</u>
	<u>\$ 7,313,632</u>	<u>\$ 8,015,207</u>

MARRAKECH, INC.

Consolidated Supporting Schedule of Employee Benefits

For the years ended June 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Health insurance benefits	\$ 1,682,878	\$ 1,555,910
FICA	1,520,857	1,601,461
Workers' compensation insurance	545,422	681,053
Miscellaneous	29,243	24,443
Unemployment insurance	<u>172,330</u>	<u>194,083</u>
	<u>\$ 3,950,730</u>	<u>\$ 4,056,950</u>