

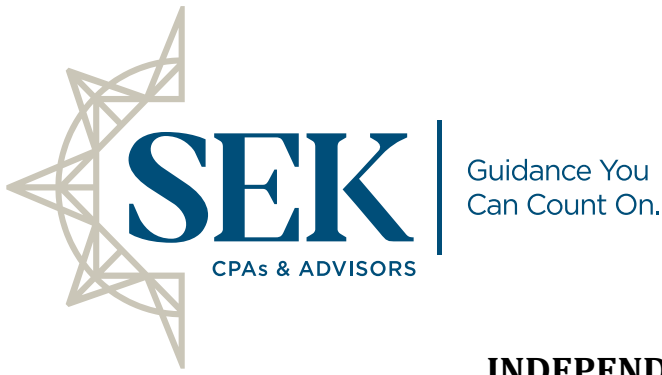
Audited
Financial
Statements

June 30, 2019

**Brook Lane Health
Services, Inc.**

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Brook Lane Health Services, Inc.
Hagerstown, Maryland

We have audited the accompanying financial statements of Brook Lane Health Services, Inc. (Brook Lane) which comprise the balance sheets as of June 30, 2019 and 2018, 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 Brook Lane'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 Brook Lane's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Brook Lane Health Services, Inc. as of June 30, 2019 and 2018, and the results of its operations, 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.

Effect of Adopting New Accounting Standard

As discussed in Note 1 to the financial statements, Brook Lane adopted new accounting guidance issued by the Financial Accounting Standards Board (FASB) related to the presentation of financial statements for not-for-profit organizations. Our opinion is not modified with respect to this matter.

Smith Elliott Hearn & Company, LLC.

Chambersburg, Pennsylvania
October 21, 2019

BROOK LANE HEALTH SERVICES, INC.
Balance Sheets
June 30, 2019 and 2018

	2019	2018
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 1,237,493	\$ 2,523,044
Investments	277	714
Patient accounts receivable, net of allowance for doubtful accounts of \$ 367,900 for 2019 and \$ 325,386 for 2018	3,452,615	5,271,591
Amounts due from third-party payors, current portion	259,729	6,684
Amounts due from affiliates	1,165,830	-
Inventories	164,674	151,125
Prepaid expenses	514,322	562,328
Other receivables	22,073	24,711
Total current assets	<u>6,817,013</u>	<u>8,540,197</u>
Board Designated Investments		
Capital replacement and expansion	296,915	267,864
Special purposes	-	173,112
Total board designated investments	<u>296,915</u>	<u>440,976</u>
Assets Whose Use is Limited		
Pledges receivable, net of allowance for doubtful pledges of \$ 0 for 2019 and 2018	3,750	8,750
Unemployment fund collateral	286,140	265,434
Total assets whose use is limited	<u>289,890</u>	<u>274,184</u>
Property, Plant and Equipment		
Land and land improvements	500,286	500,286
Buildings	16,594,856	15,877,708
Fixed equipment	3,426,765	2,048,431
Major moveable equipment	1,559,640	1,518,453
Construction in progress	669,089	1,444,188
	22,750,636	21,389,066
Less allowance for depreciation	8,838,903	7,719,722
	<u>13,911,733</u>	<u>13,669,344</u>
Other Assets		
Long-term patients accounts receivable, net of allowance for doubtful accounts of \$221,328 for 2019 and \$ 63,333 for 2018	579,988	162,834
TOTAL ASSETS	<u>\$ 21,895,539</u>	<u>\$ 23,087,535</u>

	2019	2018
LIABILITIES AND NET ASSETS		
Current Liabilities		
Current portion of long term debt	\$ 645,234	\$ 629,139
Trade accounts payable and accrued expenses	645,273	976,086
Accrued salaries, wages, and payroll taxes	673,624	683,955
Accrued vacation	<u>1,342,818</u>	<u>1,216,671</u>
Total current liabilities	<u>3,306,949</u>	<u>3,505,851</u>
Other Liabilities		
Long-term debt, net of current portion	5,290,664	5,901,237
Obligation under interest rate swap agreement	<u>334,183</u>	<u>165,523</u>
Total other liabilities	<u>5,624,847</u>	<u>6,066,760</u>
Total liabilities	<u>8,931,796</u>	<u>9,572,611</u>
Net Assets		
Without donor restrictions	12,663,078	13,238,310
With donor restrictions	<u>300,665</u>	<u>276,614</u>
Total net assets	<u>12,963,743</u>	<u>13,514,924</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 21,895,539</u>	<u>\$ 23,087,535</u>

BROOK LANE HEALTH SERVICES, INC.
Statements of Operations
Years Ended June 30, 2019 and 2018

	2019	2018
NET ASSETS WITHOUT DONOR RESTRICTIONS		
Revenue, Gains, and Other Support		
Net patient service revenue		
Routine services	\$ 14,633,509	\$ 14,352,334
Ancillary services	6,655,075	6,923,341
Net patient service revenue	<u>21,288,584</u>	<u>21,275,675</u>
Provision for bad debts	<u>(837,415)</u>	<u>(628,767)</u>
Net patient service revenue less provision for bad debts	<u>20,451,169</u>	<u>20,646,908</u>
Other operating revenues	<u>541,479</u>	<u>266,021</u>
Total revenue, gains and other support	<u>20,992,648</u>	<u>20,912,929</u>
Expenses and Losses		
Salaries and wages	12,565,755	12,079,895
Employee benefits	2,767,192	2,966,130
Supplies	1,386,395	1,383,311
Contractual services	1,698,178	1,315,776
Facility expense	905,602	900,191
Depreciation	1,119,182	900,827
Interest	293,905	253,609
General and administrative	<u>1,029,177</u>	<u>997,232</u>
Total expenses	<u>21,765,386</u>	<u>20,796,971</u>
Operating income (loss)	<u>(772,738)</u>	<u>115,958</u>
Other Income		
Contributions	40,877	9,113
Investment income	13,635	13,314
Realized losses on investments	(438)	(8,603)
Other, net	<u>304,579</u>	<u>759,101</u>
Total other income	<u>358,653</u>	<u>772,925</u>
Excess (deficit) of revenues, gains, and other support over expenses		
	<u>(414,085)</u>	<u>888,883</u>
Unrealized losses on investments	-	(438)
Change in value of interest rate swap agreement	(168,659)	164,876
Net assets released from restriction	7,512	91,200
Transfer to affiliate	<u>-</u>	<u>(757,427)</u>
INCREASE (DECREASE) IN NET ASSETS WITHOUT DONOR RESTRICTIONS	<u>\$ (575,232)</u>	<u>\$ 387,094</u>

BROOK LANE HEALTH SERVICES, INC.
Statements of Changes in Net Assets
Years Ended June 30, 2019 and 2018

	2019	2018
NET ASSETS WITHOUT DONOR RESTRICTIONS		
Excess (deficit) of revenues, gains, and other support over expenses	\$ (414,085)	\$ 888,883
Unrealized losses on investments	-	(438)
Change in value of interest rate swap agreement	(168,659)	164,876
Net assets released from restriction	7,512	91,200
Transfer to affiliate	<u>-</u>	<u>(757,427)</u>
Increase (decrease) in net assets without restrictions	<u>(575,232)</u>	<u>387,094</u>
NET ASSETS WITH DONOR RESTRICTIONS		
Contributions	31,563	64,245
Net assets released from restrictions	<u>(7,512)</u>	<u>(91,200)</u>
Increase (decrease) in net assets with donor restrictions	<u>24,051</u>	<u>(26,955)</u>
Increase (decrease) in net assets	(551,181)	360,139
Net Assets, Beginning	<u>13,514,924</u>	<u>13,154,785</u>
NET ASSETS, ENDING	<u><u>\$ 12,963,743</u></u>	<u><u>\$ 13,514,924</u></u>

BROOK LANE HEALTH SERVICES, INC.
Statements of Cash Flows
Years Ended June 30, 2019 and 2018

	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ (551,181)	\$ 360,139
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation and amortization	1,130,270	911,916
Provision for bad debts	837,415	628,767
Realized loss on securities	438	8,603
Unrealized loss on investments	-	438
Change in value of interest rate swap agreement	168,659	(164,876)
Transfer to affiliate	-	757,427
Contribution income with donor restrictions	(31,563)	(64,245)
(Increase) decrease in:		
Patient accounts receivable	564,407	(2,795,950)
Pledges receivable	5,000	79,756
Inventories	(13,549)	8,109
Amounts due from third-party payors	(253,045)	51,441
Amounts due from affiliates	(1,165,830)	-
Other assets	50,647	(762)
Increase (decrease) in:		
Accounts payable and accrued expenses	(214,998)	608,255
Net cash provided by operating activities	<u>526,670</u>	<u>453,263</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(1,361,571)	(515,935)
Net (increase) decrease in designated investments:		
Capital replacement and expansion	(29,051)	(61,404)
Special purposes	173,112	(56,985)
Escrow funds	-	1,159,655
Unemployment fund collateral	(20,706)	(3,440)
Net cash provided (used) by investing activities	<u>(1,238,216)</u>	<u>521,891</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Transfer to affiliate	-	(757,427)
Payments on long-term debt	(605,568)	(608,492)
Contribution income with donor restrictions	31,563	64,245
Net cash used by financing activities	<u>(574,005)</u>	<u>(1,301,674)</u>
Net decrease in cash and cash equivalents	(1,285,551)	(390,765)
Cash and cash equivalents, beginning of year	<u>2,523,044</u>	<u>2,913,809</u>
Cash and cash equivalents, end of year	<u>\$ 1,237,493</u>	<u>\$ 2,523,044</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for interest net of capitalized interest of \$ 0 and \$ 26,879 in 2019 and 2018	<u>\$ 281,521</u>	<u>\$ 251,806</u>

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Brook Lane Health Services, Inc. (Brook Lane), located in Hagerstown, Maryland, is a not-for-profit provider of mental health services established in 1949. It provides short-term hospitalization services to the residents of Washington County and surrounding areas.

Brook Lane is a subsidiary of the parent organization Brook Lane, Inc. and an affiliate of Brook Lane Behavioral Services, Inc. located in Hagerstown, Maryland. These entities collectively are not-for-profit providers of mental health services and provide short-term hospitalization, Level 1 schooling, and transitional care to the residents of Washington County and surrounding areas.

Accounting Method

Brook Lane presents its financial statements on the accrual basis of accounting, with income recognized when earned and expenses recognized when incurred.

Use of Estimates

The preparation of the financial statements in conformity with generally accepted accounting principles 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. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were management's estimate of the allowance for doubtful accounts and reserve for contractual allowances on accounts receivable balances. Actual results could differ from those estimates.

Cash Equivalents

For purposes of the statement of cash flows, Brook Lane has defined cash and cash equivalents as those amounts included in "cash and cash equivalents" on the balance sheets. No investments are considered cash equivalents.

Investments

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the balance sheets. Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in the excess (deficit) of revenues, gains, and other support over expenses unless the income or loss is restricted by donor or law. Realized gains and losses are computed on the specific identification method. Unrealized gains and losses are reflected as other changes in net assets.

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Patient Receivables

Brook Lane provides credit in the normal course of its business to patients. Patient receivables are generally due 90 days after billed. Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, Brook Lane analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for doubtful accounts and provision for bad debts. Management regularly reviews data about these major payor 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, Brook Lane analyzes contractually due amounts and provides an allowance for doubtful accounts and a provision for bad debts, if necessary (for example, for expected uncollectible deductibles and copayments on accounts for which the third-party payor has not yet paid, or for payors who are known to be having financial difficulties that make the realization of amounts due unlikely). 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), Brook Lane records a provision for bad debts in the period of service on the basis of its past experience, which indicates that some 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) and the amounts actually collected after all reasonable collection efforts have been exhausted is charged off against the allowance for doubtful accounts.

Brook Lane's allowance for doubtful accounts for self-pay patients was 25% of self-pay accounts receivable at June 30, 2019 and 2018. The Organization periodically reviews its charity care program and uninsured discount policy. The Organization does not maintain an allowance for doubtful accounts from third-party payors, nor did it have significant write-offs from third-party payors.

Pledges Receivable

In 2013, Brook Lane began a capital campaign to raise money for construction and expansion of the hospital. Pledges are recorded as receivables when a commitment is signed. No allowance for doubtful accounts has been established based on management's estimate of the promises being fully collectible.

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Inventories

Inventories of supplies are recorded at the lower of cost (using the first-in, first-out method) or market.

Property, Plant, and Equipment

Property, plant, and equipment acquisitions which exceed \$ 3,000 are recorded at cost. Depreciation is provided over the estimated useful life of each class of depreciable asset and is computed using the straight-line method. The cost and accumulated depreciation relating to capital assets sold or retired are removed from the respective accounts at the time of disposition and the resulting gain or loss is reflected in non-operating revenue. Depreciation expense was \$ 1,119,182 and \$ 900,827 for the years ended June 30, 2019 and 2018, respectively.

Gifts of long-lived assets such as land, buildings, or equipment are reported as support without donor restrictions, and are excluded from the excess (deficit) of revenues, gains, and other support over expenses, unless explicit donor stipulations specify how the assets are to be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

Excess (Deficit) of Revenues, Gains, and Other Support Over Expenses

The statement of operations includes *excess (deficit) of revenues, gains, and other support over expenses*. Changes in net assets without donor restrictions which are excluded from *excess (deficit) of revenues, gains, and other support over expenses*, consistent with industry practice, include permanent transfers of assets to and from affiliates for other than goods and services, unrealized gains or losses on investments other than trading securities, the effective portion of the change in the value of the interest rate swap agreement and contributions of long-lived assets (including assets acquired using donor restricted contributions).

Donor-Restricted Gifts

Unconditional promises to give cash and other assets to the Organization are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends, or purpose restriction is accomplished, restricted net assets are reclassified as net assets without donor restrictions and reported in the statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as contributions without donor restrictions in the accompanying financial statements.

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Advertising Costs

Brook Lane follows the policy of charging costs of advertising to expense as incurred. Advertising expense was \$ 14,172 and \$ 25,501 for the years ended June 30, 2019 and 2018, respectively.

Net Patient Service Revenue

Net patient service revenue is reported at the estimated net realizable amounts from patients and third-party payors for services rendered. Rates for patients' services in Maryland hospitals are subject to investigation, review, and approval by the Health Services Cost Review Commission (HSCRC), an independent commission created by a State of Maryland legislative act. All payors, except Medicare and Medicaid, are required to pay the HSCRC approved rates. Medicare payments are based on prospective payment system (PPS) rates and Medicaid payments are based on 96% of HSCRC approved rates.

Laws and regulations governing Medicare, Medicaid and other third-party programs are extremely complex and subject to interpretation. As a result, there is at least a reasonable possibility that recorded estimates will change in the near term.

Charity Care

Brook Lane provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Brook Lane calculates charity care based on a ratio of total expenses to charges. Brook Lane's estimated annual cost of providing charity care for the years ended June 30, 2019 and 2018 was \$ 517,847 and \$ 393,872, respectively. There were no contributions or grant income received to offset the cost of charity care for the years ended June 30, 2019 and 2018.

Concentration of Credit Risk

Brook Lane services patients principally living in the Washington County area. The majority of these patients have insurance through CareFirst (Blue Cross Blue Shield of Maryland) or another insurance company, a health maintenance organization, or qualify for the Maryland Medical Assistance or Federal Medicare programs. Brook Lane grants credit without requiring collateral.

At June 30, Brook Lane's patient accounts receivable consisted of the following payors:

	<u>2019</u>	<u>2018</u>
Blue Cross Blue Shield	10.06%	22.33%
Medicare	16.44%	11.90%
Commercial Insurance	6.43%	8.63%
Health Maintenance Organizations	8.09%	10.55%
Medical Assistance	36.04%	30.64%
Self-Pay and Other	<u>22.94%</u>	<u>15.95%</u>
	<u>100.00%</u>	<u>100.00%</u>

Brook Lane's cash balances at a local financial institution periodically exceed the Federal Deposit Insurance Corporation limit. Management considers this a normal business risk.

NOTE 1 ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Unemployment Compensation

Brook Lane has elected under Maryland Unemployment Compensation Law to reimburse the Maryland Department of Unemployment Insurance for unemployment insurance benefits paid to former employees rather than make quarterly unemployment insurance tax payments. Reimbursable employers are required to provide collateral as a security in the event of the employer's default on these reimbursements. Brook Lane holds a certificate of deposit in the amount of \$ 286,140 and \$ 265,434 as of June 30, 2019 and 2018, respectively, as collateral for this requirement.

Income Taxes

The Internal Revenue Service has ruled that Brook Lane qualifies as a tax-exempt entity under Section 501(c)(3) of the Internal Revenue Code and is classified as a public charity. The entity files a Form 990, "Return of Organization Exempt from Income Tax".

Uncertain Tax Positions

Brook Lane follows generally accepted accounting principles, which provides guidance on accounting for uncertainty in income taxes recognized in an organization's financial statements. Brook Lane's policy is to charge penalties and interest to income tax expense as incurred. Brook Lane's federal tax returns are subject to examination by the Internal Revenue Service, generally for a period of three years after the returns are filed.

Reclassifications

Certain amounts in the prior year financial statements have been reclassified for comparative purposes to conform to the presentation in the current year financial statements.

Change in Accounting Policy

On August 18, 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, Not-for-Profit Entities (Topic 958) – Presentation of Financial Statements of Not-for-Profit Entities. The update addresses the complexity and understandability of net asset classification, deficiencies in information about liquidity and availability of resources, and the lack of consistency in the type of information provided about expenses and investment return. The Organization implemented ASU 2016-14 during the year ended June 30, 2019 and adjusted the presentation in the financial statements accordingly. ASU 2016-14 has been applied retrospectively to all periods presented for items that are required to be applied retrospectively. The implementation of ASU 2016-14 did not require a restatement of prior period net assets.

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 2 LIQUIDITY AND AVAILABILITY

Financial assets available for general expenditures within one year of the balance sheet date are as follows:

Financial assets at year end:	2019
Cash and cash equivalents	\$ 1,237,493
Investments	277
Accounts receivable	<u>4,900,247</u>
Financial assets available to meet general expenditures over the next twelve months	<u>\$ 6,138,017</u>

The Organization's goal is to maintain 30 days of available cash. There is daily monitoring of the operating bank accounts and the CFO and CEO review the cash balances weekly. The Organization maintains a focus on timely billing and collection to maintain a steady flow of operating cash. The Organization maintains a \$ 750,000 line of credit available to meet cash flow needs.

NOTE 3 INVESTMENTS

The composition of investments in Brook Lane's investment portfolio at June 30, 2019 and 2018 is set forth in the following schedule:

	<u>2019</u>		<u>2018</u>	
	Cost	Fair Value	Cost	Fair Value
Cash and cash equivalents	\$ 21	\$ 21	\$ 21	\$ 21
Equities	<u>4,039</u>	<u>256</u>	<u>4,039</u>	<u>693</u>
Current Investments	<u>\$ 4,060</u>	<u>\$ 277</u>	<u>\$ 4,060</u>	<u>\$ 714</u>
Board-designated investments				
Cash and cash equivalents	\$ 296,915	\$ 296,915	\$ 438,848	\$ 438,848
Equities	<u>-</u>	<u>-</u>	<u>2,128</u>	<u>2,128</u>
	<u>\$ 296,915</u>	<u>\$ 296,915</u>	<u>\$ 440,976</u>	<u>\$ 440,976</u>
Unemployment fund collateral				
Certificate of deposit	<u>\$ 286,140</u>	<u>\$ 286,140</u>	<u>\$ 265,434</u>	<u>\$ 265,434</u>

NOTE 4 AMOUNTS DUE FROM THIRD-PARTY PAYORS

The amounts collected under the Medicare and Medicaid programs are subject to verification by fiscal intermediaries. The Medicare program is based on a prospective payment system and is no longer cost settled. The Medicaid outpatient settlements are still open for 2017 through 2019. Medicaid in-patient payments are 96% of HSCRC approved rates and are no longer subject to a cost settlement process. An estimate for the settlement of the 2017 to 2019 Medicaid cost reports is recorded in the amount of \$ 259,729 and \$ 6,684 at June 30, 2019 and 2018, respectively. Management believes these are reasonable estimates at June 30, 2019 and 2018.

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 5 ASSETS WHOSE USE IS LIMITED

Assets whose use is limited are comprised of various funds which have restrictions placed on them either by outside third-parties, or regulatory requirements. The accounts in this grouping include pledges receivable from donors designated for the hospital expansion and an unemployment compensation trust fund. Investment income earned on these funds is reflected in investment income in the statements of operations.

	2019	2018
Pledges receivable	\$ 3,750	\$ 8,750
Unemployment fund collateral	<u>286,140</u>	<u>265,434</u>
Assets whose use is limited	<u>\$ 289,890</u>	<u>\$ 274,184</u>

NOTE 6 PLEDGES RECEIVABLE

Brook Lane has been soliciting pledges for the expansion of the hospital. Pledges restricted for capital acquisitions are reported in temporarily restricted net assets. An allowance for uncollectible pledges has not been established for 2019 and 2018 as management believes the remaining pledges will be fully collected.

The following is a summary of pledges receivable at June 30:

	2019	2018
Pledges receivable for hospital expansion	<u>\$ 3,750</u>	<u>\$ 8,750</u>

The remaining balance of these pledges at June 30 are due as follows:

	2019	2018
Less than one year	\$ 3,750	\$ 5,000
One year to five years	<u>-</u>	<u>3,750</u>
	<u>\$ 3,750</u>	<u>\$ 8,750</u>

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 7 LONG-TERM DEBT

Long-term debt as of June 30 consists of the following:

	2019	2018
Town of Smithsburg, Economic Development Revenue Bond (Series 2002)	\$ 1,552,356	\$ 1,868,059
Town of Smithsburg, Economic Development Revenue Bond (Series 2013)	3,711,248	3,889,025
BB&T Bank Note	<u>770,178</u>	<u>882,264</u>
Total long-term debt	6,033,782	6,639,348
Less net debt issuance cost	(97,884)	(108,972)
Less current portion	<u>(645,234)</u>	<u>(629,139)</u>
Long-term portion	<u>\$ 5,290,664</u>	<u>\$ 5,901,237</u>

On August 1, 2002, Brook Lane issued \$ 5,500,000 Town of Smithsburg, Economic Development Revenue Bond, Series of 2002 (Series of 2002). The bond issue was used to refinance the outstanding principal balance of the Washington County Economic Development Revenue Bonds, Series 1991, and finance the construction of two, two-story hospital wings totaling approximately 30,000 square feet and to renovate approximately 3,900 square feet of the facility. This Series of 2002 will mature on August 1, 2023. The interest rate on the bond issue is based on 92% of the prime rate and will be adjusted on various anniversary dates. The interest rate on this obligation was 4.60% and 2.99% at June 30, 2019 and 2018, respectively. This obligation is secured by a first lien on all property and rents and profits hereunder and cross-collateralized with the line of credit. The Series of 2002 also has several covenants that Brook Lane must comply with, such as maintaining minimum debt service coverage and tangible net worth ratios. The bond series may be prepaid without penalty.

On December 20, 2013, Brook Lane issued \$ 4,600,000 Town of Smithsburg, Economic Development Revenue Bond, Series of 2013. The bond issue was used to finance the construction and furnishing of a 14-bed addition and physician offices totaling approximately 24,000 square feet at Brook Lane's existing hospital facility, constructing a waste water treatment facility to serve the Brook Lane campus and building out, furnishing and equipping approximately 7,700 square feet of office space leased in Frederick County Maryland. The 2013 bonds mature on December 15, 2033. The interest rate on this obligation is 67% of the one month London Interbank Offered Rate (LIBOR) plus 2.01%. This variable rate was 3.61% and 3.41% at June 30, 2019 and 2018, respectively. The interest rate on the bond is hedged with a swap agreement (Note 14) to create a synthetic fixed rate of 4.43%. The Series of 2013 bonds are secured by a lien on all property and rents and profits hereunder and cross-collateralized with the line of credit. The Series of 2013 bonds also have several covenants that Brook Lane must comply with, such as maintaining a minimum debt service coverage of 1.10 to 1.00 and tangible net worth greater than \$ 6,000,000. The bonds may be prepaid without penalty.

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 7 LONG-TERM DEBT (CONTINUED)

As of June 30, 2019, Brook Lane was not in compliance with the debt service coverage ratio. The financial institution issued a waiver subsequent to year end. As a result, there are no changes to the classification of this liability at June 30, 2019.

In May 2015, Brook Lane entered into a note for \$ 1,200,000 with BB&T for the purchase and implementation of an electronic health records system. The note is due May 2025 and has an initial five-year fixed rate of 4.15% followed by a subsequent five-year rate based on the five-year Federal Home Loan Bank of Pittsburgh rate plus 265 basis points. This obligation is secured by a third lien on all property and rents and profits.

The aggregate future maturities of all long-term debt at June 30 are:

2020	\$	645,234
2021		679,363
2022		709,528
2023		742,952
2024		431,001
Thereafter		2,825,704
		<u>\$ 6,033,782</u>

Brook Lane has a revolving line of credit with BB&T in the amount of \$ 750,000, at an interest rate of 92% of the prime rate with a floor of 3%. The interest rate was 5.06% and 4.60% at June 30, 2019 and 2018, respectively. This line of credit is secured by accounts receivable and cross-collateralized with the Series of 2002 and Series of 2013 bonds. There were no draws on this line of credit at June 30, 2019 or 2018.

Total interest costs and amortization of debt issuance costs for the year ended June 30, 2019 were \$ 293,905. Total interest costs and amortization of debt issuance costs for the year ended June 30, 2018 were \$ 253,609, net of \$ 26,879 of capitalized interest.

NOTE 8 NET PATIENT SERVICE REVENUE

Brook Lane's routine and ancillary service revenue concentrations for the years ended June 30, 2019 and 2018 are as follows:

	<u>Net Patient Service Revenue</u>	
	<u>2019</u>	<u>2018</u>
Blue Cross Blue Shield	20.76%	22.52%
Medicare	12.90%	8.55%
Commercial Insurance	7.46%	5.83%
Health Maintenance Organizations	9.36%	13.45%
Medical Assistance	44.15%	43.30%
Self-Pay and Other	5.37%	6.35%
	<u>100.00%</u>	<u>100.00%</u>

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 8 NET PATIENT SERVICE REVENUE (CONTINUED)

Brook Lane's major payor sources are Blue Cross Blue Shield, Medicare, commercial insurance, health maintenance organizations, Medicaid, and self-pay individuals. Net patient service revenue, net of contractual and charity care allowance provided (but before the provision for bad debts), recognized in the statement of operations for the years ended June 30, 2019 and 2018 from these major payor sources is as follows:

2019						
Blue Cross Blue Shield	Medicare	Commercial Insurance	Health Maintenance Organizations	Medical Assistance	Self-Pay and Other	Total
\$ 4,417,342	\$ 2,746,079	\$ 1,588,942	\$ 1,993,445	\$ 9,398,660	\$ 1,144,116	\$ 21,288,584
2018						
Blue Cross Blue Shield	Medicare	Commercial Insurance	Health Maintenance Organizations	Medical Assistance	Self-Pay and Other	Total
\$ 4,792,299	\$ 1,819,528	\$ 1,241,434	\$ 2,861,268	\$ 9,211,565	\$ 1,349,581	\$ 21,275,675

The change in the allowance for doubtful accounts for 2019 and 2018 is as follows:

	2019	2018
Allowance for doubtful accounts at July 1	\$ 388,719	\$ 113,738
Provision for bad debts	837,415	628,767
Write off of bad debts	(636,906)	(353,786)
Allowance for doubtful accounts at June 30	\$ 589,228	\$ 388,719

NOTE 9 EMPLOYEE BENEFIT PLANS

Brook Lane has a 401(k) defined contribution plan that covers all employees who have attained the age of 21. Employees are eligible for matching contributions after completion of one year of service. An employee may contribute up to 100% of salary on a before-tax basis up to the elective deferral limit for the respective year. Brook Lane makes a 50% matching contribution up to a maximum of \$ 2,500, which is based on 5% of an eligible employee's salary up to \$ 100,000. Brook Lane may also make other discretionary contributions to the plan. All employee contributions and earnings are vested 100% immediately, as are Brook Lane's matching contributions. All discretionary employer contributions become 100% vested after three years of service.

Contribution expense of \$ 207,507 and \$ 442,512 was incurred by Brook Lane related to the 401(k) plan during the years ended June 30, 2019 and 2018, respectively.

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 9 EMPLOYEE BENEFIT PLANS (CONTINUED)

On January 1, 2019 the plan was amended to include a 100% match up to 3% of compensation and then 50% deferral between 3% and 5% of compensation up to \$ 100,000. Brook Lane may also make other discretionary contributions, but these do not apply to elective deferrals exceeding 6% of compensation.

NOTE 10 LEASES

Brook Lane has entered into lease agreements for the rental of equipment. Rentals paid under operating leases for 2019 and 2018 were \$ 89,554 and \$123,305, respectively.

NOTE 11 FUNCTIONAL EXPENSES

Brook Lane provides general psychiatric and school services to residents within its geographic service area. Expenses are allocated between program, management and general, and fundraising based on cost centers that are attributable to program and administrative costs. Expenses by functional category related to providing these services are as follows:

2019			
	<u>Program</u>	<u>Management and General</u>	<u>Total</u>
Salaries	\$ 9,752,934	\$ 2,812,821	\$ 12,565,755
Employee Benefits	2,164,971	602,221	2,767,192
Supplies	1,360,761	25,634	1,386,395
Contractual Services	1,346,532	351,646	1,698,178
Facility Expense	517,821	387,781	905,602
Depreciation	1,119,182	-	1,119,182
Interest	282,817	11,088	293,905
General and Administrative	192,117	837,060	1,029,177
Total	<u>\$ 16,737,135</u>	<u>\$ 5,028,251</u>	<u>\$ 21,765,386</u>

2018				
	<u>Program</u>	<u>Management and General</u>	<u>Fundraising</u>	<u>Total</u>
Salaries	\$ 9,355,023	\$ 2,684,367	\$ 40,505	\$ 12,079,895
Employee Benefits	2,297,057	659,127	9,946	2,966,130
Supplies	1,345,859	37,452	-	1,383,311
Contractual Services	951,865	363,911	-	1,315,776
Facility Expense	590,477	309,714	-	900,191
Depreciation	900,827	-	-	900,827
Interest	242,521	11,088	-	253,609
General and Administrative	190,674	806,558	-	997,232
Total	<u>\$ 15,874,303</u>	<u>\$ 4,872,217</u>	<u>\$ 50,451</u>	<u>\$ 20,796,971</u>

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 12 MARYLAND HEALTH SERVICES COST REVIEW COMMISSION

Brook Lane’s charges are subject to review and approval by the Maryland Health Services Cost Review Commission. Management has filed the required forms with the Commission and believes Brook Lane to be in compliance with Commission requirements.

NOTE 13 MALPRACTICE INSURANCE COVERAGE

Brook Lane is insured for malpractice under a claims-made policy. This type of policy covers only malpractice claims covered by the policy which are reported to the insurance carrier during the policy term. If this policy were discontinued, it would be Brook Lane’s intention to obtain tail coverage. Based on management's evaluation of malpractice claims, an allowance for incurred but not reported claims is considered immaterial and not necessary.

NOTE 14 INTEREST RATE SWAP AGREEMENT

Brook Lane is exposed to the impact of interest rate changes on its variable rate debt, Town of Smithsburg, Economic Development Revenue Bond, Series of 2013 (Note 7). In order to manage the impact of interest rate changes on the Series of 2013, Brook Lane entered into a swap agreement with Susquehanna Bank (BB&T Bank) on December 4, 2013 for a notional amount of \$ 4,600,000, effective on December 20, 2013, with a termination date of December 15, 2033. Brook Lane’s intention is to pay a synthetic fixed interest rate of 4.43% and receive a floating rate of 67% of monthly LIBOR plus 2.01% on the Series of 2013.

The fair value of the interest rate swap liability at June 30, 2019 and 2018 was \$ 334,183 and \$ 165,523, respectively, and is included in other liabilities on the balance sheets. The change in the value of the interest rate swap agreement of \$ (168,659) and \$ 164,876 for the years ended June 30, 2019 and 2018, respectively, is presented after the excess (deficit) of revenues, gains, and other support over expenses in the statements of operations.

NOTE 15 NET ASSETS WITH DONOR RESTRICTIONS

At June 30, 2019 and 2018, net assets with donor restrictions consist of funds solicited for the construction of the hospital addition and purchase of designated equipment, furnishings, and supplies as follows:

	2019	2018
Subject to expenditure for specified purpose:		
Building projects	<u>\$ 300,665</u>	<u>\$ 276,614</u>
Net assets released from donor restrictions by incurring expenses satisfying the restricted purpose by donors are as follows:		
Building projects	\$ 2,512	\$ 11,194
Collection/write-off of pledges receivable	<u>5,000</u>	<u>80,006</u>
	<u>\$ 7,512</u>	<u>\$ 91,200</u>

NOTE 16 FAIR VALUE MEASUREMENTS

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1) and the lowest priority to unobservable inputs (level 3). Valuation techniques maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The three levels of the fair value hierarchy are described as follows:

- Level 1:** Inputs to the valuation methodology are quoted prices available in active markets for identical assets or liabilities that the Organization can access at the measurement date.
- Level 2:** Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as:
- Quoted prices for similar assets or liabilities in active markets;
 - Quoted prices for identical or similar assets or liabilities in inactive markets;
 - Inputs other than quoted prices that are observable for the asset or liability;
 - Inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3:** Inputs that are unobservable inputs for the asset or liability.

Following a description of the valuation methodologies used for instruments measured on a recurring basis at estimated fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy:

Money Market funds: Based on the daily closing price as reported by the fund based on the daily net asset value (NAV).

Domestic and international common stocks: Based on quoted prices in an active market.

Interest rate swap agreement: The fair value is estimated by a third party using inputs that are observable or that can be corroborated by observable market data for similar agreements.

Certificates of deposit: Based on quoted prices for similar assets.

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 16 FAIR VALUE MEASUREMENTS (CONTINUED)

At June 30, 2019	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets				
Money market funds	\$ 21	\$ -	\$ 21	\$ -
Certificate of deposit	286,140	-	286,140	
Domestic common stocks:				
Energy	256	256	-	-
Technology	-	-	-	-
TOTAL ASSETS AT FAIR VALUE	<u>\$ 286,417</u>	<u>\$ 256</u>	<u>\$ 286,161</u>	<u>\$ -</u>
Financial Liabilities				
Interest rate swap agreement	<u>\$ 334,183</u>	<u>\$ -</u>	<u>\$ 334,183</u>	<u>\$ -</u>
At June 30, 2018	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Financial Assets				
Money market funds	\$ 21	\$ -	\$ 21	\$ -
Certificate of deposit	265,434	-	265,434	
Domestic common stocks:				
Energy	693	693	-	-
Technology	2,128	2,128	-	-
TOTAL ASSETS AT FAIR VALUE	<u>\$ 268,276</u>	<u>\$ 2,821</u>	<u>\$ 265,455</u>	<u>\$ -</u>
Financial Liabilities				
Interest rate swap agreement	<u>\$ 165,523</u>	<u>\$ -</u>	<u>\$ 165,523</u>	<u>\$ -</u>

BROOK LANE HEALTH SERVICES, INC.
Notes to Financial Statements

NOTE 17 RELATED PARTIES

During the years ended June 30, 2019 and 2018, Brook Lane Health Services, Inc. charged Brook Lane Behavioral Health Services, Inc. a management fee of \$ 127,499 and \$ 125,000, respectively. During the year ended June 30, 2019, Brook Lane Health Services, Inc. charged Brook Lane Behavioral Health Services, Inc. for contracted capital costs of \$ 234,448. These are included in other income in the statements of operations.

Brook Lane Health Services, Inc. has a \$ 1,165,830 receivable from Brook Lane Behavioral Services, Inc. as of June 30, 2019 that is recorded as amounts due from affiliates in the balance sheets. Management believes this amount will ultimately be collected.

Brook Lane Health Services, Inc. transferred \$ 757,427 to Brook Lane Behavioral Health Services, Inc. during the year ended June 30, 2018. This is reported as transfer to affiliate in the statements of operations

NOTE 18 SUBSEQUENT EVENTS

Brook Lane has evaluated events and transactions subsequent to June 30, 2019 through October 21, 2019, the date these financial statements were available to be issued. Based on the definitions and requirements of generally accepted accounting principles, management has not identified any events that require recognition or disclosure in the financial statements.