Consolidated Financial Statements

2021

**Seven Counties Services, Inc.**

June 30, 2021 and 2020

Strothman+Co

Consolidated Financial Statements

**Seven Counties Services, Inc.**

June 30, 2021 and 2020

**Strothman and Company**
*Certified Public Accountants and Advisors*
1600 Waterfront Plaza
325 West Main Street
Louisville, KY 40202
502 585 1600

Strothman+Co

## Independent Auditors' Report

To the Board of Directors
Seven Counties Services, Inc.
Louisville, Kentucky

### Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Seven Counties Services, Inc. and its subsidiary (formerly Centerstone of Kentucky, Inc.) (the "Corporation"), which comprise the consolidated statement of financial position as of June 30, 2021, and the related consolidated statements of activities, functional expenses, and cash flows for the year 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit 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 consolidated financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the Corporation's preparation and fair presentation of the consolidated 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 Corporation'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 consolidated 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 financial position of the Corporation as of June 30, 2021, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### Emphasis of Matter

As explained in Note A to the consolidated financial statements, the Corporation was part of an affiliated group of entities. The Corporation was included in the reporting entity, Centerstone of America, Inc. through June 30, 2020, and the 2020 consolidated financial statements include only the financial position, activities, functional expenses, and cash flows of the Corporation. Our opinion is not modified with respect to this matter.

### Uncertainty Regarding the Future Outcome of Litigation

As discussed in Note M to the consolidated financial statements, the Corporation is the defendant in a lawsuit regarding participation in the Kentucky Employee Retirement System. The legal matter has been in various stages of litigation since 2013. Management and legal counsel for the Corporation are of the opinion that the legal action is without merit, and they plan to vigorously defend their position. However, it is at least reasonably possible that a negative outcome will occur, although the amount cannot be estimated. Settlement of the legal action is not expected within the next year. Our opinion is not modified with respect to this matter.

### Other Matter--2020 Consolidated Financial Statements

The consolidated financial statements of the Corporation as of June 30, 2020 and for the year then ended, were audited by other auditors. Those auditors expressed an unqualified opinion on those consolidated financial statements in their report dated December 17, 2020.

Strothman and Company

Louisville, Kentucky
November 23, 2021

Consolidated Statements of Financial Position

**Seven Counties Services, Inc.**

| | June 30 2021 | June 30 2020 |
|---|---|---|
| **Assets** | | |
| **Current Assets** | | |
| Cash, restricted cash and cash equivalents | $ 9,203,138 | $ 5,526,972 |
| Investments | 4,211,921 | 4,180,393 |
| Accounts receivable, net | 2,556,868 | 2,287,722 |
| Other receivables | 2,813,970 | 1,903,897 |
| Prepaid expenses and other current assets | 1,088,809 | 1,292,409 |
| **Total Current Assets** | 19,874,706 | 15,191,393 |
| **Property and Equipment**, net | 8,755,322 | 9,988,422 |
| **Other Assets,** net | 1,457,500 | 1,602,500 |
| | $ 30,087,528 | $ 26,782,315 |
| **Liabilities and Net Assets** | | |
| **Current Liabilities** | | |
| Accounts payable and accrued expenses | $ 3,888,245 | $ 5,655,013 |
| Accrued payroll, benefits and taxes | 7,261,694 | 6,311,461 |
| Due to affiliated entities, net | 30,000 | 988,229 |
| Current portion of long-term debt | 472,675 | 759,251 |
| **Total Current Liabilities** | 11,652,614 | 13,713,954 |
| **Long-Term Debt,** less current portion | 370,202 | 842,877 |
| **Other Long-Term Liabilities** | 1,272,589 | 808,497 |
| **Total Liabilities** | 13,295,405 | 15,365,328 |
| **Net Assets** | | |
| Without donor restrictions | 15,038,337 | 9,444,322 |
| With donor restrictions | 1,753,786 | 1,972,665 |
| **Total Net Assets** | 16,792,123 | 11,416,987 |
| **Total Liabilities and Net Assets** | $ 30,087,528 | $ 26,782,315 |

See Notes to Consolidated Financial Statements

Consolidated Statements of Activities

**Seven Counties Services, Inc.**

| | Year Ended June 30 | |
|---|---|---|
| | **2021** | **2020** |
| **Net Assets Without Donor Restrictions** | | |
| **Revenues and Support** | | |
| Net client service revenue, net | $ 45,015,077 | $ 50,087,674 |
| Public support | 45,295,954 | 43,866,684 |
| Rental income | 364,499 | 388,187 |
| In-kind contributions | 680,437 | 614,665 |
| Other operating revenue | 966,062 | 1,424,424 |
| Net assets released from restrictions | 251,235 | 150,050 |
| **Total Revenues and Support** | 92,573,264 | 96,531,684 |
| **Expenses** | | |
| **Program Services** | | |
| Mental health | 40,214,954 | 45,112,578 |
| Developmental disabilities | 9,131,285 | 9,028,361 |
| Substance abuse | 13,184,065 | 12,520,263 |
| Trust and agency | 15,065,285 | 15,323,631 |
| **Total Program Services** | 77,595,589 | 81,984,833 |
| **Support Services** | | |
| General and administrative | 9,012,634 | 15,992,216 |
| Fundraising | 170,461 | 492,062 |
| **Total Support Services** | 9,183,095 | 16,484,278 |
| **Total Expenses** | 86,778,684 | 98,469,111 |
| **Operating Income (Loss)** | 5,794,580 | (1,937,427) |
| **Nonoperating Revenues (Expenses)** | | |
| Loss on disposal of assets | (310,059) | (50) |
| Investment income and other | 109,494 | 170,087 |
| **Total Nonoperating (Expenses) Revenues** | (200,565) | 170,037 |
| **Change in Net Assets Without Donor Restrictions** | 5,594,015 | (1,767,390) |
| **Net Assets With Donor Restrictions** | | |
| Restricted public support | 32,356 | 40,776 |
| Net assets released from donor restrictions | (251,235) | (150,050) |
| **Change in Net Assets With Donor Restrictions** | (218,879) | (109,274) |
| **Change in Net Assets** | 5,375,136 | (1,876,664) |
| **Net Assets Beginning of Year** | 11,416,987 | 13,293,651 |
| **Net Assets End of Year** | $ 16,792,123 | $ 11,416,987 |

See Notes to Consolidated Financial Statements

Consolidated Statement of Functional Expenses

**Seven Counties Services, Inc.**

For the Year Ended June 30, 2021

| | Mental Health | Developmental Disabilities | Addiction Services | Trust and Agency | Total Program Services | General and Administrative | Fundraising | Total Expenses |
|---|---|---|---|---|---|---|---|---|
| Salary and fringe benefits | $ 34,652,215 | $ 6,530,763 | $ 7,887,751 | $ 14,928,469 | $ 63,999,198 | $ 4,776,625 | $ 27,992 | $ 68,803,815 |
| Professional fees | 388,908 | 2,048,976 | 303,795 | 14,911 | 2,756,590 | 1,082,815 | 114,471 | 3,953,876 |
| Facilities | 2,261,355 | 91,025 | 1,852,238 | | 4,204,618 | 133,302 | 3,441 | 4,341,361 |
| Equipment | 410,293 | 76,608 | 136,504 | | 623,405 | 56,466 | 574 | 680,445 |
| Depreciation | 523,483 | 37,814 | 217,866 | | 779,163 | 752,188 | 3,000 | 1,534,351 |
| Travel and transportation | 149,659 | 3,517 | 86,588 | 414 | 240,178 | 12,920 | 136 | 253,234 |
| Consumables | 350,065 | 28,120 | 684,976 | | 1,063,161 | 67,406 | 231 | 1,130,798 |
| Communications | 473,629 | 82,734 | 166,268 | 1,328 | 723,959 | 68,610 | 968 | 793,537 |
| Interest | 31,037 | | 3,333 | | 34,370 | 13,901 | | 48,271 |
| Computer hardware and software | 58,326 | 6,695 | 25,803 | | 90,824 | 1,567,343 | 15 | 1,658,182 |
| Miscellaneous | 915,984 | 225,033 | 1,818,943 | 120,163 | 3,080,123 | 481,058 | 19,633 | 3,580,814 |
| **Total Functional Expenses** | $ 40,214,954 | $ 9,131,285 | $ 13,184,065 | $ 15,065,285 | $ 77,595,589 | $ 9,012,634 | $ 170,461 | $ 86,778,684 |

See Notes to Consolidated Financial Statements

Consolidated Statement of Functional Expenses

**Seven Counties Services, Inc.**

For the Year Ended June 30, 2020

| | Mental Health | Developmental Disabilities | Substance Abuse | Trust and Agency | Total Program Services | General and Administrative | Fundraising | Total Expenses |
|---|---|---|---|---|---|---|---|---|
| Salary and fringe benefits | $ 38,149,853 | $ 6,473,752 | $ 8,112,865 | $ 15,200,330 | $ 67,936,800 | $ 2,739,981 | | $ 70,676,781 |
| Professional fees | 551,315 | 1,863,024 | 83,997 | 1,388 | 2,499,724 | 1,444,547 | | 3,944,271 |
| Facilities | 2,336,402 | 120,819 | 1,767,579 | | 4,224,800 | 363,148 | | 4,587,948 |
| Equipment | 462,678 | 79,359 | 183,729 | | 725,766 | 95,607 | | 821,373 |
| Depreciation | 510,613 | 40,362 | 276,515 | | 827,490 | 301,231 | | 1,128,721 |
| Travel and transportation | 469,758 | 143,213 | 143,649 | 1,368 | 757,988 | 33,563 | | 791,551 |
| Supplies | 347,121 | 25,082 | 713,317 | 886 | 1,086,406 | 94,396 | | 1,180,802 |
| Communications | 459,262 | 82,906 | 146,547 | 211 | 688,926 | 86,003 | | 774,929 |
| Affiliated management fees | | | | | | 8,939,080 | $ 492,062 | 9,431,142 |
| Interest | 44,500 | | 7,285 | | 51,785 | 30,960 | | 82,745 |
| Computer hardware and software | 94,768 | 2,528 | 29,972 | | 127,268 | 985,157 | | 1,112,425 |
| Miscellaneous | 1,686,308 | 197,316 | 1,054,808 | 119,448 | 3,057,880 | 878,543 | | 3,936,423 |
| **Total Functional Expenses** | $ 45,112,578 | $ 9,028,361 | $ 12,520,263 | $ 15,323,631 | $ 81,984,833 | $ 15,992,216 | $ 492,062 | $ 98,469,111 |

See Notes to Consolidated Financial Statements

Consolidated Statements of Cash Flows

**Seven Counties Services, Inc.**

| | Year Ended June 30 | |
|---|---|---|
| | **2021** | **2020** |
| **Operating Activities** | | |
| Change in net assets | $ 5,375,136 | $ (1,876,664) |
| Adjustments to reconcile change in net assets to net cash provided by operating activities | | |
| Loss on disposal of assets | 310,059 | 50 |
| Depreciation | 1,534,351 | 1,128,721 |
| Affiliated management fees related to property and equipment | | 291,592 |
| Investment income (loss) | 109,494 | (60,400) |
| Changes in operating assets and liabilities | | |
| Accounts receivable, net | 269,146 | 3,413,541 |
| Due to affiliates | (940,343) | (1,149,418) |
| Other receivables | (910,073) | 691,551 |
| Prepaid expenses and other assets | (348,600) | (88,233) |
| Accounts payable and accrued expenses | (1,766,768) | 829,436 |
| Accrued payroll, benefits and taxes | 950,233 | 509,400 |
| Other long-term liabilities | 464,092 | 808,497 |
| **Net Cash Provided By Operating Activities** | 5,046,727 | 4,498,073 |
| **Investing Activities** | | |
| Purchase of property and equipment | (611,310) | (1,409,374) |
| **Financing Activities** | | |
| Principal payments on long-term debt | (759,251) | (557,751) |
| **Increase in Cash, Restricted Cash, and Cash Equivalents** | 3,676,166 | 2,530,948 |
| **Cash, Restricted Cash, and Cash Equivalents Beginning of Year** | 5,526,972 | 2,996,024 |
| **Cash, Restricted Cash, and Cash Equivalents End of Year** | $ 9,203,138 | $ 5,526,972 |
| **Supplemental Cash Flow Information** | | |
| Cash paid for interest | $ 48,310 | $ 85,046 |
| **Noncash Investing Activities** | | |
| Property and equipment received by the Corporation transferred from Centerstone of America, Inc. | | $ 841,281 |

See Notes to Consolidated Financial Statements

## Note A--Description of Business

Description of Business**--**Seven Counties Services, Inc. and its subsidiary (the "Corporation") (formerly known as Centerstone of Kentucky, Inc.) is a community mental health-developmental disabilities organization which provides planning, coordination and direct delivery of mental health, substance abuse and developmental disability services. These services are provided at various centers located throughout various counties in the Commonwealth of Kentucky, with the main administrative offices located in Louisville, Kentucky.

Affiliation**--**Effective November 1, 2016, Centerstone of America, Inc. (“Parent”) assumed control of Seven Counties Services, Inc. and SCS Learning, Inc. (collectively "Seven Counties Services") through sole corporate membership to help further its mission. With the change in control, Seven Counties Services was renamed to Centerstone of Kentucky, Inc. Centerstone of America, Inc. and its affiliates are private, non-profit corporations that provide multifunded, locally directed mental health and addiction services to people of all ages. Centerstone of America, Inc. and its affiliates maintain clinics in multiple locations in Tennessee, Illinois, Kentucky, Florida and Indiana counties, with its main administrative offices located in Nashville, Tennessee. No consideration was paid as a result of the change in control.

On October 31, 2019, the Corporation entered into an agreement to disaffiliate from Centerstone of America, Inc. by June 30, 2020. A final agreement was signed in February 2020 and the Corporation changed its name back to Seven Counties Services, Inc. The disaffiliation was effective June 30, 2020. The Corporation will pay residual costs related to the disaffiliation to Centerstone of America, Inc. beginning on July 1, 2020 of approximately $1,000,000 which is included in net due to affiliated entities on the accompanying consolidated statements of financial position as of June 30, 2020.

## Note B--Summary of Significant Accounting Policies

The Corporation follows generally accepted accounting principles outlined in the Financial Accounting Standards Board’s (“FASB”) *Accounting Standards Codification* (“ASC”). Significant accounting policies are as follows:

Principles of Consolidation--The consolidated financial statements include Seven Counties Services, Inc. and Personnel Best, LLC. Seven Counties Services, Inc. controls and provides all management and support services. All intercompany balances and transactions have been eliminated in consolidation.

Seven Counties Services, Inc. is the sole member of Personnel Best, LLC, a limited liability company. Personnel Best, LLC serves as a pass-through entity to receive benefit payments and process the corresponding payroll to providers for Kentucky Medicaid recipients who receive benefits under the Kentucky Consumer Directed Options program.

Continued

**Note B--Summary of Significant Accounting Policies**--Continued

Affiliated Entities and Related Parties--The Corporation was part of an affiliated group of entities through June 30, 2020. The Corporation was included in the reporting entity, Centerstone of America, Inc. ("Parent"), and these consolidated financial statements include only the financial position, changes in net assets and cash flows of the Corporation and its subsidiary.

The Parent was the holding company and was the sole corporate member of the Corporation prior to June 30, 2020.

Basis of Presentation--Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Corporation and changes therein are classified and reported as follows:

> Net Assets Without Donor Restrictions--Net assets that are not restricted by donor-imposed restrictions and available to support operations. The only limits on the use of net assets without donor restrictions are the broad limits resulting from the nature of the Corporation, the environment in which it operates, the purposes specified in its corporate documents and its application for tax-exempt status, and any limits resulting from contractual agreements with creditors and others that are entered into in the course of its operations.
>
> Net Assets With Donor Restrictions--Net assets resulting from contributions and other inflows of net assets whose use by the Corporation is limited by donor-imposed restrictions. These include net assets with donor restrictions, some of which may or will be met either by action of the Corporation and/or passage of time. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated statements of activities as net assets released from restrictions. These also include net assets with donor restrictions that neither expire by the passage of time nor can be fulfilled or otherwise removed by actions of the Corporation. Net assets with donor restrictions at June 30, 2021 and 2020 represent donor restricted funds designated for various programs offered by the Corporation, and contributed rent.

Cash and Cash Equivalents--For purposes of reporting cash flows, the Corporation considers all liquid investments with an original maturity of three months or less to be cash equivalents. The Corporation maintains these deposits with banks. At times, these deposits may exceed federally insured limits. The Corporation believes it is not exposed to any significant credit risk on cash and cash equivalents.

Continued

**Note B--Summary of Significant Accounting Policies**--Continued

Investments--Investments are reported at fair value, based primarily on market quotes. In the accompanying consolidated statements of activities, cumulative market appreciation on donor restricted funds is classified as with donor restriction in cases where the donor has placed temporary restrictions on the use of the income until the restrictions have been met. Where no donor restrictions are placed on the use of income, the market appreciation and other income is classified as without donor restriction.

Investments include certificates of deposits and cash and cash equivalents. Certificates of deposit (regardless of original maturity) are recorded at fair value in accordance with FASB ASC 820, *Fair Value Measurement*. Interest income is accounted for in accordance with donor restrictions or, in the absence of specific donor restrictions, as without donor restrictions.

Accounts Receivable--The accounts receivable balance represents the unpaid amounts billed to clients and third party payors. Implicit and explicit price concessions (formerly known as contractual adjustments, discounts and an allowance for doubtful accounts) are recorded to report receivables for client care services at net realizable value.

Client accounts receivable are reduced by appropriate implicit price concessions (formerly allowances for doubtful accounts) based on the Corporation's evaluation of its major payor sources of revenue, the aging of the accounts, historical losses, current economic conditions, and other factors unique to its service area and the healthcare industry. Management regularly reviews data about the major payor sources of revenue in evaluating the sufficiency of implicit price concessions. For receivables associated with services provided to clients who have third-party coverage, the Corporation analyzes contractually due amounts and provides explicit price concessions (formerly known as allowance for contractual adjustments) and implicit price concessions (formerly known as provision for bad debts), if necessary. For receivables associated with self-pay payments, which includes both clients without insurance and clients with deductible and copayment balances due for which third party coverage exists for part of the bill, the Corporation records implicit price concessions in the period of service on the basis of its past experience, which indicates that many clients are unable or unwilling to pay the portion of their bill for which they are financially responsible.

Other Receivables--The Corporation has recorded receivables from federal and state agencies related to grants under contract. The Corporation expects full collection of these receivables.

Property and Equipment and Depreciation--Property and equipment are stated at cost. Depreciation is provided over the assets' estimated useful lives using the straight-line method as follows:

| | |
|---|---|
| Buildings and improvements | 10 – 30 years |
| Furnishings, equipment and vehicles | 3 – 10 years |

Expenditures for maintenance and repairs are expensed when incurred. Expenditures for renewals or betterments are capitalized. When property is retired or sold, the cost and the related accumulated depreciation are removed from the accounts, and the resulting gain or loss is recorded as a change in net assets.

Continued

**Note B--Summary of Significant Accounting Policies**--Continued

Gifts of long-lived assets such as land, buildings or equipment are reported as without donor restrictions, unless explicit donor stipulations specify how the donated assets must 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 with donor restrictions. 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.

Contributed Rent Receivable--The Corporation has a donated lease with Seven Counties Addictions Recovery Center ("SCARC"), formerly known as Jefferson Alcohol and Drug Abuse Center ("JADAC"), from Louisville Metro Government. Future contributed rent under this lease is valued at $1,522,500 and $1,667,500 at June 30, 2021 and 2020, respectively, and is being amortized over the life of the lease which matures December 31, 2031. Contributed rent receivable is included in other assets on the consolidated statements of financial position.

Net Client Service Revenue--The Corporation recognizes net client service revenues on the accrual basis of accounting in the reporting period in which services are performed based on the current gross charge structure, less implicit and explicit price concessions (adjustments and estimated discounts for contractual allowances), principally for clients covered by Medicare, Medicaid, and managed care and other health plans. Gross client service revenue is recorded in the accounting records using the established rates for the type of service provided to the client. The Corporation recognizes an estimated explicit price concession to reduce gross client charges to the estimated net realizable amount for services rendered based upon previously agreed to rates with a payor. The Corporation utilizes the client billing system to calculate explicit price concessions on a payor by payor basis based on historical collections. The management of the Corporation continually reviews the process to consider and incorporate updates to laws and regulations and the frequent changes in managed care contractual terms that result from contract renegotiations and renewals.

Payors include federal and state agencies, including Medicare and Medicaid, managed care health plans, commercial insurance companies, and employers. These third-party payors provide payments to the Corporation at amounts different from its established rates based on negotiated reimbursement agreements. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, discounted charges, and fee schedule payments. Retroactive adjustments under reimbursement agreements with third-party payors are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Given the current regulatory and reimbursement environment, there can be no assurances that adequate reimbursement levels will continue to be available for the services provided by the Corporation. Significant limits on the scope of services reimbursed and on reimbursement rates and fees could have a material adverse effect on the Corporation's liquidity, financial condition, results of operations and cash flows.

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

Continued

**Note B--Summary of Significant Accounting Policies**--Continued

Charity Care--The Corporation provides care to clients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. The charity care amounts are not reported as net client service revenue as the Corporation does not pursue collection. Amounts for forgone charges related to charity care are approximately $2,251,000 and $3,174,000 for the years ended June 30, 2021 and 2020, respectively.

Of the Corporation's total unrestricted operating expenses pertaining to providing client care, an estimated $2,278,000 and $2,543,000 arose from providing services to charity care clients during the years ended June 30, 2021 and 2020, respectively.

The estimated costs of providing charity care services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity clients. The ratio of cost to charges is calculated based on the Corporation's total expenses divided by gross client service revenue.

Public Support--The Corporation receives federal, state, and county grants for providing services in specific program areas. Receipt of these funds is subject to the fulfillment of certain obligations by the Corporation as prescribed by these programs and funds may be subject to repayment upon a determination of noncompliance made by a funding agency.

The Corporation has contracts with the State of Kentucky to provide community mental health services. During 2021 and 2020, the Corporation was paid by the State based upon applicable contractually agreed to stipulations.

The Corporation derives a significant portion of its revenue from third-party payors and federal, state and county funding programs. The receipt of future revenues by the Corporation is subject to among other factors, federal, state, and county policies affecting the health care industry, economic conditions that may include an inability to control expenses in periods of inflation, increased competition, market pressures on premium rates and other conditions which are impossible to predict.

Contributions--Contributions received and unconditional promises to give are recorded as revenue without donor restrictions or revenue with donor restrictions depending on the existence of donor restrictions, if they exist.

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statements of activities as net assets released from restriction.

If a restriction is fulfilled in the same accounting period in which the contribution is received, the contribution is reported as support without donor restrictions.

In-kind contributions are recorded based on their estimated fair value at the date of donation.

Continued

**Note B--Summary of Significant Accounting Policies**--Continued

Advertising Costs--The Corporation uses advertising to promote its programs and services among the general public. The advertising costs are expensed as incurred. Advertising costs for the Corporation totaled approximately $188,000 and $65,000 for 2021 and 2020, respectively.

Income Taxes--The Corporation and its subsidiary are organized as not-for-profit corporations under Section 501(c)(3) of the United States Internal Revenue Code ("IRC"). The Corporation and its subsidiary had no unrelated business income for the fiscal years ended June 30, 2021 and 2020. Personnel Best, LLC is a disregarded entity for tax purposes, and its activity is included with Seven Counties Services, Inc. for tax reporting.

Accounting principles generally accepted in the United States of America (“GAAP”) requires management to evaluate tax positions taken and recognize a tax liability if it is more likely than not that an uncertain tax position would not be sustained upon examination by various federal and state taxing authorities. Management has analyzed the tax positions taken and has concluded that as of June 30, 2021 and 2020, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the accompanying consolidated financial statements. The Corporation is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

Performance Indicator and Operating Indicator--The consolidated statements of activities include a performance indicator, excess of expenses over revenues for June 30, 2021 and 2020. Changes in net assets without restrictions which would be excluded from the performance indicator, consistent with industry practice, include net assets released for long-lived assets and contributions to supported entities. The consolidated statements of activities also include an operating indicator, operating income (loss) for June 30, 2021 and 2020. Certain non-operating items are excluded from the operating indicator, including investment income, contributions from donors and related parties, other non-operating income and gains (losses) on disposal of equipment.

Use of Estimates--The preparation of consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues, support and expenses during the reporting period. Actual results could differ from those estimates.

Functional Expenses--The consolidated financial statements report certain categories of expenses that are attributable to one or more program or supporting functions of the Corporation. Therefore, expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include salaries and fringe benefits, professional fees, facilities, equipment, depreciation, travel and transportation, supplies, communications, interest, and miscellaneous expenses. Other than depreciation and amortization, these costs are allocated based on management's estimates of time and effort involved for each program or supporting function. Depreciation expense is allocated based on management's assessment of administrative square footage used as a percent of the total facility's square footage.

Continued

**Note B--Summary of Significant Accounting Policies**--Continued

Subsequent Events--The Corporation has evaluated events and transactions that occurred through November 23, 2021, which is the date that the consolidated financial statements were available to be issued, for possible recognition or disclosure in the consolidated financial statements.

**Note C--Other Receivables**

Other receivables consist of the following:

| | June 30 | |
|---|---|---|
| | **2021** | **2020** |
| U.S. Department of Health and Human Services | $ 1,348,091 | $ 650,450 |
| Metro Louisville | 264,711 | 141,465 |
| Kentucky Department of Behavioral Health | 336,692 | |
| University of Louisville | 18,875 | 46,842 |
| Other agencies | 845,601 | 1,065,140 |
| | $ 2,813,970 | $ 1,903,897 |

**Note D--Investments**

Accounting standards establish a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. This hierarchy consists of three broad levels: *Level 1* inputs consist of unadjusted quoted prices in active markets for identical assets and have the highest priority, and *Level 3* inputs have the lowest priority. The Corporation uses appropriate valuation techniques based on the available inputs to measure the fair value of its investments. When available, the Corporation measures fair value using *Level 1* inputs because they generally provide the most reliable evidence of fair value. *Level 3* inputs were only used when *Level 1* or *Level 2* inputs were not available.

*Level 1 Fair Value Measurements* - The fair values of cash equivalents and U.S. Government securities are based on quoted market prices.

*Level 2 Fair Value Measurements* - The fair values of certificates of deposits are based upon the stated interest rates compared to current market interest rates.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Corporation believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Continued

**Note D--Investments**--Continued

Investment securities are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risk in the near term would result in material changes in the fair value of investments and net assets of the Corporation.

The investments of the Corporation are reported at fair value in the accompanying consolidated statements of financial position. The following table presents the fair value of investments at June 30, 2021 and 2020:

| | Fair Value | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Unobservable Inputs (Level 2) |
|---|---|---|---|
| **June 30, 2021** | | | |
| U. S. Government securities | $ 3,145,000 | $ 3,145,000 | |
| Cash equivalents | 850,000 | 850,000 | |
| **Total Assets in Fair Value Hierarchy** | 3,995,000 | $ 3,995,000 | $ |
| Beneficial interests held by outside foundations | 217,000 | | |
| **Total Investments** | $ 4,212,000 | | |
| **June 30, 2020** | | | |
| Certificate of deposits | $ 2,008,000 | | $ 2,008,000 |
| U. S. Government securities | 1,900,000 | $ 1,900,000 | |
| Cash equivalents | 81,000 | 81,000 | |
| **Total Assets in Fair Value Hierarchy** | 3,989,000 | $ 1,981,000 | $ 2,008,000 |
| Beneficial interests held by outside foundations | 191,000 | | |
| **Total Investments** | $ 4,180,000 | | |

Continued

**Note D--Investments**--Continued

Investment income and other includes the following:

| | June 30 | |
|---|---|---|
| | 2021 | 2020 |
| Interest income | $ 60,076 | $ 170,087 |
| Dividend income | 49,418 | |
| | $ 109,494 | $ 170,087 |

**Note E--Concentrations of Credit Risk**

The mix of the accounts receivable and net client service revenue is as follows:

| | Receivables | | Revenue | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| Medicare | 4% | 4% | 3% | 2% |
| Medicaid | 74% | 80% | 90% | 93% |
| Self-pay | 7% | 11% | 2% | 3% |
| Other third-party payors | 15% | 5% | 5% | 2% |
| | 100% | 100% | 100% | 100% |

**Note F--Property and Equipment**

Property and equipment consist of the following:

| | June 30 | |
|---|---|---|
| | **2021** | **2020** |
| Land | $ 1,434,900 | $ 1,434,900 |
| Buildings and improvements | 11,470,172 | 11,637,341 |
| Furnishings, equipment and vehicles | 7,829,670 | 7,212,716 |
| | 20,734,742 | 20,284,957 |
| Less accumulated depreciation | 12,019,420 | 10,581,369 |
| | 8,715,322 | 9,703,588 |
| Construction in progress | 40,000 | 284,834 |
| | $ 8,755,322 | $ 9,988,422 |

**Note G--Liquidity and Availability**

The Corporation regularly monitors liquidity required to meet its operating needs and other commitments, while also striving to maximize the investment of its available funds. As part of the Corporation's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities and other obligations come due.

Financial assets available for general expenditures within one year of the consolidated statements of financial position at June 30, 2021 and 2020 are as follows:

| | June 30 | |
|---|---|---|
| | **2021** | **2020** |
| Cash and cash equivalents | $ 9,182,281 | $ 5,526,972 |
| Investments | 3,994,550 | 3,989,086 |
| Accounts receivable, net | 2,556,868 | 2,287,722 |
| Other receivables | | 305,186 |
| | $ 15,733,699 | $ 12,108,966 |

None of the above assets are subject to donor or other restrictions. Investments excludes approximately $217,000 and $191,000 as of June 30, 2021 and 2020, respectively, related to investments held in outside foundations. Other receivables exclude approximately $2,835,000 and $1,599,000, as of June 30, 2021 and 2020, respectively, which are related to certain grants received by the Corporation. The Corporation also has a $2,000,000 line of credit that could be utilized (see Note H).

**Note H--Long-Term Debt**

A summary of long-term debt is as follows:

| | June 30 | | | |
|---|---|---|---|---|
| | 2021 | | 2020 | |
| Note payable to Republic Bank in monthly installments of $63,113 including interest at 3.85% through October 3, 2021. Subsequent to year end, this note was repaid in full. | $ | 436,063 | $ | 1,160,979 |
| Note payable to landlord in monthly installments of $4,494 including interest at 7.00% through July 1, 2029 | | 329,634 | | 359,351 |
| Other note payable | | 77,180 | | 81,798 |
| | | 842,877 | | 1,602,128 |
| Less current portion | | 472,675 | | 759,251 |
| **Long-Term Debt,** less current portion | $ | 370,202 | $ | 842,877 |

In June 2014, the Corporation entered into a debt agreement with the landlord of a leased facility. The debt acquired was for $500,000 used to finance the construction of leasehold improvements with the debt being repaid to the landlord over the life of the lease. This note payable is unsecured.

In October 2016, the Corporation entered into a debt agreement with Republic Bank for $3,435,000. The loan is secured by certain real and personal property. In April 2020, the terms of the loan were modified to defer payments for three months due to the COVID-19 pandemic. Standard payments resumed in July 2020. The deferred payments will be due along with all unpaid principal and interest upon maturity. The Corporation made the last payment in July 2021, which covered August through October payments. In August 2021, the Corporation paid the deferred payments, including interest.

In November 2018, the Corporation entered into a revolving line of credit in the amount of $2,000,000, secured by substantially all assets. There were no borrowings outstanding as of June 30, 2021 or 2020. In November 2020, the maturity date was extended to November 18, 2021.

Continued

**Note H--Long-Term Debt**--Continued

Aggregate annual maturities of long-term debt as of June 30, 2021 are as follows:

| Year Ending June 30 | |
|---|---|
| 2022 | $ 472,675 |
| 2023 | 38,963 |
| 2024 | 41,481 |
| 2025 | 44,178 |
| 2026 | 47,067 |
| Thereafter | 198,513 |
| | $ 842,877 |

**Note I--Net Assets With Donor Restrictions**

Net assets with donor restrictions consist of the following:

| | June 30 | |
|---|---|---|
| | **2021** | **2020** |
| Specified Period of Time: | | |
| Contributed rent | $ 1,522,500 | $ 1,667,500 |
| Other | 30,649 | 39,069 |
| | 1,553,149 | 1,706,569 |
| Specified Purpose or Use: | | |
| Shepherd's Garden Apartments | 179,780 | 179,780 |
| Reserve cash funds | 20,857 | 19,150 |
| Other | | 67,166 |
| | 200,637 | 266,096 |
| | $ 1,753,786 | $ 1,972,665 |

## Note J--Public Support

The composition of public support is set forth in the following table:

| | For the Year Ended June 30 | |
|---|---|---|
| | 2021 | 2020 |
| Kentucky Department for Behavioral Health, Developmental and Intellectual Disabilities | $ 16,765,846 | $ 17,485,578 |
| Louisville Metro Government | 778,309 | 773,741 |
| Other state funds | 22,896,592 | 22,250,794 |
| Federal funds | 3,973,781 | 2,788,051 |
| Other public support | 881,426 | 568,520 |
| | $ 45,295,954 | $ 43,866,684 |

## Note K--Defined Contribution Plan

The Corporation has a 403(b) defined contribution plan (the "Plan"). Contributions are made to employees who meet the eligibility requirements. Effective January 1, 2019, the Corporation matches up to 3% of the participating employees' compensation. Employer contributions to the Plan were approximately $1,129,000 and $1,060,000 for 2021 and 2020, respectively.

## Note L--Affiliated Entities and Related Party Transactions

During the fiscal year ended June 30, 2020, the Corporation was a party to certain working capital, administrative and general transactions with its Parent as are disclosed in Note A. The services provided included finance, payroll, human resources, marketing, executive support, and other supporting services. The Corporation incurred a net related party payable of approximately $988,000 that is reported in current liabilities as of June 30, 2020. This management agreement terminated effective June 30, 2020.

The Corporation entered into a management services agreement (the "Agreement") with a nonprofit corporation effective July 1, 2018. The Corporation received a management fee of $500 each month which is included in other operating revenue on the consolidated statement of activities. There were no amounts due from the nonprofit corporation at June 30, 2021 and 2020. The Corporation is reimbursed for direct expense incurred related to salaries and benefits per the Agreement. These expenses and reimbursements are reported at net on the consolidated statements of activities.

## Note M--Commitments and Contingencies

*Operating Leases*

The Corporation has several non-cancelable operating leases for facilities and equipment through 2029. Total rent expense was approximately $2,787,000 and $3,064,000 for the years ended June 30, 2021 and 2020, respectively, which includes the fair market value of the donated lease of SCARC from Louisville Metro Government of $519,133 and $630,767 for the years ended June 30, 2021 and 2020, respectively.

A summary of approximate future minimum payments under these leases as of June 30, 2021 is as follows:

| Year Ending June 30 | |
|---|---|
| 2022 | $ 2,219,000 |
| 2023 | 1,501,000 |
| 2024 | 1,270,000 |
| 2025 | 677,000 |
| 2026 | 681,000 |
| Thereafter | 2,767,000 |
| | $ 9,115,000 |

*Insurance*

The Corporation participates in a multi-provider insurance program which provides professional and general liability insurance to cover medical malpractice claims. Insurance coverages are $1,000,000 individually and $3,000,000 in the aggregate annually. There are known claims and incidents that may result in the assertion of additional claims, as well as claims from unknown incidents that may be asserted arising from services provided to clients.

The Corporation is self-insured for certain costs related to employee health, dental and accident benefit programs. Expenses resulting from claims experience are recorded as incurred including an estimate of claims incurred but not reported. The accrued liability for such covered medical claims was approximately $335,000 and $600,000 at June 30, 2021 and 2020, respectively, and is included in accrued expenses in the consolidated statements of financial position.

The Corporation has purchased insurance, which limits its exposure on a per individual basis to $200,000 annually and no annual aggregate.

*Litigation*

The Corporation is involved in certain litigation arising in the ordinary course of business and has made provisions for any known estimable settlements. The Corporation is also involved in other litigation for which the outcome is unknown. After consultation with legal counsel, it is management's opinion that these matters will be resolved without material adverse effect on the Corporation's financial position, results of operations, or cash flows.

Continued

**Note M--Commitments and Contingencies**--Continued

*Litigation - Kentucky Employee Retirement System*

On April 4, 2013, the Corporation filed a petition for relief under Chapter 11 of the federal bankruptcy laws in the United States Bankruptcy Court and filed a motion to terminate participation in Kentucky Employee Retirement System ("KERS"). The Corporation's liability to KERS, which was in existence prior to filing for bankruptcy under Chapter 11 was stayed while the Corporation continued business operations.

In May 2014, the Court ruled that the Corporation was neither a state entity nor a state instrumentality and thus had legal standing to seek relief under Chapter 11 and withdraw from KERS. The Corporation officially emerged from bankruptcy in February 2015.

Various motions were filed related to the April 4, 2013 filing, and the court ruled, following an evidentiary hearing, that KERS was not entitled to injunctive relief to compel the Corporation to continue making reports and employer and employee contributions into the KERS plan. KERS appealed the court's ruling allowing relief under Chapter 11 to the United States Sixth Circuit Court of Appeals.

Following briefing and argument, the Court of Appeals affirmed that the Corporation was eligible to seek relief under Chapter 11 of the Bankruptcy Code. It certified to the Kentucky Supreme Court the question of whether the Corporation's participation in, and contributions to, KERS were based on a statutory obligation. On August 29, 2019, the Kentucky Supreme Court issued an opinion stating that the Corporation's participation in KERS was statutory in nature.

The case returned to the United States Sixth Circuit Court of Appeals, which asked for supplemental briefing on the effect of the Kentucky Supreme Court's decision on KERS's pending appeal and the Corporation's pending cross-appeal. On July 20, 2020, the Sixth Circuit issued a ruling that the Corporation's relationship with KERS was statutory in nature. The case has been remanded back to the District Court for further proceedings. It is anticipated that the District Court will further remand the case to Bankruptcy Court.

Recently, the United States Sixth Circuit Court of Appeals supplemented its ruling on the Corporation's relationship with KERS being statutory in nature to include that the Corporation may be liable to KERS for pension contributions accruing during the bankruptcy proceedings, which are estimated to be approximately $18 million.

The Corporation has and continues to take the position that it owes KERS nothing and believes it has meritorious claims and arguments to support this position. However, at this time, the outcome of this litigation cannot be determined.

Continued

**Note M--Commitments and Contingencies**--Continued

*Health Care Industry*

The delivery of personal health care services entails an inherent risk of liability. Participants in the health care services industry have become subject to an increasing number of lawsuits alleging negligence or related legal theories, many of which involve large claims and result in the incurrence of significant exposure and defense costs. The Corporation is insured with respect to medical malpractice risk on a claims-made basis. The Corporation also maintains insurance for general liability, director and officer liability and property. Certain policies are subject to deductibles. In addition to the insurance coverage provided, the Corporation indemnifies certain officers and directors for actions taken on behalf of the Corporation. Management is not aware of any claims against the Corporation which would have a material financial impact.

The health care industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health care program participation requirements, reimbursement for patient services, and Medicare fraud and abuse. Recently, government activity has increased with respect to investigations and/or allegations concerning possible violations of fraud and abuse statutes and/or regulations by health care providers. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that the Corporation is in compliance with fraud and abuse statutes, as well as other applicable government laws and regulations.

*COVID-19 Pandemic*

In January 2020, the Secretary of the U.S. Department of Health and Human Services (“HHS”) declared a national public health emergency due to a novel strain of coronavirus ("COVID-19"). In March 2020, the World Health Organization declared the outbreak of COVID-19 a pandemic. During March 2020, the global pandemic began to affect the Corporation’s facilities, employees, clients, communities, business operations and financial performance, as well as the global economy and financial markets. The Corporation is committed to protecting the health of our communities and has been responding to the evolving COVID-19 situation while taking steps to provide quality care and protect the health and safety of clients and employees. All of the Corporation’s facilities are closely following infectious disease protocols, as well as recommendations by the Centers for Disease Control and Prevention (“CDC”), the National Health Service (“NHS”) and local health officials. The Corporation has taken steps to secure its supply chain, expanded telehealth capabilities and implemented emergency planning in directly impacted markets. Nevertheless, COVID-19 is impacting the Corporation’s business and may have an impact on its financial results that the Corporation is not currently able to quantify. Continuing disruptions to the Corporation’s business as a result of the COVID-19 pandemic could continue to have an effect on its results of operations, financial condition, and cash flows.

Continued

**Note M--Commitments and Contingencies**--Continued

As part of the Coronavirus Aid, Relief and Economic Security Act (the “CARES Act”), the U.S. government announced it would offer relief funding to eligible healthcare providers. During the year ended June 30, 2020, the Corporation participated in certain relief programs offered through the CARES Act including distributions relating to portions of the Public Health and Social Services Emergency Fund (“PHSSE Fund”).

For the year ended June 30, 2021, the Corporation received approximately $1,702,000 in stimulus funds (Provider Relief Funds), which is recorded within public support revenue in the consolidated statements of activities.

As part of the CARES Act, the U.S. government announced it would allow employers to defer the deposit and payment of the employer's share of Social Security taxes for the period from March 27, 2020 through December 31, 2020. The deferred payments are due in two installments with 50% due on or by December 31, 2021 and the remaining 50% being due on or by December 31, 2022. The Corporation deferred approximately $2,545,000 of Social Security taxes as of June 30, 2021. The Corporation deferred approximately $808,000 of Social Security taxes as of June 30, 2020. The amount is reflected in other long-term liabilities in the accompanying consolidated statements of financial position.

**Note N--Future Accounting Standards**

On February 25, 2016, the FASB issued Accounting Standards Update (“ASU”) No. 2016-02 *Leases* (Topic 842). This new standard, which the Corporation is not required to adopt until its year ending June 30, 2023, is intended to improve financial reporting about leasing transactions by requiring entities that lease assets to recognize on their consolidated statement of financial position the assets and liabilities for the rights and obligations creased by those leases, and to provide additional disclosures regarding the leases. Leases with terms (as defined in the ASU) of twelve months or less are not required to be reflected on a corporation’s consolidated statement of financial position.

On September 17, 2020, the FASB issued Accounting Standards Update (“ASU”) 2020-07 *Not-for-Profit Entities* (Topic 958). This new standard, which the Corporation is not required to adopt until its year ending June 30, 2022, is intended to increase transparency for contributed nonfinancial assets through enhancements to presentation and disclosure. Nonfinancial assets include property and equipment, use of property and equipment or utilities, materials and supplies, intangible assets, services and unconditional promises of those assets.

The Corporation is presently evaluating the effects that these ASUs will have on its future consolidated financial statements, including related disclosures.