

HOSPICE OF PALM BEACH COUNTY, INC.

FINANCIAL STATEMENTS

September 30, 2009 and 2008

HOSPICE OF PALM BEACH COUNTY, INC.

FINANCIAL STATEMENTS
September 30, 2009 and 2008

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Crowe Horwath LLP
Independent Member Crowe Horwath International

REPORT OF INDEPENDENT AUDITORS

Board of Directors
Hospice of Palm Beach County, Inc.
West Palm Beach, Florida

We have audited the accompanying balance sheets of Hospice of Palm Beach County, Inc. ("HPBC") as of September 30, 2009 and 2008, and the related statements of operations and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of HPBC's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hospice of Palm Beach County, Inc. as of September 30, 2009 and 2008, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.


Crowe Horwath LLP

South Bend, Indiana
December 17, 2009

HOSPICE OF PALM BEACH COUNTY, INC.
BALANCE SHEETS
September 30, 2009 and 2008

| | <u>2009</u> | <u>2008</u> |
|--|----------------------|----------------------|
| ASSETS | | |
| Current assets | | |
| Cash and cash equivalents | \$ 6,040,353 | \$ 1,417,275 |
| Temporary investments held by affiliate | - | 2,500,000 |
| Patient accounts receivable, net | 8,195,969 | 6,852,670 |
| Bequests receivable | - | 23,250 |
| Due from affiliates | 5,355,877 | 1,223,504 |
| Prepaid and other current assets | <u>1,242,714</u> | <u>1,169,479</u> |
| Total current assets | 20,834,913 | 13,186,178 |
| Investments | 500,000 | - |
| Interest in net assets of Hospice Foundation of Palm Beach County, Inc. ("HFPBC") | 15,511,714 | 16,296,695 |
| Property and equipment, net | 20,585,503 | 19,690,298 |
| Deferred financing costs, net | <u>173,914</u> | <u>181,822</u> |
| | <u>\$ 57,606,044</u> | <u>\$ 49,354,993</u> |
| LIABILITIES AND NET ASSETS | | |
| Current liabilities | | |
| Accounts payable | \$ 625,623 | \$ 550,262 |
| Accrued payroll and benefits | 4,739,974 | 3,537,450 |
| Accrued expenses and other current liabilities | 2,690,473 | 2,567,813 |
| Due to affiliate | <u>1,168,370</u> | <u>788,382</u> |
| Total current liabilities | 9,224,440 | 7,443,907 |
| Long-term debt | <u>12,000,000</u> | <u>12,000,000</u> |
| | <u>21,224,440</u> | <u>19,443,907</u> |
| Net assets | | |
| Unrestricted | 18,605,171 | 11,585,056 |
| Temporarily restricted | <u>17,776,433</u> | <u>18,326,030</u> |
| | <u>36,381,604</u> | <u>29,911,086</u> |
| | <u>\$ 57,606,044</u> | <u>\$ 49,354,993</u> |

See accompanying notes to financial statements.

HOSPICE OF PALM BEACH COUNTY, INC.
STATEMENTS OF OPERATIONS AND CHANGES IN NET ASSETS
Years ended September 30, 2009 and 2008

| | <u>2009</u> | <u>2008</u> |
|--|----------------------|----------------------|
| Unrestricted net assets | | |
| Revenues and other support | | |
| Net patient service revenues | \$ 82,712,530 | \$ 77,963,580 |
| Resale of donated merchandise | 1,169,442 | 1,314,825 |
| Contributions, memorials, and bequests | - | 570,179 |
| Grants from HPBC Foundation | 4,581,708 | 4,888,004 |
| Net assets released from restriction for use in operations | <u>383,996</u> | <u>334,462</u> |
| | 88,847,676 | 85,071,050 |
| Expenses | | |
| Payroll and related expenses | 50,822,060 | 52,001,051 |
| Patient related expenses | 15,113,534 | 14,044,924 |
| Occupancy and equipment expenses | 11,928,980 | 12,064,003 |
| Other operating expenses | <u>3,881,284</u> | <u>3,583,470</u> |
| | <u>81,745,858</u> | <u>81,693,448</u> |
| Change in unrestricted net assets from operations | 7,101,818 | 3,377,602 |
| Nonoperating expenses | | |
| Other non operating expenses | (68,391) | (287,378) |
| Loss on termination of projects in progress | <u>(13,312)</u> | <u>(367,776)</u> |
| | <u>(81,703)</u> | <u>(655,154)</u> |
| Change in unrestricted net assets | 7,020,115 | 2,722,448 |
| Temporarily restricted net assets | | |
| Grants and contributions | 619,380 | 335,381 |
| Change in interest in net assets of HFPBC | (784,981) | (2,604,437) |
| Net assets released from restrictions | <u>(383,996)</u> | <u>(334,462)</u> |
| Decrease in temporarily restricted net assets | <u>(549,597)</u> | <u>(2,603,518)</u> |
| Change in net assets | 6,470,518 | 118,930 |
| Net assets at beginning of year | <u>29,911,086</u> | <u>29,792,156</u> |
| Net assets at end of year | <u>\$ 36,381,604</u> | <u>\$ 29,911,086</u> |

See accompanying notes to financial statements.

HOSPICE OF PALM BEACH COUNTY, INC.
 STATEMENTS OF CASH FLOWS
 Years ended September 30, 2009 and 2008

| | <u>2009</u> | <u>2008</u> |
|---|---------------------|---------------------|
| Cash flows from operating activities | | |
| Change in net assets | \$ 6,470,518 | \$ 118,930 |
| Adjustments to reconcile change in net assets to net cash from operating activities | | |
| Depreciation and amortization | 1,672,535 | 1,776,996 |
| Loss on termination of projects in progress | 13,312 | 367,776 |
| Provision for uncollectible accounts | 2,213,714 | 1,891,224 |
| Change in interest in net assets of HFPBC | 784,981 | 2,604,437 |
| Changes in assets and liabilities | | |
| Patient accounts receivable | (3,557,013) | (2,795,567) |
| Other current assets | (49,985) | 619,145 |
| Accounts payable | 75,361 | (152,138) |
| Accrued payroll and benefits | 1,202,524 | (37,479) |
| Accrued expenses and other current liabilities | 122,660 | 163,954 |
| Due to/ from affiliates | <u>(3,752,385)</u> | <u>(518,233)</u> |
| Net cash from operating activities | 5,196,222 | 4,039,045 |
| Cash flows from investing activities | | |
| Temporary investments held by affiliate | 2,500,000 | (2,500,000) |
| Purchases of property and equipment | (2,573,144) | (3,593,871) |
| Purchase of investments | <u>(500,000)</u> | <u>-</u> |
| Net cash from investing activities | <u>(573,144)</u> | <u>(6,093,871)</u> |
| Net change in cash and cash equivalents | 4,623,078 | (2,054,826) |
| Cash and cash equivalents at beginning of year | <u>1,417,275</u> | <u>3,472,101</u> |
| Cash and cash equivalents at end of year | <u>\$ 6,040,353</u> | <u>\$ 1,417,275</u> |
| Supplemental disclosures of cash flow information | | |
| Cash paid for interest | \$ 148,133 | \$ 251,684 |

See accompanying notes to financial statements.

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 1 - NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations: Hospice of Palm Beach County, Inc. ("HPBC") is a non-stock, not-for-profit corporation organized in Florida. HPBC is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code and is exempt from federal income taxes on related income pursuant to Section 501(a) of the Code.

HPBC provides a coordinated, comprehensive program including physical, psychosocial, spiritual, music, and bereavement support to terminally ill patients and their families in Palm Beach County, Florida.

Affiliated Entities: HPBC's sole member is Spectrum Health, Inc. ("Spectrum"), a non-stock, not-for-profit corporation organized in Florida. Spectrum is also a holding company (and sole member) for the following affiliates:

- The Medical Store of Palm Beach County, Inc. ("TMS")
- Spectrum Healthcare Foundation, Inc. d/b/a Hospice of Palm Beach County Foundation ("HPBC Foundation")
- Hospice Partners On Call, Inc. ("HPOC"), effective October 1, 2008

Collectively, HPBC, TMS, HPBC Foundation, and HPOC are referred to as the Spectrum Affiliates.

Basis of Presentation: The financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP").

Financial Statement Presentation: The financial statements report the changes in and totals of each net asset class based on the existence of donor restrictions, as applicable. Net assets are classified as unrestricted, temporarily restricted, or permanently restricted and are detailed as follows:

Unrestricted net assets represent the part of the net assets of HPBC that is neither permanently restricted nor temporarily restricted by donor-imposed stipulations.

Temporarily restricted net assets represent the part of the net assets of HPBC resulting from contributions and other inflows of assets whose use by HPBC is limited by donor-imposed stipulations that either expire by the passage of time or by actions of HPBC. For the years ended September 30, 2009 and 2008, the temporarily restricted net assets are primarily restricted for patient-related care and therapeutic activities, in addition to the interest in net assets of Hospice Foundation of Palm Beach County, Inc. ("HFPBC").

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 1 - NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES
(Continued)

Permanently restricted net assets represent the part of the net assets of HPBC resulting from contributions and other inflows of assets whose use by HPBC is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of HPBC. For the years ended September 30, 2009 and 2008, HPBC has no permanently restricted net assets.

Use of Estimates: The preparation of financial statements in conformity with U.S. GAAP 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 reported amounts of revenues and expenses during the reporting period. These estimates and assumptions may change in the near future resulting in different actual results.

Cash and Cash Equivalents: Cash and cash equivalents consist of bank deposits in accounts that are subject to, and which at times may be in excess of, federally insured amounts. Additionally, for purposes of the statements of cash flows, HPBC considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. In October 2008, management entered into an overnight sweep arrangement whereby all cash is moved daily into a treasury-only money market fund.

Temporary Investments Held by Affiliate: Temporary investments held by affiliate represents an amount due from HPBC Foundation. This amount was moved from HPBC's operating cash in September 2008 to a treasury-only money market fund previously established by HPBC Foundation. After HPBC established its overnight sweep arrangement in October 2008, the amount invested through affiliate was repaid to HPBC.

Accounts Receivable: The accounts receivable balance represents the unpaid amounts billed to patients and third-party payors. Contractual adjustments, discounts, and an allowance for uncollectible accounts are recorded to report receivables at net realizable value. Past due receivables are determined based on contractual terms. HPBC does not accrue interest on any of its accounts receivable.

Allowance for Uncollectible Accounts: The allowance for uncollectible accounts is determined by management based on HPBC's historical losses, specific patient circumstances, and general economic conditions. Periodically, management reviews accounts receivable and adjusts the allowance based on current circumstances and charges off uncollectible receivables when all attempts to collect have failed in accordance with the Organization's collection policy. Management believes the allowance of \$1,068,575 and \$766,090 as of September 30, 2009 and 2008, is adequate to cover potential losses from uncollectible accounts.

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 1 - NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES
(Continued)

Investments: Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair value based on quoted market prices or dealer quotes in the balance sheets. These investments are initially recorded at cost if they were purchased or at their fair market value on the date of the gift if they were received as a donation. Unrealized gains and losses resulting from year-end adjustments are included in the statements of operations and changes in net assets.

Property and Equipment: Property and equipment are stated at cost or, if donated to HPBC, at fair market value on the date of acquisition. Additions and improvements over \$5,000 are capitalized; expenditures for routine maintenance are charged to operations. Depreciation is provided over the estimated useful lives of the various classes of assets which range from three to thirty years and is computed on the straight-line method. All leasehold improvements are amortized over the shorter of the lease term or the estimated useful life of the asset.

Gifts of long-lived assets such as land, buildings, and equipment are reported as unrestricted support unless explicit donor stipulations specify how the donated 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 and other assets that must be used to acquire long-lived assets are reported as temporarily restricted support. Absent explicit donor stipulations about how long-lived assets must be maintained, expirations of donor restrictions are reported when the donated or acquired long-lived assets are placed in service.

The cost of property and equipment sold or otherwise disposed of and the accumulated depreciation applicable thereto are eliminated from the accounts, and any resulting gain or loss is reflected in the financial statements in the period of disposition.

Deferred Financing Costs: Costs associated with the issuance of the bonds have been deferred and are being amortized on the straight-line method, which approximates the effective interest method, over the life of the related debt.

Net Patient Service Revenues: Net patient service revenues are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered.

Hospice organizations are subject to two specific payment limit caps under the Medicare program. One limit relates to inpatient care days that exceed 20% of the total days of hospice care provided for the year. HPBC did not exceed the 20% cap related to inpatient days in 2009 or 2008. The second limit relates to an aggregate Medicare reimbursement cap calculated by the Medicare fiscal intermediary. HPBC did not exceed the Medicare cap for the years ended September 30, 2009 or 2008.

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 1 - NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES
(Continued)

Charity Care: HPBC provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because HPBC does not expect payment, charges are not included in the net patient service revenues. Charity care is measured using HPBC's established rates and amounted to \$1,397,255 in 2009 and \$1,487,856 in 2008.

Resale of Donated Merchandise: HPBC operates resale shops that sell primarily donated merchandise. The fair value of the donated merchandise sold approximates the revenue generated from its sale.

Contributions: Contributions received and unconditional promises to give are recorded as unrestricted, temporarily restricted, or permanently restricted revenue depending on the existence of donor restrictions and the nature of such restrictions, if they exist. Conditional promises to give are recognized in the statements of operations and changes in net assets only when the conditions on which they depend are substantially met and the promises become unconditional.

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of operations and changes in net assets as net assets released from restrictions.

Donor restricted gifts that are received for which their restricted purpose is met during the same year are initially recorded as temporarily restricted net assets and then reported as net assets released from restrictions and reclassified as unrestricted net assets.

Effective December 1, 2007, HPBC Foundation began actively soliciting contributions on behalf of the Spectrum Affiliates, including HPBC. Since that date, donations to HPBC or the other Spectrum Affiliates have been recorded by HPBC Foundation and are reported in HPBC Foundation's financial statements.

Special Events: The following amounts relate to special events that are on-going and major activities of HPBC.

| | <u>2008</u> |
|--------------|-------------------|
| Revenue | \$ 157,844 |
| Expense | <u>48,981</u> |
| Net proceeds | <u>\$ 108,863</u> |

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 1 - NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES
(Continued)

For the year ended September 30, 2008, revenue is included in contributions, memorials, and bequests, and expenses are included in operating expenses in the statements of operations and changes in net assets. Special events for the year ended September 30, 2009, were conducted by and reported in HPBC Foundation's financial statements.

Fair Value of Financial Instruments: HPBC's carrying amount for its financial instruments, which include cash, accounts receivable, interest in net assets of HFPBC, investments, accounts payable, and long-term debt, approximates fair value.

Adoption of New Accounting Policy: In 2006, the Financial Accounting Standards Board ("FASB") issued new guidance on fair value measurements of financial instruments. This guidance defines fair value, provides enhanced guidance for using fair value to measure assets and liabilities under current U.S. GAAP standards, and expands the disclosure of the methods used and the effect of fair value measurements on earnings. This guidance is effective for financial statements issued for fiscal years beginning after November 15, 2007. Accordingly, HPBC adopted applicable portions of this guidance for the year ended September 30, 2009.

Subsequent Events: Management has performed an analysis of the activities and transactions subsequent to September 30, 2009 to determine the need for any adjustments to and/or disclosures within the audited financial statements for the year ended September 30, 2009. Management has performed their analysis through the date of this report.

Income Taxes: HPBC is exempt from income taxes on income from related activities under Section 501(c)(3) of the U.S. Internal Revenue Code and corresponding state tax law. Accordingly, no provision has been made for federal or state income taxes.

Reclassifications: Certain reclassifications have been made to present last year's financial statements on a basis comparable to the current year's financial statements. These reclassifications had no effect on total net assets or the change in net assets.

NOTE 2 - ACCOUNTS RECEIVABLE

HPBC provides hospice and palliative care services, medicine, medical equipment, and medical supplies to patients, and does not require collateral or other security in providing these services. However, HPBC routinely obtains assignment of benefits payable under patients' health care insurance programs, plans, or policies. Since over 90% of HPBC's revenues come from Medicare and Medicaid, credit risk with respect to accounts receivable is limited. At September 30, 2009 and 2008, approximately 80% and 84%, respectively, of HPBC's accounts receivable are from Medicare and Medicaid.

HOSPICE OF PALM BEACH COUNTY, INC.
 NOTES TO FINANCIAL STATEMENTS
 September 30, 2009 and 2008

NOTE 2 - ACCOUNTS RECEIVABLE (Continued)

At September 30, accounts receivable from third-party payors consists of the following:

| | <u>2009</u> | <u>2008</u> |
|---------------------------------------|---------------------|---------------------|
| Medicare | \$ 3,250,913 | \$ 2,712,170 |
| Medicaid | 4,159,601 | 3,670,952 |
| Private insurance | 1,750,152 | 1,160,148 |
| Patients and others | <u>103,878</u> | <u>75,490</u> |
| | 9,264,544 | 7,618,760 |
| Less: Allowance for doubtful accounts | <u>(1,068,575)</u> | <u>(766,090)</u> |
| | <u>\$ 8,195,969</u> | <u>\$ 6,852,670</u> |

NOTE 3 - PROPERTY AND EQUIPMENT

HPBC's property and equipment at September 30, 2009 and 2008 is as follows:

| | <u>2009</u> | <u>2008</u> |
|--------------------------------|----------------------|----------------------|
| Land and improvements | \$ 2,191,915 | \$ 1,191,915 |
| Buildings and improvements | 18,181,674 | 16,668,021 |
| Leasehold improvements | 1,465,769 | 1,465,769 |
| Furniture and equipment | 4,643,297 | 4,297,796 |
| Technology costs | 5,852,858 | 5,060,851 |
| Vehicles | 125,425 | 115,425 |
| Projects in progress | <u>1,145,538</u> | <u>2,276,976</u> |
| | 33,606,476 | 31,076,753 |
| Less: Accumulated depreciation | <u>(13,020,973)</u> | <u>(11,386,455)</u> |
| | <u>\$ 20,585,503</u> | <u>\$ 19,690,298</u> |

Technology costs include the costs incurred to develop HPBC's proprietary patient services and billing software as well as purchased software and hardware. Capitalized software and hardware costs include amounts paid to vendors, fees to third parties related to implementation, and internal costs of HPBC's personnel directly related to implementation.

Depreciation expense for the years ended September 30, 2009 and 2008 was \$1,664,627 and \$1,761,187, respectively.

Projects in progress at September 30, 2009 and 2008 primarily relate to inpatient unit renovations and software implementation projects.

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 3 - PROPERTY AND EQUIPMENT (Continued)

During the years ended September 30, 2009 and 2008, management abandoned plans to build a new administrative facility and terminated certain software implementation projects. Costs for these projects had previously been recorded as projects in progress. Upon the decision to discontinue the projects, accumulated costs of \$13,312 and \$367,776, respectively, were charged to loss on termination of projects in progress and reported as such in the statements of operations and changes in net assets.

NOTE 4 - LONG-TERM DEBT

In December 2001, HPBC entered into a loan agreement with Palm Beach County, Florida relating to the issuance of \$12,000,000 in variable rate demand revenue bonds (Series 2001). The bonds were issued in connection with a project to expand HPBC's Gerstenberg Center facility. The entire bond issue is due October 1, 2031 and bears interest at prevailing market rates determined by the remarketing agent, reset every seven (7) days (effective average interest rates of 0.87% and 2.43% for fiscal years 2009 and 2008, respectively). In the event the remarketing agent is unable to remarket the bonds, they become a demand note under the letter of credit and require repayment under the terms of the letter of credit.

The Series 2001 Bonds are secured by an irrevocable transferable letter of credit issued by The Northern Trust Company. The letter of credit expires September 2010, and contains a guarantee from Spectrum and HPBC Foundation, both related parties.

The bonds contain covenants relating to ongoing operations and tax-exempt status. HPBC is in compliance with all financial covenants.

Interest expense was \$108,158 and \$291,659 for the years ended, September 30, 2009 and 2008, respectively.

NOTE 5 - RELATED PARTY TRANSACTIONS

Expenses incurred by HPBC in 2009 and 2008 for management services provided by Spectrum were \$1,214,999 and \$693,000, respectively.

TMS provides durable medical equipment and medical supplies to HPBC, other health care providers, and to individuals through contracts and agreements with Medicare, Medicaid, and commercial insurance companies. TMS also sells and services rehabilitation equipment. The majority of the billings of TMS are to HPBC. The billings to HPBC in 2009 and 2008 were \$2,348,721 and \$2,149,747, respectively.

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 5 - RELATED PARTY TRANSACTIONS (Continued)

HPBC Foundation provides fundraising, investment management, and other support services to Spectrum and its affiliates. HPBC Foundation provides grants in support of various patient care and supportive care programs, as well as other strategic initiatives. HPBC received grants from HPBC Foundation in the amounts of \$4,610,083 and \$4,888,004 for 2009 and 2008, respectively.

HPOC is a triage call center service that provides seamless telephone access to hospice trained professionals after hours. This service allows hospices that do not have a centralized, clinical based call center with triage capability to meet the evening and weekend needs of their patients and families. Prior to the formation of HPOC, effective October 1, 2008, the triage call center service was a department within HPBC, serving HPBC, TMS, and a limited number of beta site customers. Expenses incurred by HPBC in the year ended September 30, 2009 for call center services provided by HPOC was \$882,850.

As of September 30, 2009, HPBC is owed \$364,504 from Spectrum, \$377,914 from HPOC, and \$4,613,459 from HPBC Foundation, and owes \$1,168,370 to TMS. As of September 30, 2008, HPBC is owed \$252,921 from Spectrum and \$970,583 from HPBC Foundation, and owes \$788,382 to TMS.

NOTE 6 - PATIENT SERVICE REVENUES

Patient service revenues for the years ended September 30 are as follows:

| | <u>2009</u> | <u>2008</u> |
|---|----------------------|----------------------|
| Government sources | | |
| Medicare | \$ 76,140,298 | \$ 70,956,253 |
| Medicaid | <u>4,762,931</u> | <u>4,785,570</u> |
| | 80,903,229 | 75,741,823 |
| Other sources | | |
| Insurance, private pay, and other third-parties | <u>3,995,226</u> | <u>4,112,982</u> |
| | 84,898,455 | 79,854,805 |
| Less: Allowances and charity care | <u>(2,185,925)</u> | <u>(1,891,225)</u> |
| | <u>\$ 82,712,530</u> | <u>\$ 77,963,580</u> |

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 7 - PENSION PLAN

HPBC maintains a non-contributory defined contribution pension plan covering substantially all of its full-time employees. The amounts contributed to the plan are five percent of eligible employees' gross wages. Total pension expense for 2009 and 2008 was \$1,680,685 and \$1,538,673, respectively.

NOTE 8 - LEASES

HPBC leases various patient care facilities, resale shops, and office space under operating leases that extend through December, 2014. Total rent expense, included in occupancy and equipment expenses, amounted to \$5,050,969 in 2009 and \$5,027,874 in 2008.

Future minimum payments under the operating leases consist of the following at September 30, 2009:

| | |
|------------|----------------------|
| 2010 | \$ 4,347,704 |
| 2011 | 2,845,772 |
| 2012 | 2,463,170 |
| 2013 | 1,173,126 |
| 2014 | 1,166,244 |
| Thereafter | <u>80,808</u> |
| | <u>\$ 12,076,824</u> |

NOTE 9 - DONATED SERVICES

HPBC has estimated that during 2009 and 2008 dedicated volunteers have donated hours of service as follows:

| | <u>2009</u> | <u>2008</u> |
|-----------------------------|---------------|---------------|
| Patient care services | 10,749 | 10,306 |
| Clerical and other services | <u>31,415</u> | <u>33,593</u> |
| Total hours of service | <u>42,164</u> | <u>43,899</u> |

Because the above donated services do not meet the recognition criteria of U.S. GAAP, their estimated values have not been recognized in the statements of operations and changes in net assets.

HOSPICE OF PALM BEACH COUNTY, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2009 and 2008

NOTE 10 - FUNCTIONAL EXPENSES

Expenses related to providing hospice and palliative care services as well as general and administrative, fundraising, and resale activities for the years ended September 30 are as follows:

| | <u>2009</u> | <u>2008</u> |
|-----------------------------|----------------------|----------------------|
| Hospice and palliative care | \$ 69,840,674 | \$ 71,005,075 |
| General and administrative | 11,068,057 | 9,746,645 |
| Fundraising | - | 87,789 |
| Resale | <u>905,518</u> | <u>1,141,317</u> |
| | <u>\$ 81,814,249</u> | <u>\$ 81,980,826</u> |

NOTE 11 - SUPPORT ORGANIZATION

HFPBC, an independently managed non-profit corporation, was established in 1985 to exclusively support the programs, services, activities, interest, and organization of HPBC. U.S. GAAP requires HPBC to recognize as an asset its interest in the net assets of HFPBC, and to reflect in its changes in net assets the changes in the net assets of HFPBC. Net assets held by HFPBC as of September 30, 2009 and 2008 amounted to \$15,511,714 and \$16,296,695, respectively.

During 2009 and 2008, HFPBC made grants to HPBC totaling \$560,000 and \$325,000, respectively, to provide funding for the following activities:

| | <u>2009</u> | <u>2008</u> |
|--|-------------------|-------------------|
| Integrative Therapies | \$ 200,000 | \$ 200,000 |
| Palliative Medicine Fellowship Grant | - | 125,000 |
| John J. Brogan Bereavement Center Fund | 150,000 | - |
| Palliative Medicine Fellowship Grant | 140,000 | - |
| Jewish Hospice Programming | 50,000 | - |
| End-of-Life Doulas Program | <u>20,000</u> | <u>-</u> |
| | <u>\$ 560,000</u> | <u>\$ 325,000</u> |

These grants were initially recognized as temporarily restricted net assets, and portions have been reclassified to unrestricted net assets upon meeting their purpose requirements.

HOSPICE OF PALM BEACH COUNTY, INC.
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NOTE 12 - FAIR VALUE MEASUREMENTS OF FINANCIAL INSTRUMENTS

In 2006, the FASB issued new guidance on fair value measurements of financial instruments. This guidance defines fair value as the price that would be received for an asset or paid to transfer a liability (an exit price) in HPBC's principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

In determining fair value, management uses various valuation approaches. FASB utilizes a fair value hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Unobservable inputs reflect HPBC's assumptions about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The fair value hierarchy is categorized into three levels based on the inputs as follows:

Level 1: Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date. The fair values of debt and equity investments that are readily marketable are determined by obtaining quoted prices on nationally recognized securities exchanges.

Level 2: Significant other observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data. Management utilizes information such as historical and current performance of the underlying funds and financial trend analysis with respect to the overall fund compared to benchmark performance ratios.

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability. The interest in the net assets of HFPBC is largely composed of underlying investments that have observable inputs and market activity allowing for pricing based on the market prices of the items in the investments. Another portion of HFPBC's investments consist of alternative investments (hedge funds) that have observable inputs and market activity allowing for pricing based on the underlying market prices of the items in the investments, utilizing the market approach and income approach valuation techniques. Management utilizes information such as historical and current performance of the underlying funds and financial trend analysis with respect to the interest compared to benchmark performance ratios.

HOSPICE OF PALM BEACH COUNTY, INC.
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NOTE 12 - FAIR VALUE MEASUREMENTS OF FINANCIAL INSTRUMENTS (Continued)

Management has determined that the adoption of fair value guidance has no material impact on the valuation of the HPBC's assets and liabilities, but does require additional disclosure about fair value measurements. In many cases, a valuation technique used to measure fair value includes inputs from multiple levels of the fair value hierarchy. The lowest level of significant input determines the placement of the entire fair value measurement in the hierarchy.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

| | <u>Fair Value Measurements at September 30, 2009</u> | | | |
|---------------------------------|--|-------------------|----------------------|----------------------|
| | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> | <u>Total</u> |
| Investments | | | | |
| Cash and cash equivalents | \$ 297,852 | \$ - | \$ - | \$ 297,852 |
| Bonds | <u>-</u> | <u>202,148</u> | <u>-</u> | <u>202,148</u> |
| Total investments | 297,852 | 202,148 | - | 500,000 |
| Interest in net assets of HFPBC | <u>-</u> | <u>-</u> | <u>15,511,714</u> | <u>15,511,714</u> |
| Total assets | <u>\$ 297,852</u> | <u>\$ 202,148</u> | <u>\$ 15,511,714</u> | <u>\$ 16,011,714</u> |

A reconciliation of beginning and ending balances for HPBC's fair value measurements using Level 3 inputs is as follows:

| <u>Level 3 Instruments</u> | Interest in net assets of <u>HFPBC</u> |
|------------------------------|--|
| Assets at September 30, 2008 | \$ 16,296,695 |
| Unrealized losses | <u>(784,981)</u> |
| Assets at September 30, 2009 | <u>\$ 15,511,714</u> |

All gains and losses related to assets with level 3 inputs are unrealized and pertain to changes in interest in net assets of HFPBC in the year ended September 30, 2009. They are disclosed as such in HPBC's statements of operations and changes in net assets.