

LANA‘I COMMUNITY HEALTH CENTER AND SUBSIDIARY

(A Hawaii Nonprofit Corporation)

CONSOLIDATING AUDITED FINANCIAL STATEMENTS
(With Independent Auditor’s Report)

FOR THE YEAR ENDED DECEMBER 31, 2018
(With comparative totals for the year ended December 31, 2017)

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Lana'i Community Health Center
Lana'i City, Hawai'i 96763

Report on the Financial Statements

We have audited the accompanying consolidating financial statements of Lana'i Community Health Center and Subsidiary, which comprise the consolidating statement of financial position as of December 31, 2018, and the related consolidating statements of activities and changes in net assets, functional expenses and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Consolidating 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

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Opinion

In our opinion, the consolidating financial statements referred to above present fairly, in all material respects, the consolidating financial position of Lana'i Community Health Center and Subsidiary as of December 31, 2018, and the consolidating statement of activities and 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.

Other Matters

The prior year summarized comparative information has been derived from Lana'i Community Health Center's 2017 financial statements and in our report dated March 10, 2018. We expressed an unmodified opinion on the financial statements.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The Schedule of Expenditures of Federal Awards on page 14, as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Schedule of Expenditures of Federal Awards is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated April 8, 2019 on our consideration of Lana'i Community Health Center's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Lana'i Community Health Center's internal control over financial reporting and compliance.

Carbonaro CPAs & Management Group

April 8, 2019
Wailuku, Hawai'i

LANA'I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Consolidating Statement of Financial Position

As of December 31, 2018

(With comparative totals as of December 31, 2017)

	ASSETS			
	Community Health Center	LCHC Holdings	2018 Totals	2017 Totals
CURRENT ASSETS				
Cash and Cash Equivalents (Notes 2, 13 and 14)	\$ 695,837	\$ 261,456	\$ 957,293	\$ 798,557
Certificates of Deposit (Note 11)	105,641	-	105,641	104,337
Grants Receivable (Notes 2 and 14)	50,641	-	50,641	39,245
Patient Receivables (Notes 2 and 14)	370,339	-	370,339	286,675
Allowance for Doubtful Accounts (Notes 2 and 14)	(150,062)	-	(150,062)	(114,764)
Prepaid Expenses	52,324	-	52,324	44,783
Other Receivables (Note 2)	18,757	-	18,757	32,383
Total Current Assets	1,143,477	261,456	1,404,933	1,191,216
PROPERTY AND EQUIPMENT (Note 2)				
Land	313,000	250,000	563,000	563,000
Equipment and Furnishings	577,565	-	577,565	577,565
Vehicles	36,523	-	36,523	26,523
Software and Hardware	83,284	-	83,284	83,284
Facilities and Improvements	864,455	6,498,361	7,362,816	7,362,816
	1,874,827	6,748,361	8,623,188	8,613,188
Accumulated Depreciation	(343,441)	(688,724)	(1,032,165)	(676,872)
Net Property and Equipment	1,531,386	6,059,637	7,591,023	7,936,316
OTHER ASSETS				
Notes Receivable (Note 12)	5,384,200	-	5,384,200	5,384,200
Loan Costs (Net of Accumulated Amortization of \$58,935 and \$40,801, Respectively) (Note 13)	-	485,077	485,077	503,211
Construction in Progress (Note 15)	98,620	-	98,620	-
Inventory (Note 2)	46,201	-	46,201	32,600
Total Other Assets	5,529,021	485,077	6,014,098	5,920,011
TOTAL ASSETS	\$ 8,203,884	\$ 6,806,170	\$ 15,010,054	\$ 15,047,543
LIABILITIES & NET ASSETS				
CURRENT LIABILITIES				
Accounts Payable (Note 14)	\$ 107,815	\$ 28,632	\$ 136,447	\$ 122,183
Accrued Expenses (Note 14)	227,267	-	227,267	172,529
Deferred Revenue (Notes 5 and 14)	238,886	-	238,886	290,204
Current Portion of Long Term Debt (Note 13)	23,762	-	23,762	848,735
Total Current Liabilities	597,730	28,632	626,362	1,433,651
NON CURRENT LIABILITIES				
Long-term Debt (Note 13)	954,133	7,800,000	8,754,133	7,800,000
TOTAL LIABILITIES	1,551,863	7,828,632	9,380,495	9,233,651
NET ASSETS (Note 3)				
Net Assets Without Donor Restrictions	6,565,910	(1,022,462)	5,543,448	5,646,175
Net Assets With Donor Restrictions	86,111	-	86,111	167,717
Total Net Assets	6,652,021	(1,022,462)	5,629,559	5,813,892
TOTAL LIABILITIES & NET ASSETS	\$ 8,203,884	\$ 6,806,170	\$ 15,010,054	\$ 15,047,543

The accompanying notes are an integral part of these consolidating financial statements.

LANA'I COMMUNITY HEALTH CENTER AND SUBSIDIARY
Consolidating Statement of Activities and Changes in Net Assets
For the Year Ended December 31, 2018
(With comparative totals for the Year Ended December 31, 2017)

	<u>Lana'i Community Health Center</u>						
	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	Total	LCHC Holdings	Eliminations	2018 Totals	2017 Totals
PUBLIC SUPPORT AND REVENUE							
Federal Grant Income	\$ 2,165,518	\$ -	\$ 2,165,518	\$ -	\$ -	\$ 2,165,518	\$ 1,855,495
State and Local Grant Income	590,296	164,000	754,296	-	-	754,296	591,692
Clinic Revenues	1,410,611	-	1,410,611	-	-	1,410,611	1,348,584
Miscellaneous	205,197	-	205,197	-	(63,561)	141,636	36,121
In-kind Revenue (Note 9)	93,977	-	93,977	-	-	93,977	40,446
Contributions	19,907	-	19,907	-	-	19,907	18,504
Rental Income	-	-	-	74,193	(74,193)	-	-
Net Assets Released from Restrictions	245,606	(245,606)	-	-	-	-	-
Total Public Support and Revenue	<u>4,731,112</u>	<u>(81,606)</u>	<u>4,649,506</u>	<u>74,193</u>	<u>(137,754)</u>	<u>4,585,945</u>	<u>3,890,842</u>
EXPENSES							
Program Services	2,735,848	-	2,735,848	359,255	(137,754)	2,957,349	2,919,493
Management and General	1,681,998	-	1,681,998	-	-	1,681,998	1,045,681
Fundraising	130,931	-	130,931	-	-	130,931	139,839
Total Expenses	<u>4,548,777</u>	<u>-</u>	<u>4,548,777</u>	<u>359,255</u>	<u>(137,754)</u>	<u>4,770,278</u>	<u>4,105,013</u>
CHANGE IN NET ASSETS	\$ 182,335	\$ (81,606)	\$ 100,729	\$ (285,062)	\$ -	\$ (184,333)	\$ (214,171)
Net Assets, Beginning of Year	6,383,575	167,717	6,551,292	(737,400)	-	5,813,892	6,028,063
Net Assets, End of Year	<u>\$ 6,565,910</u>	<u>\$ 86,111</u>	<u>\$ 6,652,021</u>	<u>\$ (1,022,462)</u>	<u>\$ -</u>	<u>\$ 5,629,559</u>	<u>\$ 5,813,892</u>

The accompanying notes are an integral part of these consolidating financial statements.

LANA'I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Consolidating Statement of Functional Expenses

For the Year Ended December 31, 2018

(With comparative totals for the Year Ended December 31, 2017)

	Lana'i Community Health Center				LCHC Holdings	Eliminations	2018 Totals	2017 Totals
	Program Services	Management and General	Fundraising	Total				
Classification of Expenses:								
Salaries and Wages and Taxes	\$ 1,690,587	\$ 629,201	\$ 122,094	\$ 2,441,882	\$ -	\$ -	\$ 2,441,882	\$ 2,040,734
Professional Fees	323,461	435,499	-	758,960	-	-	758,960	672,356
Depreciation and Amortization	-	138,681	-	138,681	234,746	-	373,427	363,941
Supplies	193,449	17,613	-	211,062	-	-	211,062	250,025
Travel	43,549	160,043	-	203,592	-	-	203,592	107,620
Miscellaneous	84,674	21,820	-	106,494	80	-	106,574	79,276
In-kind Donations (Note 9)	-	93,977	-	93,977	-	-	93,977	40,446
Interest	-	23,779	-	23,779	114,527	(53,659)	84,647	104,444
Bad Debt	-	79,705	-	79,705	-	-	79,705	93,170
Non-Capitalized Equipment and Fixtures	52,480	4,525	-	57,005	-	-	57,005	20,295
Utilities	53,308	-	2,806	56,114	-	-	56,114	53,730
Recruiting	53,502	-	-	53,502	-	-	53,502	36,950
Telephone	48,034	-	-	48,034	-	-	48,034	43,617
Insurance	-	44,771	-	44,771	-	-	44,771	31,239
Rent	107,186	-	5,641	112,827	-	(74,193)	38,634	26,347
Membership Dues and Fees	13,474	24,980	-	38,454	-	-	38,454	32,936
Molokai Drugs Expense	33,141	-	-	33,141	-	-	33,141	57,047
Printing, Publications and Advertising	21,143	-	-	21,143	9,902	(9,902)	21,143	20,112
General Maintenance	14,541	-	-	14,541	-	-	14,541	13,014
Postage	-	7,404	390	7,794	-	-	7,794	15,010
Automobile Expense	3,319	-	-	3,319	-	-	3,319	2,704
	<u>\$ 2,735,848</u>	<u>\$ 1,681,998</u>	<u>\$ 130,931</u>	<u>\$ 4,548,777</u>	<u>\$ 359,255</u>	<u>\$ (137,754)</u>	<u>\$ 4,770,278</u>	<u>\$ 4,105,013</u>

The accompanying notes are an integral part of these consolidating financial statements.

LANA'I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Consolidating Statement of Cash Flows

For the Year Ended December 31, 2018

(With comparative totals for the Year Ended December 31, 2017)

	Lana'i Community Health Center			LCHC Holdings	Eliminations	2018 Totals	2017 Totals
CASH FLOWS FROM OPERATING ACTIVITIES							
Cash From Grants	\$ 2,857,100	\$ -	\$ -	\$ -	\$ 2,857,100	\$ 2,597,762	
Cash From Clinic Revenue	1,375,871	-	-	-	1,375,871	1,350,208	
Cash From Contributions, Rent and Miscellaneous	225,104	74,193	(137,754)		161,543	54,625	
Cash Paid for Interest	(23,779)	(114,527)	53,659		(84,647)	(104,444)	
Cash Paid to Employees and Vendors	(4,244,480)	(9,982)	84,095		(4,170,367)	(3,598,268)	
Cash Provided (Used) by Operating Activities (Note 8)	189,816	(50,316)	-		139,500	299,883	
CASH FLOWS FROM INVESTING ACTIVITIES							
Purchases of Property and Equipment	(10,000)	-	-		(10,000)	(62,123)	
Purchases of Construction in Progress	(98,620)	-	-		(98,620)	-	
Net Redemption (Purchase) of Certificates of Deposits	(1,304)	-	-		(1,304)	73,524	
Cash Provided (Used) by Investing Activities	(109,924)	-	-		(109,924)	11,401	
CASH FLOWS FROM FINANCING ACTIVITIES							
Proceeds from Borrowing on Long-term Debt	184,131	-	-		184,131	-	
Payments on Long-term Debt	(54,971)	-	-		(54,971)	(83,184)	
Cash Provided (Used) by Investing Activities	129,160	-	-		129,160	(83,184)	
Net (Decrease) Increase in Cash for the Year	209,052	(50,316)	-		158,736	228,100	
CASH BALANCE, BEGINNING OF YEAR	486,785	311,772	-		798,557	570,457	
CASH BALANCE, END OF YEAR	\$ 695,837	\$ 261,456	\$ -		\$ 957,293	\$ 798,557	
SUPPLEMENTAL CASH FLOW							
Non-Cash Financing Activities							
Long-term Debt Refinanced	\$ 815,869	\$ -	\$ -		\$ 815,869	\$ -	

The accompanying notes are an integral part of these consolidating financial statements.

LANA‘I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Notes to the Financial Statements December 31, 2018

Note 1. ORGANIZATION

Lana‘i Women’s Center, Inc. (the Organization) is a nonprofit Organization incorporated under the laws of the State of Hawai‘i on November 29, 2004. In 2009 the Center legally changed its name to Lana‘i Community Health Center. The Lana‘i Community Health Center was created to take care of the community of Lana‘i with a focus on their physical, mental, emotional, intellectual and spiritual welfare by enriching and empowering their lives to help them build healthy families in a supportive community. In addition, the Lana‘i Community Health Center has become a Federally Qualified community health center.

LCHC Holdings, Inc. (Holdings) is a nonprofit organization incorporated under the laws of the State of Hawaii that was established on January 21, 2015. The Organization was created solely to hold title to real property, collect income therefrom, and remit the entire amount thereof, less expenses, to Lana‘i Community Health Center, Inc., an organization exempt from federal tax pursuant to section 501(c)(2) of the Internal Revenue Code. The Organization’s major source of income is renting their facility to Lana‘i Community Health Center, Inc.

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Method of Accounting: The Organization and Holdings use the accrual method of accounting for financial statement reporting according to generally accepted accounting principles. Under this method of accounting, revenue is recognized when earned rather than when received and expenses are recognized when incurred rather than when paid.

Basis of Financial Statement Presentation: Lana‘i Community Health Center has conformed with ASC 958-810 “Consolidation” by consolidating the position and activities of LCHC Holdings.

Revenue Recognition: Contributions received are recorded as with or without donor restrictions depending on the existence and/or nature of any donor restrictions (Note 3). Unconditional promises to donate due in the next year are reflected as current promises to give and are recorded at their net realizable value. Grants and other contributions of cash are reported as with donor restrictions if they are received with donor stipulations that limit the use of the donated assets. When the donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, donor restricted net assets are reclassified to without donor restricted net assets and reported in the statement of activities as net assets released from restrictions.

Cash and Cash Equivalents: For the purpose of the statement of cash flows, cash is defined as demand deposits and savings accounts.

Income Taxes: Lana‘i Community Health Center and LCHC Holdings, Inc. are exempt from Federal income taxes under *Section 501(c)(3) and Section 501(c)(2)* of the Internal Revenue Code, respectively, and also from State of Hawaii income taxes under *Section 237-23 (b)* of the Hawaii Revised Statutes.

Uncertain Tax Position: The financial statement effects of a tax position taken or expected to be taken are recognized in the financial statements when it is more likely than not, based on the technical merits, that the position will be sustained upon examination. Interest and penalties, if any, are included in expenses in the statement of activities. As of December 31, 2018, the organizations have analyzed their tax positions and believe that all are more likely than not to be sustained upon examination.

LANA‘I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Notes to the Financial Statements
December 31, 2018

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Organization is subject to routine audits by taxing jurisdictions, however, there are currently no audits for any tax periods in progress. The Organization believes it is no longer subject to income tax examinations for years prior to 2015.

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

Inventory: Inventories are priced using an average cost method for service and sheet metal parts. All other inventories are priced using a first-in, first-out (FIFO) basis.

Advertising: The Organization expenses advertising costs as they are incurred. Total advertising expense was \$13,062 and \$10,365 for the years ended December 31, 2018 and 2017, respectively.

Grants, Patient and Other Receivables: Grants, patient and other receivables represent revenue earned and not yet received. Management reviews the receivables and charges off accounts when they determine they are uncollectable. Management periodically reviews the receivable listing to determine the allowance for doubtful accounts based on historical collection rates, industry standards and the composition of the receivable balance. Management has determined an allowance for doubtful accounts of \$150,062 and \$114,764 at December 31, 2018 and 2017, respectively.

Property and Equipment: The Organization and Holdings capitalize all furniture and equipment with a value of \$5,000 or greater and a useful life of more than one year. Property and equipment are stated at cost or, if donated, at the approximate fair value at the date of donation. Depreciation is computed using the straight-line method over the assets' estimated useful lives.

Note 3. NET ASSETS-NEW ACCOUNTING PRONOUNCEMENT

On August 18, 2016, the FASB issued ASU 2016-14, Not-for-Profit Entities (Topic 958) – *Presentation of Financial Statements of Not-for-Profit Entities*. Lanai Community Health Center and Subsidiary has adjusted the presentation of its financial statements accordingly, applying the changes retrospectively to the comparative period presented. The new standards change the following aspects of the Organization's financial statements:

The temporarily restricted net asset class has been renamed net assets with donor restrictions. The unrestricted net asset class has been renamed net assets without donor restrictions.

LANA‘I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Notes to the Financial Statements
December 31, 2018

Note 3. NET ASSETS-NEW ACCOUNTING PRONOUNCEMENT (CONTINUED)

Net assets, revenue, and support are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

Net assets without donor restrictions include all resources that are not subject to donor-imposed stipulations or contributions with donor-imposed restrictions that are met during the same year as the contribution is made. Net assets without donor restrictions denoted as property and equipment represent equity in such property and equipment.

Net assets with donor restrictions include amounts that the donor subjects to restrictions in perpetuity and amounts subject to legal or donor-imposed stipulations that may or will be met either by actions of the Organization and/or passage of time. Net assets with donor restrictions consist of the following at December 31, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Tobacco Prevention and Control	\$ 46,207	\$ 23,257
Susan G. Komen Hawaii	17,972	-
Jessie Ann Chalmers Charitable Trust	16,548	-
One Touch Glucose Strips	5,384	5,469
Diabetes Prevention	-	75,000
BH Post-Doc Program	-	50,000
BH Direct Services	-	7,957
Equipment and Outreach	-	6,034
	<u>\$ 86,111</u>	<u>\$ 167,717</u>

The changes have the following effect on net assets at December 31, 2017:

<u>Net Asset Class</u>	<u>As Originally Presented</u>	<u>After Adoption of ASU 2016-14</u>
Unrestricted Net Assets	\$ 5,646,175	\$ -
Temporarily Restricted Net Assets	167,717	-
Net Assets Without Donor Restrictions	-	5,646,175
Net Assets With Donor Restrictions	-	167,717
Total Net Assets	<u>\$ 5,813,892</u>	<u>\$ 5,813,892</u>

The financial statements include a statement of Functional Expenses. Functional expenses are allocated to program related and administrative functions. Most expenses are allocated directly to the program or support services benefited. Certain expenses are allocated using a percentage base.

The financial statements include a new disclosure about liquidity and availability of resources (Note 14).

Note 4. CONCENTRATIONS

The Organization receives a substantial amount of its support from the U.S. Department of Health and Human Services. In 2018, Lana‘i Community Health Center received 42% of its revenues from this grantor. The discontinuance of these grants could adversely affect the operations of the Center.

LANA‘I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Notes to the Financial Statements
December 31, 2018

Note 5. DEFERRED REVENUE

Deferred revenue represents funds received from government and foundation contracts which were not yet earned as of year-end. The contracts allow for these funds to be used and thus earned in the subsequent year. The deferred revenue balance was \$238,886 and \$290,204 as of December 31, 2018 and 2017, respectively.

Note 6. SUBSEQUENT EVENTS

In preparing these financial statements, management has evaluated events and transactions for potential recognition or disclosure through April 8, 2019, the date the financial statements were available for use.

Subsequent to year end, the Organization entered into an agreement to purchase a condominium from the Executive Director to house medical staff that assists the Organization. The Organization followed their conflict of interest policy and the Executive Director was not part of the discussion and decision to purchase the property. Total purchase price was \$150,000 and closed in March 2019.

Note 7. LINE OF CREDIT

The Organization has a \$200,000 line of credit with First Hawaiian Bank. The interest rate for the line of credit is First Hawaiian Bank Prime rate plus a 2.25% floating rate. As of December 31, 2018 and 2017 the balance due was \$-0-.

Note 8. RECONCILIATION OF CHANGES IN NET ASSETS WITH NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES

	Lana'i Community Health Center	LCHC Holdings	2018 Totals	2017 Totals
Change in Net Assets	\$ 100,729	\$ (285,062)	\$ (184,333)	\$ (214,171)
Adjustments to Reconcile:				
Add back Depreciation and Amortization Expense	138,681	234,746	373,427	363,941
Add back Bad Debt	79,705	-	79,705	93,170
Change in Grants, Patient and Other Receivables	(125,841)	-	(125,841)	(57,225)
Change in Inventory	(13,601)	-	(13,601)	174
Change in Prepaid Expenses	(7,541)	-	(7,541)	180
Change in Accounts Payable	14,264	-	14,264	(16,540)
Change in Accrued Expenses	54,738	-	54,738	14,100
Change in Deferred Revenue	(51,318)	-	(51,318)	116,254
Net Cash Provided (Used) by Operating Activities	<u>\$ 189,816</u>	<u>\$ (50,316)</u>	<u>\$ 139,500</u>	<u>\$ 299,883</u>

Note 9. DONATED GOODS AND SERVICES

Under FASB ASC 958-605-25-16 “Not-for-Profit Entities, Contributed Services”, contributions of donated services that create or enhance non-financial assets or that require specialized skills, and are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation, are recorded at their fair values in the period received.

LANA‘I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Notes to the Financial Statements December 31, 2018

Note 9. DONATED GOODS AND SERVICES (CONTINUED)

In-Kind Revenue recorded also represents the fair value of many donated items for fundraising and for the ongoing operations of the Organization. These tangible items donated are valued at their estimated fair market value at the time of donation. The Organization received \$93,977 and \$40,446 of donated goods for inventory and other items during the years ended December 31, 2018 and 2017, respectively.

Note 10. NEW MARKET TAX CREDIT PROGRAM

LCHC Holdings, Inc. and Lana‘i Community Health Center participates in a New Markets Tax Credit (NMTC) program. NMTC programs were established as part of the Community Renewal Tax Relief Act of 2000 and the New Markets Tax Credit Extension Act of 2011 extended the program through 2016. The goal of NMTC programs is to spur revitalization efforts of low-income and impoverished communities across the United States and its Territories by providing tax credit incentives to investors in certified community development entities. The tax credit for investors equals 39% of the investment, and investors receive the tax credit over a seven year period. A Community Development Entity (CDE) is required to participate and has the primary mission of providing financing for revitalization projects in low-income communities.

NMTC financing allows organizations such as LCHC Holdings, Inc. to receive low-interest loans or investment capital from CDEs, primarily financial institutions, which will allow their investors to receive tax credits. As a result of participation in the NMTC program, LCHC Holdings, Inc. has obtained the low-interest loan described in Note 13.

Note 11. INVESTMENTS

The Organization has conformed to *FASB’s ASC 820-10-50-1* which establishes a fair value hierarchy for inputs used in measuring fair market 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. Observable inputs are those that market participants would use in pricing the asset or liability based on the best information available in the circumstances. This fair value hierarchy consists of three levels:

- Level 1 inputs consist of unadjusted quoted prices in active markets such as stock exchanges for identical assets and have the highest priority.
- Level 2 inputs consist of significant other observable inputs such as quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset and liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 inputs consist of significant unobservable inputs and include situations where is little, if any, market activity for the investment. The inputs require significant judgment or estimates, such as those associated with discounted cash flow methodologies and appraisals.

Fair values of assets measured on a recurring basis are certificates of deposits totaling \$105,641 and \$104,337 at December 31, 2018 and 2017, respectively, and are measures at Level 1 inputs. There are no liabilities or other assets measured at fair value on a recurring or non-recurring basis.

LANA'I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Notes to the Financial Statements
December 31, 2018

Note 12. NOTE RECEIVABLE

Lana'i Community Health Center participates in the NMTC program described in Note 10 and has loaned \$5,384,200 to Twain Investment Fund 70, LLC. The Note Receivable has a stated interest rate is 1.000% and the loan matures on February 28, 2045. The loan calls for quarterly interest only payments beginning April 10, 2015. Beginning April 10, 2022 quarterly principle and interest payments begin unless the put/call option in Note 13 is exercised. The loan is secured by substantially all assets acquired by LCHC Holdings, Inc. from the proceeds of the loan.

Note 13. LONG-TERM DEBT

LCHC Holdings, Inc. participates in the NMTC program described in Note 10 and has obtained a loan of \$7,800,000 payable to CCM Community Development 65 LLC, which is a Community Development Entity (CDE). The loan proceeds were used solely for the purpose of constructing Lana'i Community Health Center's facility. The loan has a put/call option feature that is exercisable in March 2022. The stated interest rate is 1.4683% and the loan matures on February 28, 2045. The loan calls for quarterly interest only payments beginning April 1, 2015. Beginning March 4, 2022 quarterly principal and interest payment begin unless either party exercises the put/call option. The loan is secured by substantially all assets acquired by LCHC Holdings, Inc. from the proceeds of the loan.

In connection with the loan, LCHC Holdings, Inc. also incurred loan acquisition costs of \$544,012 which have been capitalized and will be amortized over the life of the loan. Debt issuance costs are presented net of accumulated amortization of \$58,935. LCHC Holdings, Inc. was in compliance with the terms of its NMTC loan, including loan covenants, at December 31, 2018 and 2017.

During the year, the Organization entered into an agreement with U.S. Department of Agriculture for a loan which totals \$1,000,000 to refinance debt and construct a photovoltaic energy system. A mortgage payable to U.S. Department of Agriculture is due in monthly installments of principal and interest of \$3,890, at a fixed rate of interest of 2.375% until 2048. The loan requires that the Organization maintains a debt service reserve fund. The balance of the debt service reserve fund as of December 31, 2018 was \$23,308, and is included in cash and cash equivalents.

A summary for all long term debt as of December 31, 2018 is as follows:

USDA Loan	\$ 977,895
CCM QLICI Loan A	5,464,200
CCM QLICI Loan B	2,335,800
Total long-term debt	<u>8,777,895</u>
Less current installments of long-term debt	<u>(23,762)</u>
Net long-term debt	<u><u>\$ 8,754,133</u></u>

Maturities of long term debt are as follows:

2019	\$ 23,762
2020	\$ 24,332
2021	\$ 24,917
2022	\$ 7,825,515
2023	\$ 26,127
Thereafter	<u>\$ 853,242</u>
	<u><u>\$ 8,777,895</u></u>

LANA 'I COMMUNITY HEALTH CENTER AND SUBSIDIARY

Notes to the Financial Statements

December 31, 2018

Note 14. LIQUIDITY AND AVAILABILITY OF FINANCIAL ASSETS

Management's policy is to structure its financial assets to be available as its general expenditures, liabilities and other obligations come due.

Financial Assets at December 31, 2018	\$ 957,293
Less those unavailable for general expenditures within one year due to:	
Accounts Payable	(136,447)
Accrued Expenses	(227,267)
Deferred Revenue	(238,886)
Current Portion of Long Term Debt	(23,762)
Restricted by donor with purpose restriction	<u>(86,111)</u>
Financial Assets available to meet cash needs for general expenditures within one year	<u>\$ 244,820</u>

In addition to those resources, the Association plans to continue collection efforts on \$220,277 (net of allowance for doubtful accounts of \$150,062) in patient receivable, \$50,641 in Grants Receivables and \$18,757 in other receivables, which support operations without restrictions as to use.

Note 15. COMMITMENTS

The Organization has entered into an agreement with a company to construct a 28.27 Kw DC PV Solar Energy System. The total contract price is \$109,578 and the Organization has incurred \$98,620 of expenses under the contract as of December 31, 2018. This amount is recorded in Construction in Progress.

Note 16. RECENT ACCOUNTING PRONOUNCEMENTS

In February 2016, the FASB issued ASU 2016-02, Leases, which supersedes FASB Accounting Standards Codification (ASC) Topic 840, Leases, and makes other conforming amendments to U.S. GAAP. ASU 2016-02, requires, among other changes to the lease accounting guidance, lessees to recognize most leases on the balance sheet via a right-of-use asset and lease liability as well as additional qualitative and quantitative disclosures. ASU 2016-02 is effective for fiscal years beginning after December 15, 2019, but permits early adoption, and mandates a modified retrospective transition method. The provisions are effective for the Organization's year ending December 31, 2020. Management is currently evaluating the impact that the adoption of these provisions will have on the financial statements, but expects ASU 2016-02 will not add significant right-of-use assets and lease liabilities to the statement of financial position.

In November 2016, the FASB issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash, which requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. As a result, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The new standard amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Early adoption is permitted. The provisions are effective for the Organization's year ending December 31, 2020. The amendments should be applied using a retrospective transition method to each period presented. Management is currently evaluating the impact that the adoption of these provisions will have on the financial statements.

Lana'i Community Health Center and Subsidiary

Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2018

Federal Grantor/Pass-through Grantor/Program Title	Federal CFDA Number	Contract Number	Federal Expenditures	State Expenditures
U.S. Department of Health and Human Services				
Consolidated Health Centers (Community Health Centers, Migrant Health Centers, Health Care for the Homeless, and Public Housing Primary Care)	93.224	H80CS08775	\$ 1,858,385	\$ -
Rural Health Care Services Outreach, Rural Health Network Development and Small Health Care Provider Quality Improvement Program	93.912	DO4RH31637	90,277	-
Subtotal U.S. DHHS - Direct Funding Programs			<u>1,948,662</u>	<u>-</u>
Passed Through the State of Hawaii Department of Health:				
Family Planning Services	93.217	ASO Log 13-118	67,368	49,416
Medical Assistance Program	93.778	DHS-08-MQD-5163	25,080	-
Subtotal U.S. DHHS - Passed Through the State of Hawaii Department of Health			<u>92,448</u>	<u>49,416</u>
Passed Through the Hawaii Primary Care Association:				
Strategies to Prevent Obesity, Diabetes, Heart Disease and Stroke Among Adults in Hawaii	93.757	03-0121-4018	93,045	-
Subtotal U.S. DHHS - Passed Through the Hawaii Primary Care Association			<u>93,045</u>	<u>-</u>
Total U.S. Department of Health and Human Services Programs			<u>2,134,155</u>	<u>49,416</u>
U.S. Department of Housing and Urban Development				
Community Facility Loans and Grant	10.766	61-006	1,000,000	-
Women, Infants, Children	10.557	ASO Log 18-130	31,363	-
Total U.S. Department of Housing and Urban Development			<u>1,031,363</u>	<u>-</u>
Total expenditures of Federal Awards			<u>\$ 3,165,518</u>	<u>\$ 49,416</u>

See accompanying Notes the Schedule of Expenditures of Federal Awards

Lana'i Community Health Center and Subsidiary

Notes to the Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2018

Note A. BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards includes the Federal grant activity of Lana'i Community Health Center under programs of the Federal government for the year ended December 31, 2018.

The information in this Schedule is presented in accordance with the requirements of *Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of the Lana'i Community Health Center it is not intended to and does not present the financial position, changes in net assets, or cash flows of the Lana'i Community Health Center.

Note B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting: Expenditures reported on this Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in *Uniform Guidance*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

Indirect Cost Rate: The Organization elected not to use the De Minimis indirect cost rate.

Note D. SUMMARY OF USDA LOAN ACTIVITY

The following are the loan proceeds drawn down during the year ended December 31, 2018 and the balances at December 31, 2018:

Balance at December 31, 2017	\$	-
Proceeds		1,000,000
Payments		(22,105)
Balance at December 31, 2018	\$	<u>977,895</u>

**INDEPENDENT AUDITOR'S REPORT ON FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING
STANDARDS**

The Board of Directors
Lana'i Community Health Center
Lana'i City, Hawaii 96763

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Lana'i Community Health Center, as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise Lana'i Community Health Center's basic financial statements, and have issued our report thereon dated April 8, 2019.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered Lana'i Community Health Center's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Lana'i Community Health Center's internal control. Accordingly, we do not express an opinion on the effectiveness of Lana'i Community Health Center's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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Report on Internal Control

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether Lana'i Community Health Center's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Carbonaro CPAs & Management Group

April 8, 2019
Wailuku, Hawai'i

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER COMPLIANCE
FOR EACH MAJOR FEDERAL PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE**

The Board of Directors
Lana'i Community Health Center
Lana'i City, Hawaii 96763

Report on Compliance for Each Major Federal Program

We have audited Lana'i Community Health Center's compliance with the types of compliance requirements described in the *OMB* Compliance Supplement that could have a direct and material effect on each of Lana'i Community Health Center's major Federal programs for the year ended December 31, 2018. Lana'i Community Health Center's major Federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Lana'i Community Health Center's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and the audit requirement of *Title 2 U.S. Code of Federal Regulations Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Lana'i Community Health Center's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major Federal program. However, our audit does not provide a legal determination of Lana'i Community Health Center's compliance.

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Report on Compliance For Each Major Federal Program
Page 2

Opinion on Each Major Federal Program

In our opinion, Lana‘i Community Health Center complied in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major Federal programs for the year ended December 31, 2018.

Report on Internal Control over Compliance

Management of Lana‘i Community Health Center is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Lana‘i Community Health Center’s internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Lana‘i Community Health Center’s internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Carbonaro CPAs & Management Group

April 8, 2019
Wailuku, Hawai‘i

LANA 'I COMMUNITY HEALTH CENTER

Schedule of Findings and Questioned Costs
For the year ended December 31, 2018

Section I-Summary of Auditor's Results

Financial Statements

Type of Auditor's report issued: **Unmodified**

Internal control over financial reporting:

• Significant Deficiencies **None**

• Material Weaknesses **None**

Noncompliance which is material to the financial statements **None**

Federal Awards

Internal control over Major Programs:

• Significant Deficiencies **None**

• Material Weaknesses **None**

Type of auditor's report issued in regards to major program compliance **Unmodified**

The program tested as a major programs was:

Community Facility Loans and Grant CFDA # 10.766 **\$1,000,000**

The threshold for distinguishing Type A and Type B Programs was **\$750,000**

Auditee qualified as a low-risk auditee **Yes**

Section II- Financial Statement and Compliance Findings

NONE NOTED

Section III- Prior Year Audit Findings

NONE NOTED