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MCLEAN AFFILIATES, INC.

FINANCIAL STATEMENTS

SEPTEMBER 30, 2017 AND 2016

MCLEAN AFFILIATES, INC.

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Independent Auditors' Report

To the Board of Directors
McLean Affiliates, Inc.
Simsbury, Connecticut

We have audited the accompanying financial statements of McLean Affiliates, Inc., which comprise the statements of financial position as of September 30, 2017 and 2016, and the related statements of activities and changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' 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 auditors consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of McLean Affiliates, Inc., as of September 30, 2017 and 2016, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Blum, Shapiro & Company, P.C.

West Hartford, Connecticut
December 4, 2017

MCLEAN AFFILIATES, INC.

STATEMENTS OF FINANCIAL POSITION SEPTEMBER 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 8,889,380	\$ 7,849,167
Accounts receivable, net of allowance of \$334,131 in 2017 and \$345,199 in 2016	1,819,494	1,815,172
Prepaid expenses and other current assets	322,423	324,672
Total current assets	<u>11,031,297</u>	<u>9,989,011</u>
Investments	<u>8,116,040</u>	<u>6,406,589</u>
Assets Whose Use is Limited	<u>289,873</u>	<u>284,253</u>
Charitable Remainder Trust, Net	<u>524,714</u>	<u>478,797</u>
Property and Equipment		
Land	29,950	29,950
Land improvements	2,487,961	1,749,872
Buildings	27,763,298	26,723,219
Fixed equipment	9,319,140	8,477,947
Movable equipment	2,721,877	2,604,986
Construction in progress	74,121	1,094,884
	<u>42,396,347</u>	<u>40,680,858</u>
Less accumulated depreciation	<u>23,644,766</u>	<u>21,910,772</u>
Property and equipment, net	<u>18,751,581</u>	<u>18,770,086</u>
Other Noncurrent Assets	<u>147,349</u>	<u>164,977</u>
Total Assets	<u>\$ 38,860,854</u>	<u>\$ 36,093,713</u>

The accompanying notes are an integral part of the financial statements

MCLEAN AFFILIATES, INC.

STATEMENTS OF FINANCIAL POSITION (CONTINUED) SEPTEMBER 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts payable	\$ 1,104,105	\$ 945,466
Entrance fee refunds payable	7,405	209,126
Accrued salaries, wages, payroll taxes and other	1,084,597	994,948
Accrued expenses	293,939	278,657
Deferred revenue	513,219	568,868
Deposits held for residents	430,622	594,848
Total current liabilities	<u>3,433,887</u>	<u>3,591,913</u>
Refundable Entrance Fees, Net of Current Portion	6,365,062	6,255,370
Deferred Revenue from Nonrefundable Entrance Fees	3,193,789	3,266,660
Other Liabilities	84,401	81,485
Total liabilities	<u>13,077,139</u>	<u>13,195,428</u>
Net Assets		
Unrestricted	23,681,304	21,096,715
Temporarily restricted	2,102,411	1,801,570
Total net assets	<u>25,783,715</u>	<u>22,898,285</u>
Total Liabilities and Net Assets	<u>\$ 38,860,854</u>	<u>\$ 36,093,713</u>

The accompanying notes are an integral part of the financial statements

MCLEAN AFFILIATES, INC.

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS FOR THE YEARS ENDED SEPTEMBER 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
Unrestricted Revenues and Other Support		
Net resident service fee revenue	\$ 26,485,131	\$ 24,736,454
Recovery of (provision for) bad debts	(42,000)	96,313
Net patient service revenues	<u>26,443,131</u>	<u>24,832,767</u>
Contributions received from related entities	322,992	445,008
Contributions	226,779	176,031
Other unrestricted revenues	181,123	173,471
Net assets released from restrictions	<u>138,525</u>	<u>164,866</u>
Total unrestricted revenues and other support	<u>27,312,550</u>	<u>25,792,143</u>
Expenses		
Salaries and wages	14,117,570	13,163,965
Employee benefits	2,919,828	2,856,949
Other expenses	6,662,318	6,542,650
Depreciation	<u>1,736,911</u>	<u>1,648,511</u>
Total expenses	<u>25,436,627</u>	<u>24,212,075</u>
Income from Operations	<u>1,875,923</u>	<u>1,580,068</u>
Other Income (Expense)		
Other expense	(1,220)	(2,202)
Interest and dividend income	154,351	431,774
Net other income	<u>153,131</u>	<u>429,572</u>
Excess of Revenues over Expenses	2,029,054	2,009,640
Other Changes in Unrestricted Net Assets		
Change in net unrealized gains (losses) on investments	<u>555,535</u>	<u>(20,525)</u>
Changes in unrestricted net assets	<u>2,584,589</u>	<u>1,989,115</u>
Changes in Temporarily Restricted Net Assets		
Change in value of charitable remainder trust	45,917	(113,656)
Contributions	393,449	283,514
Net assets released from restrictions	<u>(138,525)</u>	<u>(164,866)</u>
Changes in temporarily restricted net assets	<u>300,841</u>	<u>4,992</u>
Change in Net Assets	2,885,430	1,994,107
Net Assets - Beginning of Year	<u>22,898,285</u>	<u>20,904,178</u>
Net Assets - End of Year	<u>\$ 25,783,715</u>	<u>\$ 22,898,285</u>

The accompanying notes are an integral part of the financial statements

MCLEAN AFFILIATES, INC.

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED SEPTEMBER 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
Cash Flows from Operating Activities		
Change in net assets	\$ 2,885,430	\$ 1,994,107
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Proceeds from entrance fees	1,313,500	534,500
Refunds of entrance fees and entrance fee payable	(339,221)	(705,861)
Amortization of entrance fees	(1,000,106)	(662,816)
Depreciation	1,736,911	1,648,511
Recovery of (provision for) bad debts	(42,000)	96,313
Change in value of charitable remainder trust	(45,917)	113,656
Change in net unrealized (gain) loss on investments	(555,535)	20,525
(Increase) decrease in operating assets:		
Accounts receivable	37,678	(221,805)
Prepaid expenses and other current assets	2,249	15,734
Other noncurrent assets	17,628	18,628
Increase (decrease) in operating liabilities:		
Accounts payable	158,639	264,206
Accrued salaries, wages, payroll taxes and other	89,649	(72,273)
Accrued expenses	15,282	(101,537)
Deferred revenue	(55,649)	96,837
Deposits held for residents	(303,299)	4,602
Net cash provided by operating activities	<u>3,915,239</u>	<u>3,043,327</u>
Cash Flows from Investing Activities		
Purchases of investments	(1,159,536)	(1,633,535)
Purchases of property and equipment	(1,715,490)	(1,311,281)
Purchases of assets whose use is limited	-	(100,000)
Net cash used in investing activities	<u>(2,875,026)</u>	<u>(3,044,816)</u>
Cash Flows from Financing Activities		
Repayments of notes receivable	-	214,550
Net cash provided by financing activities	<u>-</u>	<u>214,550</u>
Net Increase in Cash and Cash Equivalents	1,040,213	213,061
Cash and Cash Equivalents - Beginning of Year	<u>7,849,167</u>	<u>7,636,106</u>
Cash and Cash Equivalents - End of Year	<u>\$ 8,889,380</u>	<u>\$ 7,849,167</u>

The accompanying notes are an integral part of the financial statements

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - ORGANIZATION

McLean Affiliates, Inc. (McLean) was incorporated as a nonprofit entity on October 1, 2008, as a subsidiary of the McLean Fund (the Fund), a trust created by the last will of George P. McLean. Prior to this incorporation, McLean operated as a unit of the Fund. The subsidiaries of the Fund include McLean, the McLean Foundation, Inc. (the Foundation) and the McLean Game Refuge (the Refuge). The Foundation and the Refuge are not included in these statements.

McLean operates as a Continuing Care Retirement Community (CCRC) and a long-term care facility located in Simsbury, Connecticut. As of September 30, 2017, McLean has 89 Medicaid and Medicare certified skilled nursing beds, 71 assisted living units, 3 residential care home beds, and 88 independent living apartments and cottages.

McLean provides a full range of services, including physical therapy, occupational therapy and speech therapy. The average occupancy for McLean was 85% and 84% for 2017 and 2016, respectively. In addition, McLean provides home care, hospice, adult day care and meals on wheels services to residents of Simsbury and surrounding towns.

Overall occupancy levels at McLean for the years ended September 30, 2017 and 2016, are as follows:

	<u>2017</u>	<u>2016</u>
Independent Living	86%	87%
Assisted Living	82%	79%*
Skilled Nursing Care	86%	86%

* McLean added 22 units during the year ended September 30, 2016, which affected the above calculated occupancy for 2016.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

In order to ensure observance of limitations and restrictions placed on the use of the resources available to McLean, the accounts are maintained on the accrual basis of accounting and, accordingly, the accounts of McLean are reported in the following net asset categories.

Unrestricted

Unrestricted net assets represent resources that may be expended at the direction of the Board of Directors. Net assets set aside by the Board of Directors for future capital improvements, over which the Board retains control and may, at its discretion, subsequently use for other purposes, are included in unrestricted net assets.

Temporarily Restricted

These assets represent resources that have donor-imposed restrictions as to purpose or time of expenditure. When the purpose or timing restrictions have been met, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities and changes in net assets as net assets released from restriction. Temporarily restricted net assets as of September 30, 2017 are restricted for time, capital projects and other resident assistance purposes. Details of temporarily restricted net assets are included in Note 7.

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (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 the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Financial statement areas where management applies the use of estimates consist primarily of the allowance for doubtful accounts, amortization of entrance fees and valuation of the charitable remainder trust. It is management's opinion that the estimates applied in the accompanying financial statements are reasonable. However, actual results could differ from those estimates.

Cash and Cash Equivalents

McLean considers all short-term, highly liquid instruments purchased with an original maturity of three months or less to be cash equivalents. McLean maintains its cash and cash equivalents in bank deposit accounts that, at times, may exceed federally insured limits. McLean believes it is not exposed to any significant credit risk on cash and cash equivalents.

Cash equivalents are comprised of money market funds. Money market funds are not insured by the FDIC and are not a risk-free investment. Money market funds invest in a variety of instruments including mortgage-backed and asset-backed securities. Although a money market fund seeks to preserve its one dollar per share value, it is possible that a money market fund's value can decrease below one dollar per share.

Accounts Receivable

Accounts receivable are reduced by an allowance for doubtful accounts. In evaluating the collectability of accounts receivable, McLean analyzes its past history and identifies trends for each of its major payor sources of revenue to estimate an appropriate allowance for doubtful accounts and provision for bad debts based upon management's assessment of historical and expected net collections considering business and economic conditions, trends in health care coverage and other collection indicators. Management regularly reviews data about these major payor sources of revenue in evaluating the sufficiency of the allowance for doubtful accounts.

Investment Valuation and Income Recognition

Investments are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. See Note 3 for a discussion of fair value measurements.

Purchases and sales of securities are recorded on the trade date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

Investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair value in the accompanying statements of financial position with realized and unrealized gains and losses on these investments included in the accompanying statements of activities and changes in net assets as increases or decreases in unrestricted net assets.

At September 30, 2017, there was one investment with gross unrealized holding losses greater than one year of \$218,158.

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

McLean accounts for other-than-temporary impairments in accordance with GAAP and continually reviews its securities for impairment conditions, which could indicate that other-than-temporary declines in market value have occurred. In conducting this review, numerous factors are considered, which include specific information pertaining to an individual company or a particular industry, general market conditions that reflect prospects for the economy as a whole, and the ability and intent to hold securities until recovery. The carrying value of investments is reduced to its estimated realizable value if a decline in fair value is considered to be other-than-temporary. Management does not believe any of these investment declines are other-than-temporary and, therefore, McLean did not record an impairment charge for the years ended September 30, 2017 and 2016.

Assets Whose Use is Limited

Assets whose use is limited include assets restricted under State of Connecticut law governing CCRC entrance fee escrow arrangements and assets set aside for operating CCRC escrow and reserve funds.

Charitable Remainder Trust

Charitable remainder trust consists of assets irrevocably transferred for the benefit of McLean and other beneficiaries. Revocable charitable remainder trust agreements are not recorded as contributions unless enforceable by law. Irrevocable charitable remainder trusts are recorded as contributions at fair value when the assets are received or when McLean is notified of the existence of the agreement. The accounting treatment varies depending upon the type of the agreement created and whether McLean or a third party is the trustee.

McLean is the beneficiary of an irrevocable charitable remainder trust which is managed by a third-party trustee. A charitable remainder trust provides for the payment of distributions to the grantor or other designated beneficiaries over the trust's term (usually the designated beneficiary's lifetime). At the end of the trust's term, the remaining assets are available for McLean's use.

The trusts are carried at the net fair value of the underlying investments less the estimated liability to the designated beneficiary. The portion of the trust attributable to the present value of the future benefits to be received by McLean is recognized in the statement of activities and changes in net assets as a temporarily restricted contribution in the period the trust is established.

Property and Equipment

Property and equipment are recorded at cost. Routine maintenance, repairs, renewals and replacement costs are charged against income. Expenditures in excess of \$2,000 that materially increase values, change capacities or extend useful lives are capitalized. Upon sale or retirement of property, plant and equipment, the cost and related accumulated depreciation are eliminated from the respective accounts, and the resulting gain or loss is included in other income in the statements of activities and changes in net assets.

Depreciation of property and equipment is provided using the straight-line method over the estimated useful lives of the assets as follows:

Land improvements	5-30 years
Buildings	10-40 years
Fixed equipment	5-25 years
Movable equipment	5-20 years

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

Depreciation expense totaled \$1,736,911 and \$1,648,511 for the years ended September 30, 2017 and 2016, respectively.

Asset Retirement Obligation

McLean accounts for any conditional asset retirement obligations in accordance with the provisions of GAAP. GAAP requires that an entity recognize a liability for the fair value of conditional asset retirement obligations if the fair value of the liability can be reasonably estimated. The fair value of a liability for conditional asset retirement obligations must be recognized when incurred, generally upon acquisition, construction, development or through the normal operation of the asset. McLean conducted a review of its facilities to determine if there are any assets that give rise to the obligation to perform asset retirement activity, which may not be within its control, such as the remediation or removal of asbestos containing materials.

McLean has certain items in its buildings that it believes may contain asbestos. McLean currently has no plans to renovate the areas that contain these items or remove these items from service. However, McLean has determined what it believes to be a reasonable settlement date to retire these items in the event that such retirement is not within their control. The initial estimated current cost associated with the retirement of these items was determined to be \$52,000 and was recorded as an asset retirement obligation in other liabilities on the accompanying statements of financial position. For each of the years ended September 30, 2017 and 2016, the estimated current cost accreted amounted to \$2,919 and has been reflected in the statements of activities and changes in net assets.

Revenue from Residents

Upon occupancy of an independent living unit at McLean, residents pay an entrance fee, a portion of which is refundable and a portion of which is nonrefundable (see Note 6). The nonrefundable portion of the entrance fee is deferred and amortized into income over the estimated remaining lives of the individual residents as determined by McLean use of mortality tables.

Additionally, the residents of the independent living units pay a monthly fee to cover the services they receive. These resident service fees are recorded as revenue when earned.

Health Center Patient Revenues

Patient revenues are recorded when patient services are performed. Amounts received from certain payors are different from the established billing rates of McLean, and these differences are accounted for as contractual allowances. Net patient service revenues are reported at the estimated net realizable amount from patients, third-party payors and others for services rendered.

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

Contributions

Contributions are defined as voluntary, nonreciprocal transfers. Unrestricted and unconditional contributions are recognized as support when received or pledged, if applicable. Contributions are reported as temporarily restricted support if they are received with donor stipulations that limit the use of such assets. When a 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 accompanying statements of activities and changes in net assets as net assets released from restrictions due to satisfaction of restrictions. Contributions received whose restrictions are met in the same period are presented with unrestricted net assets.

Other Unrestricted Revenues

Other unrestricted revenues consists of charges for additional resident meals, guest meals, cable television, beauty salon services and other miscellaneous charges to residents.

Income Taxes

McLean is a not-for-profit trust described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal income taxes pursuant to Section 501(a) of the Code.

Subsequent Events

In preparing these financial statements, management has evaluated subsequent events through December 4, 2017, which represents the date the financial statements were available to be issued.

NOTE 3 - FAIR VALUE OF FINANCIAL INSTRUMENTS

Generally accepted accounting principles establish a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1

Quoted market prices (unadjusted) in active markets for identical assets or liabilities that McLean has the ability to access at the measurement date.

Level 2

Inputs and information other than quoted market indices included in Level 1 that are observable for the asset or liability, either directly or indirectly, and McLean has the ability to redeem the asset or liability in the near term subsequent to the measurement date.

Level 3

Unobservable inputs are used to measure the fair value to the extent that observable inputs are not available, and McLean does not have the ability to redeem the asset or liability in the near term subsequent to the measurement date.

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Financial Instruments Measured at Fair Value

The following is a description of the valuation methodologies and investment strategies used for financial instruments measured at fair value:

Fixed Income

Fixed income investments are valued using quoted market prices in an active market in which the securities are traded.

Equity

Equity funds are valued at the quoted net asset value of shares reported in the active market in which the funds are traded.

Charitable Remainder Trust

Fair value inputs used for charitable remainder trusts are based on the estimated present value of the future payment to McLean, which is considered to be the fair value of the assets held in trust less estimated future payments to the designated beneficiaries.

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 McLean 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.

There have been no changes in the methodologies used at September 30, 2017 and 2016.

The following is a summary of the source of fair value measurements for assets and liabilities that are measured at fair value as of September 30, 2017 and 2016:

Description	2017			Total
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	
Assets:				
Investments:				
Fixed income investments	\$ 1,504,342	\$ -	\$ -	\$ 1,504,342
Equity investments	6,611,698	-	-	6,611,698
Total investments	8,116,040	-	-	8,116,040
Charitable remainder trust	-	524,714	-	524,714
Total Assets Measured at Fair Value	\$ 8,116,040	\$ 524,714	\$ -	\$ 8,640,754

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

Description	2016			Total
	Fair Value Measurements Using			
	Level 1	Level 2	Level 3	
Assets:				
Investments:				
Fixed income investments	\$ 496,204	\$ -	\$ -	\$ 496,204
Equity investments	5,910,385	-	-	5,910,385
Total investments	6,406,589	-	-	6,406,589
Charitable remainder trust	-	478,797	-	478,797
Total Assets Measured at Fair Value	\$ 6,406,589	\$ 478,797	\$ -	\$ 6,885,386

NOTE 4 - NET PATIENT SERVICE REVENUES

The following table summarizes net patient service revenues for the years ended September 30, 2017 and 2016:

	2017	2016
Gross patient service revenues:		
Long-term care	\$ 9,665,719	\$ 9,719,347
Post acute care	5,747,059	5,129,910
Home health services	4,947,179	4,682,948
Independent living	4,718,145	4,436,340
Assisted living	5,618,369	5,253,989
Outpatient services	543,749	564,031
	31,240,220	29,786,565
Less contractual allowances	4,755,089	5,050,111
Total Net Patient Service Revenues	\$ 26,485,131	\$ 24,736,454

McLean has agreements with third-party payors that provide for payments to McLean at amounts different from established rates. A summary of the payment arrangements with major third-party payors is as follows:

Medicare

Inpatient long-term care services rendered to Medicare program beneficiaries are paid based upon a per-diem prospective payment rate. Home care services rendered to Medicare program beneficiaries are paid based upon a 60-day episodic prospective payment rate.

Medicaid

Inpatient long-term care services rendered to Medicaid program beneficiaries are paid based upon a per-diem cost based payment rate, which is subject to State audit adjustments. Home care services rendered to Medicaid program beneficiaries are paid based upon a per visit or per hour payment rate.

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

Revenue under third-party payor agreements is subject to audit and retroactive adjustments. Provisions for estimated third-party payor settlements and adjustments are estimated in the period in which the related services are rendered and adjusted in future periods as final settlements are determined. Management believes that all applicable government reimbursement principles have been properly applied and that no material adjustments will occur as a result of an audit.

During 2017 and 2016, approximately 32% of net patient revenue was received under the Medicare program and 14% and 17% under the Medicaid program, respectively. Significant concentrations of net patient receivables are 51% Medicare and 14% Medicaid as of September 30, 2017, and 53% Medicare and 11% Medicaid as of September 30, 2016.

NOTE 5 - ASSETS WHOSE USE IS LIMITED

Under Connecticut state law, McLean is required to maintain certain reserve funds as follows:

Operation and Maintenance Account

McLean is required to maintain one month's budgeted operating expenses in this account as described in Note 2.

Entry Fee Proceeds Account

McLean is required to deposit all entrance fees into the entry fee proceeds account as received. Upon the later of the expiration of the applicable statutory rights of the purchaser to rescind (30 days) or the date of occupancy, the balance in the account is available for operations.

The reserve funds are all included within assets whose use is limited on the statements of financial position.

NOTE 6 - CCRC ENTRY FEES AND OBLIGATIONS TO PROVIDE FUTURE BENEFITS

Certain McLean residents are provided living accommodations, other facilities and services, and certain medical care in exchange for payment of entrance fees and monthly service charges. Residents can choose from refundable and nonrefundable agreements.

Under the terms of nonrefundable agreements, entrance fees are not refundable to residents who reside independently at McLean for more than fifty months. A resident who leaves prior to fifty months under this agreement is refunded a portion of their entrance fee, which declines approximately 2% per month for each month the unit was occupied. These entrance fees are recorded as deferred revenue upon receipt and amortized on a straight-line basis into revenue over the remaining estimated life expectancy of the individual resident. Upon termination of the agreement, the amount of any unamortized, nonrefundable entrance fee is recorded as revenue.

Under the terms of refundable agreements, portions of the entrance fees are fully refundable at a designated percentage. The entire amount of this designated refundable percentage is recorded as refundable entry fees on the statements of financial position. The remaining nonrefundable portion of the entrance fees are accounted for and amortized in line with the nonrefundable agreements. Entrance fee refunds due under these agreements but not paid as of year-end are recorded as current liabilities.

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

Based upon McLean's existing fee structure and management's expectation that future monthly service charges will be reflective of related operating costs, McLean is not required to record a liability for its obligation to provide future services and facilities to current residents. Based upon management's projections, McLean does not believe such a liability on its CCRC contracts exists at this time.

Prior to September 30, 2012, McLean capitalized \$275,000 of costs related to acquiring the initial CCRC contracts. These costs include wages and marketing costs directly related to acquiring these contracts and are being amortized on a straight-line basis over the average remaining residential life expectancies. These amounts are included in other noncurrent assets on the statements of financial position and represent \$147,349 and \$164,977 as of September 30, 2017 and 2016, respectively.

NOTE 7 - TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes as of September 30, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Capital projects	\$ 524,714	\$ 478,797
Sorenson Media Center	968,321	832,596
Healthcare services and other	<u>609,376</u>	<u>490,177</u>
Total	<u>\$ 2,102,411</u>	<u>\$ 1,801,570</u>

During the years ended September 30, 2017 and 2016, there were releases of \$32,609 and \$69,108, respectively, for the Sorenson Media Center and \$105,916 and \$95,758, respectively, for healthcare services and other.

NOTE 8 - EMPLOYEE BENEFIT PLAN

McLean sponsors a 401(k) Retirement Savings Plan (the Plan) for its employees. The Plan is a defined contribution plan covering all salaried and hourly employees of McLean who elect to participate and have been scheduled to work 1,000 hours a year and have reached 20 years of age. Participants may contribute up to the Internal Revenue Service salary deferral limits. McLean contributes to the Plan on behalf of its qualified employees based on their wages once the employee has completed one year of service as defined.

McLean contributed \$839,928 and \$845,879 to the Plan for the years ended September 30, 2017 and 2016, respectively.

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

NOTE 9 - HEALTHCARE INDUSTRY

Regulatory Environment

The healthcare 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 healthcare program participation requirements, reimbursement for patient services, and Medicare fraud and abuse. Government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed. Management believes that McLean is in compliance with fraud and abuse regulations as well as other applicable government laws and regulations. While no material regulatory inquiries have been made, compliance with such laws and regulations can be subject to future government review and interpretation, as well as regulatory actions unknown or unasserted at this time.

NOTE 10 - FUNCTIONAL EXPENSES

McLean's functional expenses are as follows for the years ended September 30, 2017 and 2016:

	<u>2017</u>	<u>20156</u>
Long-term care	\$ 5,826,188	\$ 5,542,694
Home health services	4,229,700	3,790,663
Post-acute care	3,848,946	3,738,782
Independent living	2,526,881	2,495,095
Assisted living	4,566,420	4,183,297
General and administrative	3,810,190	3,830,395
Outpatient services	464,479	482,341
Development	<u>163,823</u>	<u>148,808</u>
Total	<u>\$ 25,436,627</u>	<u>\$ 24,212,075</u>

NOTE 11 - RELATED PARTY TRANSACTIONS

The Fund is an entity that holds investment assets used to support the subsidiaries of the Fund. The Fund provided McLean with contributions for programs that McLean provides. These contributions amounted to \$262,992 and \$385,000 for the years ended September 30, 2017 and 2016, respectively. These contributions have been recorded within contributions received from related entities in the statements of activities and changes in net assets.

The Foundation is a nonprofit corporation whose purpose is to receive, maintain and apply funds to promote and engage in activities in furtherance of the public welfare, principally by supporting and assisting the Fund and its operating entities. McLean received contributions from the Foundation for general use. This support amounted to \$60,000 and \$60,008 for the years ended September 30, 2017 and 2016, respectively, and has been recorded within contributions received from related entities.

MCLEAN AFFILIATES, INC.

NOTES TO FINANCIAL STATEMENTS

McLean has been reimbursed by the Refuge for expenses that have been paid on its behalf. This reimbursement amounted to \$218,485 and \$175,556 for the years ended September 30, 2017 and 2016, respectively, and has been recorded as a reduction to certain operating expenses in the statements of activities and changes in net assets.

NOTE 12 - DEFERRED REVENUE

McLean recognizes deferred revenues in relation to its private payor long-term care and assisted living businesses. In addition, McLean recognizes deferred revenues under its home health Medicare prospective payment system. As of September 30, 2017 and 2016, McLean recorded \$513,219 and \$568,868, respectively, in deferred revenue shown as a current liability.

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Independent Auditors' Report on Supplementary Information

To the Board of Directors
McLean Affiliates, Inc.
Simsbury, Connecticut

We have audited the financial statements of McLean Affiliates, Inc., a subsidiary of the McLean Fund, as of and for the years ended September 30, 2017 and 2016, and our report thereon dated December 4, 2017, which expressed an unmodified opinion on those financial statements, appears on pages 1 and 2. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental detail of operating expenses for the years ended September 30, 2017 and 2016, is presented for the 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 information is fairly stated in all material respects in relation to the financial statements as a whole.

Blum, Shapiro & Company, P.C.

West Hartford, Connecticut
December 4, 2017

MCLEAN AFFILIATES, INC.

SUPPLEMENTAL DETAIL OF OPERATING EXPENSES FOR THE YEARS ENDED SEPTEMBER 30, 2017 AND 2016

	<u>2017</u>	<u>2016</u>
Salaries and Wages		
Nursing	\$ 8,656,936	\$ 7,815,962
General and administrative	2,019,618	2,083,607
Auxiliary	1,440,797	1,341,532
Dietary	1,102,534	1,043,653
Housekeeping	376,788	380,357
Plant	371,729	353,732
Development	125,376	121,384
Laundry	23,795	23,738
Total salaries and wages	<u>14,117,573</u>	<u>13,163,965</u>
Employee Benefits		
Payroll taxes	1,017,672	972,341
Retirement plan expense	839,928	857,759
Health insurance	751,883	721,647
Workers' compensation	209,103	266,251
Other employee benefits	101,237	38,951
Total employee benefits	<u>2,919,823</u>	<u>2,856,949</u>
Other Expenses		
General and administrative	1,959,167	1,746,788
Dietary	1,341,084	1,299,842
Plant	1,251,996	1,359,831
Nursing	1,164,395	1,311,623
Auxiliary	624,763	620,737
Housekeeping	171,684	62,124
Laundry	110,685	114,281
Development	38,546	27,424
Total other expenses	<u>6,662,320</u>	<u>6,542,650</u>
Depreciation	<u>1,736,911</u>	<u>1,648,511</u>
Total Expenses	<u>\$ 25,436,627</u>	<u>\$ 24,212,075</u>