

Audited Financial Statements

Gardner Family Care Corporation

For The Years Ended June 30, 2018 and 2017

Gardner Family Care Corporation

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Independent Auditor's Report

Board of Directors
Gardner Family Care Corporation
San Jose, California

Report on the Financial Statements

We have audited the accompanying financial statements of Gardner Family Care Corporation (the "Organization"), which comprise the balance sheets as of June 30, 2018 and 2017 and the related statements of operations 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.

Auditor's Responsibility

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Gardner Family Care Corporation as of June 30, 2018 and 2017 and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

CAW. LLP

Fresno, California

October 24, 2018

Gardner Family Care Corporation
Balance Sheets
June 30, 2018 and 2017

Assets	2018	2017
Current assets:		
Cash and cash equivalents	\$ 3,302,172	\$ 3,804,077
Grants and contracts receivables	4,227,647	2,627,934
Due from affiliate – GFHN	63,995	25,120
Prepaid expenses and other assets	232,648	208,235
Deposits and other assets	309,663	303,894
Total current assets	8,136,125	6,969,260
Estimated third-party payer settlements	397,172	575,519
Property and equipment, net	5,130,330	5,193,443
Total assets	\$ 13,663,627	\$ 12,738,222
 Liabilities And Net Assets		
Liabilities:		
Current liabilities:		
Accounts payable and other accrued expenses	\$ 480,667	\$ 629,849
Due to affiliate – GFHN	59,781	51,753
Accrued payroll and related liabilities	1,069,040	1,021,097
Accruals for self-insurance	478,036	444,557
Deferred revenue	22,753	12,250
Long-term debt, current portion	160,556	149,286
Total current liabilities	2,270,833	2,308,792
Noncurrent liabilities:		
Long-term debt	6,138,895	5,464,738
Total liabilities	8,409,728	7,773,530
Net assets:		
Unrestricted	5,253,899	4,964,692
Total net assets	5,253,899	4,964,692
 Total liabilities and net assets	\$ 13,663,627	\$ 12,738,222

See accompanying Notes to the Financial Statements

Gardner Family Care Corporation
Statements of Operations and Changes in Net Assets
For the years ended June 30, 2018 and 2017

Revenue and Other Support	2018	2017
Contracts:		
Mental health	\$ 19,183,440	\$ 17,953,216
Women, infant, and children	1,981,494	2,066,798
Total contract revenue	21,164,934	20,020,014
 Court-ordered program revenues:		
Drinking driver program	692,379	727,744
Drug diversion	139,463	121,483
Outpatient substance abuse	20,528	30,871
Total patient revenue	852,370	880,098
 Other revenue	879,270	988,022
Total unrestricted revenue and other support	22,896,574	21,888,134
 Expenses:		
Salaries and benefits	18,445,846	17,591,140
Purchased services	862,021	864,970
Professional fees	138,952	164,124
Supplies	170,147	150,260
Travel, conference, and meetings	433,728	418,890
Facility costs	694,172	689,773
Insurance	97,000	108,046
Depreciation and amortization	478,912	488,677
Interest	268,393	235,389
Other	1,018,196	892,289
Total expenses	22,607,367	21,603,558
 Excess of revenues over expenses	289,207	284,576
 Net Assets:		
Beginning of year	4,964,692	4,680,116
End of year	\$ 5,253,899	\$ 4,964,692

See accompanying Notes to the Financial Statements

Gardner Family Care Corporation
Statements of Cash Flows
For the years ended June 30, 2018 and 2017

	2018	2017
Cash Flows From Operating Activities:		
Change in net assets	\$ 289,207	\$ 284,576
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	478,912	488,677
Changes in operating assets and liabilities:		
Grant and contract receivable	(1,599,713)	1,238,630
Due from affiliate – GFHN	(38,875)	14,296
Prepaid and other assets	(24,413)	(35,722)
Deposits	(5,769)	(16,671)
Estimated third-party payer settlements	178,347	334,351
Accounts payable and accrued expenses	(149,182)	202,025
Accruals for self-insurance	33,479	(51,606)
Accrued payroll and related liabilities	47,943	(29,118)
Deferred revenue	10,503	7,672
Due to affiliate	8,028	(5,091)
Net cash provided by (used in) operating activities	(771,533)	2,432,019
Cash Flows From Investing Activities:		
Purchase of property and equipment	(415,799)	(109,324)
Net cash used in investing activities	(415,799)	(109,324)
Cash Flows From Financing Activities:		
Change in line-of-credit	-	(300,000)
Proceeds from new debt	835,086	-
Principal payments on long-term debt	(149,659)	(171,613)
Net cash provided by (used in) financing activities	685,427	(471,613)
Net increase (decrease) in cash and cash equivalents	(501,905)	1,851,082
Cash and cash equivalents at beginning of year:	3,804,077	1,952,995
Cash and cash equivalents at end of year:	\$ 3,302,172	\$ 3,804,077
Supplemental Disclosure of Cash Flow Information:		
Interest paid	\$ 268,393	\$ 235,389
Donated space and services	\$ 188,494	\$ 316,756

See accompanying Notes to the Financial Statements

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 1: Organization and Operations

Gardner Family Care Corporation (the “Organization”) is a community based multi-services organization, which operates as a California non-profit corporation, located in San Jose, California. The Organization provides a full range of behavioral - social services programs for the community of Santa Clara County. The following is a summary of these special programs:

- Mental Health Program (Gardner Centro De Bienestar)
- Women, Infants, and Children (WIC) Program
- Proyecto Primavera Programs
 - Drug Diversion
 - Drinking Driver Program

Note 2: Summary of Significant Accounting Policies

Basis of Accounting:

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Net assets, revenues, and expenses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Organization and changes therein are classified and reported as follows:

Unrestricted net assets: Net assets are those currently available for use and are not subject to donor-imposed stipulations.

Temporarily restricted net assets: Net assets subject to donor-imposed stipulations that may or will be met, either by actions of the Organization and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of operations as net assets released from restrictions. Donor-restricted contributions whose restricts expire during the same fiscal year are recognized as unrestricted revenue.

Permanently restricted net assets: Net assets subject to donor-imposed stipulations that they be maintained permanently by the Organization.

There were no temporarily or permanently restricted net assets as of June 30, 2018.

Cash and Cash Equivalents:

Cash and cash equivalents include short-term highly liquid investments with original maturities of three months or less. As of June 30, 2018 and 2017, the carrying amount of all the accounts, net of outstanding checks, was \$3,302,172 and \$3,804,077, respectively. Per the various financial institutions as of June 30, 2018 and 2017, approximately \$250,000 and \$250,000, respectively, was covered by federal depository insurance.

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 2: Summary of Significant Accounting Policies (Continued)

Property and Equipment:

Property and equipment is stated at cost at the date of acquisition. Depreciation of property and equipment is computed on the straight-line method over the estimated useful lives of the individual assets. The lives of the assets range from 5 years to 25 years. Repairs and maintenance are charged to operations and major improvements are capitalized. Donated assets are recognized at market value at the time of donation. Expenses for assets in excess of \$5,000 are capitalized and assets purchased with government grants are expended in accordance with government program guidelines.

Accrued Vacation:

Accumulated unpaid employee vacation leave benefits are recognized as liabilities on the books as required by the generally accepted accounting principles. As of June 30, 2018 and 2017, accrued vacation amounted to \$659,911 and \$636,982, respectively. The Organization's policy on sick leave benefits is to record amounts as operating expenditures in the period sick leave is taken.

Revenues and Support:

Contract revenue is primarily funded by government grants which generally restrict the use of such funds to cover the operating expenses directly related to providing services under the contracts. These contracts are recognized as revenue when services are provided and over the periods specific in the related contract agreements. Other grants and contributions that have been awarded for a specified purpose, but have not yet been spent are recognized as temporarily restricted net assets. When the services have been rendered, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Program service fee is recorded during the period in which services were rendered. For the year ended June 30, 2018 and 2017, the Organization received received \$19,183,440 and \$17,953,216, respectively, in mental health contract revenue from the County of Santa Clara, which represents 84% and 82% of the total revenue received. For the year ended June 30, 2018 and 2017, the Organization received \$1,981,494 and \$2,066,798, respectively, in Supplemental Food Program for Women, Infants, and Children revenue from the California Department of Public Health, which represents 9% and 9% of the total revenue received.

Collective bargaining:

The Organization has approximately 219 employees. A concentration of labor supply in employees working under union collective bargaining agreements represents approximately 69 percent of its hourly and salaried workforce in one collective bargaining units. The Organization's management workforce is not represented by unions.

Concentration of credit risk:

Financial instruments potentially subjecting the Organization to concentrations of credit risk consist primarily of bank demand deposits in excess of Federal Deposit Insurance Corporation ("FDIC") insurance thresholds, cash held in money market accounts in excess of the amounts insured by the U.S. Treasury insurance for money market funds, and various debt and equity investments in excess of Securities Investor Protection Corporation ("SIPC") insurance. Demand deposits are placed with a local financial institution, and management has not experienced any loss related to these demand deposits in the past. Investment securities are exposed to various risks, such as interest rate, market, and credit risk. It is at least reasonably possible, given the level of risk associated with investment securities, that changes in the near term could materially affect the amount reported in the consolidated financial statements. The risk associated with the investments is mitigated through diversification.

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 2: Summary of Significant Accounting Policies (Continued)

Functional Allocation of Expenses:

The Organization allocates various functional expenses among the programs based on actual personnel time and space utilized for the related activities. Fiscal and administrative costs were allocated based on percentage of program operating costs to total operating costs.

Excess (Deficit) of Revenues over Expenses:

The statement of operations includes excess (deficit) of revenues over expenses. Changes in unrestricted net assets which are excluded from excess of revenues over expenses, consistent with industry practice, include unrealized gains and losses on investments other than trading securities, permanent transfers of assets to and from affiliates for other than goods and services, and contributions of long-lived assets (including assets acquired using contributions which by donor restriction were to be used for the purposes of acquiring such assets).

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.

Tax-exempt Status:

The Organization is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code and has been granted tax-exempt status by the Internal Revenue Service and the California Franchise Tax Board. Accordingly, no provision for federal and state income taxes has been made in the accompanying financial statements. There was no unrelated business income for fiscal year 2018.

GAAP provides accounting and disclosure guidance about positions taken by an organization in its tax returns that might be uncertain. Management has considered its tax positions and believes that all of the positions taken by the Organization in its federal and state exempt organization tax returns are more likely than not to be sustained upon examination. The Organization's returns are subject to examination by federal and state taxing authorities generally for three years after they are filed.

Reclassification:

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

Subsequent Events:

The Organization has evaluated subsequent events through October 24, 2018, which is the date the financial statements were available to be issued.

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 3: Cash and Cash Equivalents

The cash balance as of June 30, 2018 and 2017, consists of the following:

	<u>2018</u>	<u>2017</u>
Cash - operating accounts	\$ 1,549,800	\$ 2,783,028
Cash - self-insurance reserve	450,764	252,365
Cash - board reserved	1,286,908	755,484
Petty cash	14,700	13,200
Total cash and cash equivalents	<u>\$ 3,302,172</u>	<u>\$ 3,804,077</u>

Note 4: Prepaid Expenses, Deposits, and Other Assets

Prepaid expenses, deposits, and other assets were comprised of the following at June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Prepaid Expenses:		
Insurance	\$ 81,130	\$ 60,057
Other	149	149
HSA Contribution	151,369	148,029
	<u>\$ 232,648</u>	<u>\$ 208,235</u>
Deposits and Other Assets:		
Unemployment Insurance (Joint Agencies Trust)	\$ 309,002	\$ 301,558
Other	661	2,336
	<u>\$ 309,663</u>	<u>\$ 303,894</u>

Note 5: Grants and Contracts Receivable

Grants and contracts receivable were comprised of the following at June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
CalWorks	\$ 168,217	\$ 140,931
Family Services	1,195,623	477,861
Adult Outpatient	185,029	97,837
First 5 Medi-Cal	386,732	195,327
WIC	296,505	364,307
Prop 63	471,865	148,561
Differential Response	253,203	361,954
Adult/Older Adult	569,549	385,285
First 5 Superior Court	74,946	67,360
Other	625,978	388,511
Total	<u>\$ 4,227,647</u>	<u>\$ 2,627,934</u>

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 6: Accrued Payroll and Related Expenses

Accrued expenses and other liabilities as of June 30, 2018 and 2017 consist of the following:

	2018	2017
Accrued salaries	\$ 277,408	\$ 265,628
Accrued vacation	659,911	636,982
Accrued payroll taxes	50,465	45,853
Accrued employee benefits	81,256	72,645
Total	\$ 1,069,040	\$ 1,021,108

Note 7: Property and Equipment

Land, building and equipment at June 30, 2018 and 2017 was comprised of the following:

	2018	2017
Land	\$ 1,315,654	\$ 1,315,654
Buildings and building improvements	8,986,949	8,723,413
Leasehold improvement	115,827	115,827
Furniture & equipment	642,504	731,519
Total	11,060,934	10,886,413
Less: Accumulated depreciation and amortization	(5,930,604)	(5,692,970)
Property and equipment, net	\$ 5,130,330	\$ 5,193,443

Depreciation expense for the year ended June 30, 2018 and 2017 amounted to \$478,912 and \$488,677, respectively.

Note 8: Bank Line of Credit

The Organization has a revolving line of credit for a maximum of \$500,000 through Heritage Bank of Commerce. The line of credit is unsecured and the line of credit agreement ends on May 18, 2019. The interest is payable monthly at a variable rate that is .750 percentage points above the Prime Rate as published by the Wall Street Journal. The initial interest rate is 4.00%. The line of credit had no outstanding balance as of June 30, 2018.

Note 9: Functional Expenses

	2018	2017
Program services	\$ 19,908,921	\$ 18,964,964
General and administrative	2,698,445	2,638,594
Total	\$ 22,607,366	\$ 21,603,558

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 10: Estimated Third-party Payor Settlements

Estimated third-party payor settlements relate to the County of Santa Clara's Mental Health Services — Short-Doyle Program contracts for the reimbursement of patient charges. Cost settlement receivables and liabilities as of June 30, 2018 and 2017, consist of the following:

<u>Fiscal Year</u>	<u>2018</u>	<u>2017</u>
2006 - 2007	\$ 580,484	\$ 580,484
2007 - 2008	122,474	122,474
2008 - 2009	755,432	755,432
2009 - 2010	403,150	403,150
2010 - 2011	(89,850)	(89,850)
2011 - 2012	133,647	133,647
2012 - 2013	345,212	345,212
2013 - 2014	(10,189)	(10,189)
2014 - 2015	(216,657)	(216,657)
2015 - 2017	(106,299)	(106,299)
2017 - 2018	(114,595)	(114,595)
2018 - 2019	(112,466)	-
	<u>1,690,343</u>	<u>1,802,809</u>
Provision for uncollectible	(1,293,171)	(1,227,290)
Net value	<u>\$ 397,172</u>	<u>\$ 575,519</u>

Cost settlement receivables are carried at their estimated collectible amounts. They are periodically evaluated for collectability based on information provided by County of Santa Clara. Provision for uncollectible on cost settlement receivable is determined on the basis of experience in dealing with County of Santa Clara and their mandate with the State.

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 11: Long-term Debt

Long-term debt at June 30, 2018 consisted of the following:

	2018	2017
On September 27, 2012, the Organization secured a loan from Heritage Bank for \$4,650,000 with an annual interest rate of 4.00%, amortized over 25 years with fixed monthly payments of \$24,686 and a maturity date of September 26, 2017. On September 25 2017, the Organization refinanced the loan for \$4,900,000 with an annual interest rate of 4.41% amortized over 25 years. Monthly payments of \$27,154 consist of principal and interest and the loan matures September 25, 2027. The loan is secured by the 1st Deed of Trust on the 160 E. Virginia Street, San Jose property.	\$ 4,817,856	\$ 4,086,596
On April 24, 2013, the Organization secured a loan from Heritage Bank for \$1,693,000, with an annual interest rate of 4.25%, amortized over five years with fixed monthly payment of \$9,231 and a maturity date of April 15, 2020. The Organization used the loan to pay off two loans from GFHN (\$924,213 and \$378,620) and the remainder was used to reduce the \$250,000 loan from GFHN. The loan is secured by the Deed of Trust on the 195 E. Virginia Street, San Jose property.	1,481,595	1,527,428
Total long-term debt	6,299,451	5,614,024
Less: current portion	(160,556)	(149,286)
	\$ 6,138,895	\$ 5,464,738

Future principal payments are as follows for the years ended June 30:

Year	Principal
2019	\$ 160,556
2020	1,550,999
2021	123,190
2022	128,813
2023	134,692
Thereafter	4,201,201
Total	\$ 6,299,451

The Organization is subject to various covenants and restrictions under its borrowing arrangements. In addition, the Organization has agreed to maintain certain financial ratios and adhere to other loan covenants described in the loan documents. At June 30, 2018, the Organization is in compliance with all covenants.

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 12: Related Party Transactions

On July 1, 1997, Gardner Family Care Corporation (formerly Gardner Health Center, Inc.) affiliated with Gardner Family Health Network, Inc. ("GFHN") (formerly Family Health Foundation, Inc.), a nonprofit corporation, operating as a licensed community clinic providing primary care medical, dental, optometric and pharmacy services, as well as substance abuse, WIC and other programs, at multiple clinic locations in San Jose and Alviso, California.

With the affiliation: (a) GFHN became the sole corporate member of the Organization, (b) the Organization and GFHN retained its own separate corporate identity, (c) the Organization and GFHN agreed upon a group of individuals to serve as common directors of both organizations; and (d) GFHN's social, mental, and behavioral care programs were transferred to the Organization, while its primary care program was transferred to GFHN. The affiliation allowed both organizations to use its resources to the greatest effectiveness for the benefit of their respective communities.

The total amount due from GFHN at June 30, 2018 is \$63,995, which is comprised of employee expenses. The total amount due to GFHN at June 30, 2018 is \$59,781, which is comprised of rent and other shared services. GFHN contributed \$85,000 to GFCC for general operating purposes for the year ended June 30, 2018.

GFHN has guaranteed the line of credit and loans payable by the Organization to Heritage Bank. As such, the bank includes GFHN's financial performance in evaluation of the financial covenants.

Lease Expense:

The Organization leases clinic space at GFHN's CompreCare facility (3030 Alum Rock Avenue, San Jose, California) for the Organization's WIC program. The monthly rent is \$5,471. The lease expires on June 30, 2019. The minimum future rental payments excluding any operating expenses escalation that may be calculated in the future as of June 30, 2018, are:

<u>Year</u>	
2019	\$ 65,652

Lease Income:

The Organization leases clinic space on its 195 Virginia Street, San Jose, California facility to GFHN under an operating lease expiring on November 30, 2027. The monthly rent during the term of the lease is \$18,542. Rent received from GFHN during the year was \$273,870.

The Organization also leases clinic space on its 160 Virginia Street, San Jose, California facility to GFHN under an operating lease expiring on June 30, 2020. The monthly rent during the term of the lease is \$9,202. Rent received from GFHN during the year was \$110,424.

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 13 – Accruals for Self-Insurance

Effective May 1, 2007, the Organization terminated its employee health insurance with Kaiser and started its own self-insurance health program. Plan oversight and administration is provided by an independent third party, Benefit and Risk Management Services (“BRMS”), and by the plan consultant, Innovative Cost Management Services, Inc. (“ICMS”).

BRMS processes and adjudicates all medical, dental and vision claims. BRMS maintains an interactive database to monitor plan eligibility, plan experience reporting functionality, claims, and plan member communication.

ICMS provides oversight of plan components, including providing reports on experience/claims reporting, plan expenses, premiums, and overall review and oversight. As the plan consultants/brokers they maintain daily interaction with the Organization's executive staff for any issues not directly maintained by BRMS.

The self-insurance liability as of June 30, 2018, is comprised of an estimated accrual of \$331,487 for incurred but not reported (“IBNR”) claims, and \$146,549 related to accrued liabilities of the program. The IBNR liability pertains to claims that have been incurred but not yet submitted by the various doctors and/or hospitals to BRMS for processing as of the end of the fiscal year. Under the Self Insured Health Plan, doctors have up to one year to submit claims. The IBNR amount was calculated independently by ICMS, using information provided by BRMS. The calculation has been reviewed by management, and it is determined to properly reflect the liability that would still be incurred should the Organization change plans.

In order to maintain adequate funds in the program, the Organization opened a Self-Insurance Money Market Fund (SIMMF) where it deposits premiums for the program. These premiums are derived from actuarial tables set up with the assistance of ICMS, which take into consideration past, and future utilization for medical, dental and vision claims. Based on the number of employees enrolled in the program and the type of health insurance plan selected, BRMS provides a Fully Insured Equivalent (FIE) which the Organization deposits into the SIMMF. BRMS processes the employee insurance claims, ascertaining that they meet the plan's provision and the Organization pays these claims from funds in the SIMMF. As of June 30, 2018, the balance in the SIMMF account was \$315,647

The medical and prescription drug plan is partially insured through a specific and aggregate stop loss (excess risk) insurance policy with HCC Life Insurance Company. Medical and prescription drug claims paid during the policy year per individual member in excess of \$150,000 or \$1,000,000 in aggregate are covered through the stop loss insurance policy.

Gardner Family Care Corporation
Notes to Financial Statements
For the years ended June 30, 2018 and 2017

Note 14: Commitments and Contingencies

Federal and state contracts and other requirements:

The Organization receives grants and contracts which require fulfillment of certain conditions as set forth in the terms of the grant agreement and contract, and are subject to audit and adjustment upon review by the granting agencies. Failure to comply with the conditions of the grants could result in the return of funds to the granting agencies. The amounts, if any, of expenditures that may be disallowed by the granting agencies cannot be determined at this time, although management believes that it has complied with conditions of its grants and contracts it expects they will not have a significant effect on the Organization's financial position.

Contingencies:

In the ordinary course of business, the Organization may be a party to claims and legal actions. While the outcome cannot be determined at this time, management's opinion is the liability, if any, from these actions will not have a material adverse effect on the Organization's financial position.

The health care industry is subject to numerous laws and regulations of federal, state, and local governments. 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. These laws and regulations include, but are not limited to, accreditation, licensure, and government health care program participation requirements, reimbursement for patient services, and Medicare and Medi-Cal fraud and abuse. Recently, government activity has increased with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by health care providers. Violations of these laws and regulations could result in exclusion from government health care program participation, together with the imposition of significant fines and penalties, as well as significant repayment for past reimbursement for patient services received. While the Organization is subject to similar regulatory reviews, there are no reviews currently underway, and management believes that the outcome of any potential regulatory review will not have a material adverse effect on the Organization's financial position.