



AIDS Healthcare Foundation
Audited Consolidated Financial Statements
and Supplementary Information
As of and For the Years Ended December 31, 2018 and 2017
with Report of Independent Auditors

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Report of Independent Auditors

Board of Directors AIDS Healthcare Foundation

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of AIDS Healthcare Foundation, which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of operations and changes in net assets, functional expenses and cash flows for the years then ended, and the related notes to the consolidated financial statements (collectively, 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 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.



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of AIDS Healthcare Foundation as of December 31, 2018 and 2017, and the changes in its net assets, and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated April 30, 2019 on our consideration of AIDS Healthcare Foundation'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 the effectiveness of AIDS Healthcare Foundation's 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 AIDS Healthcare Foundation's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Vaqueria & Company LLP".

**Glendale, California
April 30, 2019**

**AIDS Healthcare Foundation
Consolidated Balance Sheets**

	December 31	
	2018	2017
ASSETS		
Current assets		
Cash and cash equivalents	\$ 70,228,387	\$ 32,620,381
Pharmacy revenue receivable, net of allowance for doubtful accounts of \$6,046,344 and \$3,400,468 at December 31, 2018 and 2017, respectively	61,344,162	58,682,069
Premium revenue receivable, net of allowance for doubtful accounts of \$3,748,640 at December 31, 2018 and 2017	8,057,158	9,660,604
Grant revenue receivable	11,278,675	8,433,226
Accounts receivable, net of allowance for doubtful accounts of \$7,576,952 and \$6,398,426 at December 31, 2018 and 2017, respectively	5,924,348	3,800,489
Inventories	34,980,430	30,843,334
Investments	22,623,345	18,437,312
Prepaid expenses and other current assets	23,084,187	22,967,807
Total current assets	237,520,692	185,445,222
Noncurrent assets		
Assets limited as to use	6,828,111	6,828,111
Property and equipment, net	192,978,034	138,426,791
Long-term investments	68,510,128	117,387,453
Intangibles, deposits and other assets	22,435,100	24,086,402
Total assets	\$ 528,272,065	\$ 472,173,979
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable	\$ 42,699,104	\$ 60,713,214
Accrued expenses	22,695,882	16,490,032
Unearned premiums	9,690,159	30,147,718
Claims payable	22,223,621	17,618,697
Current portion of long-term debt	2,948,538	2,616,154
Total current liabilities	100,257,304	127,585,815
Deferred rent	2,892,710	2,790,833
Interest rate swap	354,345	164,186
Long-term debt, net of current portion	37,759,046	19,523,397
Total liabilities	141,263,405	150,064,231
Net assets		
Without donor restrictions	386,651,104	321,806,096
With donor restrictions	357,556	303,652
Total net assets	387,008,660	322,109,748
Total liabilities and net assets	\$ 528,272,065	\$ 472,173,979

See notes to consolidated financial statements.

AIDS Healthcare Foundation
Consolidated Statements of Operations and Changes in Net Assets

	Years ended December 31	
	2018	2017
Operating revenues		
Unrestricted revenues, gains, and other support		
Pharmacy revenue, net	\$ 1,135,863,420	\$ 1,030,597,409
Premiums earned, net	194,357,261	191,986,268
Grant revenue	52,085,078	43,330,788
Net patient service revenue	8,260,844	9,311,874
Contributions		
Cash	4,922,820	1,991,949
In-kind, thrift store	9,994,684	10,420,670
In-kind, other	2,000,245	1,257,694
Other	4,164,100	3,158,773
Operating revenues before net assets released from restrictions for operations	1,411,648,452	1,292,055,425
Net assets released from restrictions for operations	303,652	499,671
Total operating revenues	1,411,952,104	1,292,555,096
Operating expenses		
Salaries	155,135,213	132,843,102
Benefits	49,186,140	44,853,774
Medical services, supplies and drugs	211,667,398	197,850,594
Cost of pharmacy and thrift stores sales	722,075,551	675,424,750
Rent and other facilities related expenses	47,034,518	38,937,583
Depreciation and amortization	15,188,250	13,349,254
Interest expense	1,238,418	1,309,499
Provision for bad debts	3,573,253	9,850,712
Insurance	2,384,598	2,050,488
Professional services	33,473,779	29,664,730
Charitable contributions	10,182,912	9,262,304
Other expenses	95,897,778	87,607,904
Total operating expenses	1,347,037,808	1,243,004,694
Income from operations	64,914,296	49,550,402
Investment (loss) Income, net	(69,288)	4,234,140
Increase in net assets without donor restrictions	64,845,008	53,784,542
Changes in net assets with donor restrictions		
Contributions	357,556	395,124
Net assets released from restrictions for operations	(303,652)	(499,671)
Increase (decrease) in net assets with donor restrictions	53,904	(104,547)
Increase in net assets	64,898,912	53,679,995
Net assets, beginning of year	322,109,748	268,429,753
Net assets, end of year	\$ 387,008,660	\$ 322,109,748

See notes to consolidated financial statements.

AIDS Healthcare Foundation
Consolidated Statements of Functional Expenses
Years ended December 31, 2018 and 2017

	<u>Healthcare Services</u>	<u>Housing Services</u>	<u>Thrift Stores</u>	<u>Outreach</u>	<u>Fundraising</u>	<u>Administration</u>	<u>Total</u>
2018							
Salaries	\$ 127,199,097	\$ 300,844	\$ 4,444,818	\$ 12,519,281	\$ 1,468,387	\$ 9,202,786	\$ 155,135,213
Benefits	40,103,274	98,955	1,736,842	4,651,930	381,773	2,213,366	49,186,140
Medical services, supplies and drugs	205,531,180	5,666	1,037	5,953,040	51,534	124,941	211,667,398
Cost of pharmacy and thrift stores sales	722,039,097	-	36,454	-	-	-	722,075,551
Rent and other facilities related expenses	36,002,829	1,636,144	2,432,861	3,091,822	115,243	3,755,619	47,034,518
Depreciation and amortization	10,226,917	498,917	142,329	1,201,410	20,083	3,098,594	15,188,250
Interest expense	814,711	7	8,866	45,014	-	369,820	1,238,418
Provision for bad debts	3,120,813	4,957	-	447,483	-	-	3,573,253
Insurance	2,013,653	120,797	46,458	141,481	758	61,451	2,384,598
Professional services	20,274,676	470,269	219,351	5,946,721	307,240	6,255,522	33,473,779
Charitable contributions	1,458,748	43,104	-	6,397,183	2,078,605	205,272	10,182,912
Other expenses	54,187,066	107,193	833,484	33,164,795	2,513,228	5,092,012	95,897,778
	<u>\$ 1,222,972,061</u>	<u>\$ 3,286,853</u>	<u>\$ 9,902,500</u>	<u>\$ 73,560,160</u>	<u>\$ 6,936,851</u>	<u>\$ 30,379,383</u>	<u>\$ 1,347,037,808</u>
2017							
Salaries	\$ 109,294,455	\$ 27,198	\$ 4,073,726	\$ 10,213,360	\$ 1,348,804	\$ 7,885,559	\$ 132,843,102
Benefits	36,035,675	17,174	1,684,831	4,199,887	360,133	2,556,074	44,853,774
Medical services, supplies and drugs	192,663,870	-	2,814	4,728,470	13,007	442,433	197,850,594
Cost of pharmacy and thrift stores sales	675,366,228	-	58,522	-	-	-	675,424,750
Rent and other facilities related expenses	28,869,438	107,597	2,511,058	2,188,411	166,365	5,094,714	38,937,583
Depreciation and amortization	9,200,886	3,593	188,851	905,675	34,649	3,015,600	13,349,254
Interest expense	901,451	-	7,238	46,026	5,314	349,470	1,309,499
Provision for bad debts	9,828,719	-	-	21,993	-	-	9,850,712
Insurance	1,576,793	21,583	47,582	102,648	2,100	299,782	2,050,488
Professional services	17,681,716	54,539	256,706	4,999,846	486,878	6,185,045	29,664,730
Charitable contributions	1,884,642	-	1,849	4,250,437	1,663,931	1,461,445	9,262,304
Other expenses	50,477,845	7,237	1,000,714	29,843,787	2,706,759	3,571,562	87,607,904
	<u>\$ 1,133,781,718</u>	<u>\$ 238,921</u>	<u>\$ 9,833,891</u>	<u>\$ 61,500,540</u>	<u>\$ 6,787,940</u>	<u>\$ 30,861,684</u>	<u>\$ 1,243,004,694</u>

See notes to consolidated financial statements.

AIDS Healthcare Foundation
Consolidated Statements of Cash Flows

	Years ended December 31	
	2018	2017
Cash flows from operating activities		
Change in net assets	\$ 64,898,912	\$ 53,679,995
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Impairment of goodwill and intangible assets	275,000	207,148
Depreciation of property and equipment	13,415,299	11,564,866
Loss on sale of property and equipment	26,221	63,944
Amortization of debt issuance costs	158,397	146,212
Amortization of intangible assets	1,471,730	1,437,980
Provision for bad debts	3,573,253	9,850,712
Unrealized (gain) loss on interest rate swap	190,159	(318,292)
Contributed pharmacy inventory	2,000,245	1,257,694
Changes in operating assets and liabilities:		
Accounts receivable	(11,204,654)	(15,959,360)
Premiums revenue receivable	4,448,895	2,891,130
Grant revenue receivable	(2,845,449)	732,300
Inventories	(6,137,341)	(5,602,258)
Prepaid expenses, deposits, and other current assets	(211,808)	5,556,980
Accounts payable	(18,014,110)	4,720,132
Unearned premiums	(20,457,559)	20,074,548
Accrued expenses	6,205,850	(965,971)
Claims payable	4,604,924	(7,650,528)
Deferred rent	101,877	214,939
Net cash provided by operating activities	42,499,841	81,902,171
Cash flows from investing activities		
Additions to property and equipment	(67,992,763)	(42,221,692)
Goodwill recognized from acquisition	-	(3,500,000)
Purchases of investments	(2,308,708)	(59,877,237)
Sale of investments	47,000,000	-
Net cash used in investing activities	(23,301,471)	(105,598,929)
Cash flows from financing activities		
Proceeds from issuance of long-term debt	21,647,000	-
Principal payments on long-term debt	(3,237,364)	(2,818,662)
Net cash provided by (used in) financing activities	18,409,636	(2,818,662)
Net change in cash, cash equivalents and restricted cash	37,608,006	(26,515,420)
Cash, cash equivalents and restricted cash, beginning of year	39,448,492	65,963,912
Cash, cash equivalents and restricted cash, end of year	\$ 77,056,498	\$ 39,448,492
Supplemental disclosures of cash flow information		
Cash paid for interest during the year	\$ 1,238,418	\$ 1,309,499

See notes to consolidated financial statements.

AIDS Healthcare Foundation
Consolidated Statements of Cash Flows (Continued)

The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported within the consolidated balance sheets that sum to the total of the same such amounts shown in the consolidated statement of cash flows.

	Years ended December 31	
	2018	2017
Cash and cash equivalents	\$ 70,228,387	\$ 32,620,381
Restricted cash included in assets limited as to use	6,828,111	6,828,111
Total cash, cash equivalents and restricted cash shown in the statement of cash flows	\$ 77,056,498	\$ 39,448,492

See notes to consolidated financial statements.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business

AIDS Healthcare Foundation (the Foundation) headquartered in Los Angeles, California is a not-for-profit healthcare organization incorporated in 1987. The Foundation provides medical care for those affected by Human Immuno-deficiency Virus (HIV) or living with the Acquired Immune Deficiency Syndrome (AIDS). In addition, the Foundation participates in patient advocacy, housing and scientific research for those in need. The Mission of the Foundation is to provide “Cutting edge medicine and advocacy regardless of the ability to pay”. The Foundation has a network of 64 outpatient healthcare centers and 48 pharmacies that are located in 15 States including California, Florida, Texas, Washington, New York, Pennsylvania, Georgia, Nevada, Louisiana, South Carolina, Mississippi, Maryland, Illinois, Indiana and Ohio as well as Washington DC and Puerto Rico. The Foundation operates 19 Out of the Closet Thrift Stores in 7 States. The Foundation also operates in 43 countries including 13 in Africa, 12 in the Americas, 10 in Asia and 8 in Europe. During 2018 and 2017, the Foundation purchased properties in Los Angeles, California and Hollywood, Florida to provide very low income and transitional housing.

Principles of Consolidation

The Foundation’s consolidated financial statements include the accounts of AIDS Healthcare Foundation, AHF Healthcare Centers, AHF MCO of Florida, Inc., AIDS Healthcare Foundation Disease Management of Florida, Inc., HIV Immunotherapeutics Institute (formerly AHF Pharmacy Network), AIDS Healthcare Foundation Texas, Inc., AJ Brooklyn Medical Practice, P.C., AIDS Task Force of Greater Cleveland, Women Organized to Respond to Life-threatening Diseases (WORLD), AIDS Center of Queens County, Inc. (ACQC), South Side Help Center, Inc. (SSHC), AID Atlanta, Incorporated, AHF China LLC., AHF MCO of Georgia, Inc., AIDS Outreach Center (AOC) and Coalition to Preserve LA. All significant inter-organization balances and transactions have been eliminated in consolidation.

Basis of Presentation

The consolidated financial statements of the Foundation have been prepared in accordance with U.S. generally accepted accounting principles (US GAAP), which require the Foundation to report information regarding its financial position and activities according to the following net assets classifications:

Net assets without donor restrictions: Net assets that are not subject to donor-imposed restrictions and may be expended for any purpose in performing the primary objectives of the Foundation. These net assets may be used at the discretion of the Foundation’s management and the Board of Directors.

Net assets with donor restrictions: Net assets subject to stipulations imposed by donors, and grantors. Some donor restrictions are temporary in nature; those restrictions will be met by actions of the Foundation or by passage of time. Other donor restrictions are perpetual in nature, whereby the donor has stipulated the funds be maintained in perpetuity.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Presentation (continued)

Donor restricted contributions are reported as increase in net assets with donor restrictions. When a restriction expires, net assets are classified from net assets with donor restrictions to net assets without donor restrictions in the statement of operations and changes in net assets.

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, 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. Significant items subject to such estimation include: retroactive adjustments on premium revenues, valuation allowances on receivables, useful lives for property and equipment, estimates of the liability for claims incurred but not reported, and interest rate swap valuation. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include certain highly liquid investments with original maturities of three months or less.

Assets Limited as to Use

Assets limited as to use primarily include deposits restricted by the States of Florida, California and Georgia in connection with the Foundation's Medicare and Medicaid health maintenance organization (HMO) contracts. Assets limited as to use include deposits as required by Florida Office of Insurance Regulation (FLOIR), the Florida Agency for Healthcare Administration (FL AHCA), the California Department of Managed HealthCare (CA DMHC) and the Georgia Office of Insurance and Safety Fire Commissioner. These assets consist primarily of cash deposits and investments in money market funds which are reported at fair value based on quoted market prices.

Contributions

Contributions received are recorded as net assets without donor restrictions or net assets with donor restrictions, depending on the existence and/or nature of any donor-imposed restrictions. Contributions that are restricted by the donor are reported as an increase in net assets without donor restrictions if the restriction expires in the reporting period in which the contribution is recognized. All other donor restricted contributions are reported as an increase in net assets with donor restrictions, depending on the nature of restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statement of operations and changes in net assets as net assets released from restrictions.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Contributions (continued)

Contributed property and equipment are recorded at fair value at the date of donation. Contributions with donor-imposed stipulations regarding how long the contributed assets must be used are recorded as net assets with donor restrictions; otherwise, the contributions are recorded as net assets without donor restrictions.

Inventories

Inventories consist of pharmacy drugs, test kits, condoms and thrift store merchandise. Thrift store inventory consists primarily of donated goods held for resale. Contributions of thrift store inventory are recorded in the period received at estimated fair value.

All inventories other than thrift store inventory are determined on the first-in, first-out (FIFO) method and are stated at the lower of cost or market.

Property and Equipment

Property and equipment acquisitions are recorded at cost or, if donated, at the estimated fair value at the date of donation. The provision for depreciation and amortization is computed using the straight-line method over the estimated useful life of each class of depreciable asset, except for leasehold improvements, for which amortization is provided over the shorter of the estimated useful life or remaining lease term, as follows.

Buildings and fixed equipment	5 to 50 years
Furniture and movable equipment	3 to 15 years
Software	3 to 10 years

The Foundation's policy is to capitalize acquisitions of property and equipment with a cost of \$1,000 or more. Maintenance, repairs, and investments in minor equipment are charged to operations. Expenditures that will materially increase the value of properties or extend useful lives are capitalized.

Impairment of Long-lived Assets

The Foundation reviews the carrying amount of its long-lived assets for possible impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. The measurement of possible impairment is based primarily on the undiscounted future operating cash flows without interest charges generated through the use of these assets during their remaining estimated useful life. The assessed recoverability of long-lived assets will be impacted if estimated future operating cash flows are not achieved. Based upon its most recent analysis, the Foundation believes that no events occurred during the years ended December 31, 2018 and 2017 that would impair the carrying amount of its long-lived assets.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Goodwill and Intangible Assets

Goodwill represents the excess of cost of an acquired entity over the net of the amounts assigned to the fair value of assets acquired and liabilities assumed less fair value of assets and businesses acquired. As of December 31, 2018, and 2017, goodwill of \$5,942,930, is recorded in the Foundation's consolidated balance sheets within intangibles, deposits and other assets. Goodwill is reviewed annually for impairment or more frequently if events or circumstances indicate that the carrying value of an asset may not be recoverable. In accordance with GAAP, an entity has the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to the determination that it is more likely than not that the fair value of a reporting unit is less than its carrying value. If, after assessing the totality of events and circumstances, an entity determines that it is more likely than not that the fair value of the reporting unit is less than its carrying amount, then performing the two-step goodwill impairment test is unnecessary.

Intangible assets primarily represent the customer relationships acquired in the MOMs Pharmacies business acquisition. The intangible was measured at fair value using Level 3 inputs. The income approach was utilized in valuing the customer relationships, whereby the Foundation capitalized the future cash flows attributable to the customers based upon their expected future mortality dispersion function. The value of the customer relationships is amortized, to reflect the pattern of economic benefits consumed, on a straight-line basis over its useful life of 15 years. As of December 31, 2018, and 2017, net intangible assets amounted to \$14,630,457 and \$16,377,187, respectively.

Based on management's analysis, goodwill and intangible assets amounting to \$275,000 and \$207,148 was written off for the years ended December 31, 2018 and 2017, respectively.

Debt Issuance Costs

Debt issuance costs are deferred and amortized to interest expense using a method that approximates the effective-level-interest method over the term of the related debt. The debt issuance costs are related to the notes and loan agreements with Wells Fargo as further described in Note 12.

Claims Payable

Claims payable includes the liability for claims and medical services incurred but not paid and the estimated liability for claims incurred but not reported as of year end. The liability for claims incurred but not reported is determined based on historical evaluations and statistical analysis of paid claims. Although considerable variability is inherent in such estimates, management believes that the liability for unpaid claims is adequate. The estimate is continually reviewed and adjusted, as necessary, based on claims experience or as new information becomes known; such adjustments are included in current operations.

Net Patient Service Revenue

The Foundation has agreements with third-party payers that provide for payments to the Foundation at amounts different from its established rates.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Net Patient Service Revenue

Payment arrangements include individually contracted rates determined between the Foundation and the third-party payers as well as charges determined by publicly funded payers including Medi-Cal, Medicaid and Medicare. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for services rendered, including retroactive adjustments that are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Provision for bad debts from patient service revenue amounted to \$16,304 and \$187,624 for the years ended December 31, 2018 and 2017, respectively.

Premiums

The Foundation has agreements with third-party payers to provide medical services and/or disease management to subscribing participants. Under these agreements, the Foundation receives monthly capitation payments based on the number of each payer's participants, regardless of services actually performed by the Foundation.

Premiums are billed monthly and are recognized as revenue over the period in which the Foundation is obligated to provide services to its members. Premiums collected in advance are recorded as unearned premiums liability. Premiums are a predetermined amount on a per member per month (PMPM) basis. For the Medicare Plans, the Center for Medicare and Medicaid Services (CMS) determines the amount based on the county in which the member resides and other factors.

For the Medicaid Plans, the Medicaid agency for each state determines the amount based on the county in which the member resides and other factors. Member census is subject to audit and retroactive adjustment and such adjustments when determinable are included in current operations. Retroactive adjustments are accrued on an estimated basis in the period the related services are provided and adjusted in future periods as final settlements are determined.

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

Grant Revenue

Amounts received under government grant agreements are recognized as revenue as qualifying expenditures are incurred or when the service has been performed.

Functional Expenses

The costs of providing program and other activities have been summarized on a functional basis in the statements of functional expenses. Accordingly, certain costs have been allocated among program services, fundraising and administration benefited. Such allocations are determined by management on an equitable basis. The expenses were mainly allocated using the time and effort method (salaries, benefits, and other expenses), usage (supplies), full time equivalents (rent and other facilities related expenses).

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Pharmacy Revenue

The Foundation has agreements with third-party payers that provide payments to the Foundation at amounts different from its established rates. Payment arrangements include contracted calculations based upon Average Wholesale Price or Acquisition Cost. Pharmacy revenue is reported at the estimated net realizable amounts from patients, third-party payers, and others for pharmacy drugs dispensed. The allowance for doubtful accounts from pharmacy revenue receivables amounted to \$6,046,344 and \$3,400,468 at December 31, 2018 and 2017, respectively.

Federal and State Income Taxes

The Foundation is exempt from taxation under Section 501(c)(3) of the Internal Revenue Code and Section 23701d of the California Revenue and Taxation code and is generally not subject to federal or state income taxes. However, the Foundation is subject to income taxes on any net income that is derived from a trade or business, regularly carried on, and not in furtherance of the purposes for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the consolidated financial statements taken as a whole.

GAAP prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. It requires that an organization recognize in the financial statements the impact of the tax position if that position will more likely than not be sustained on audit, based on the technical merits of the position. As of and for the years ended December 31, 2018 and 2017, the Foundation had no material unrecognized tax benefits or tax penalties or interest.

The Foundation's federal and state income tax returns for the years 2014 through 2018 are subject to examination by regulatory agencies. Tax returns are subject to examination generally for three and four years after they were filed for federal and state, respectively.

Charity Care

The Foundation provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Foundation does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue.

Deferred Rent

For lease agreements that provide for escalating rent payments or free-rent occupancy periods, the Foundation recognizes rent expense on a straight-line basis over the non-cancelable lease term and option renewal periods where failure to exercise such options would result in an economic penalty in such amount that renewal appears, at the inception of the lease, to be reasonably assured. The lease term commences on the date that the Foundation takes possession of or controls the physical use of the property. Deferred rent is included in other liabilities (non-current) on the consolidated balance sheets.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Transactions in Foreign Currencies

The Foundation operates in 43 countries and accordingly, transacts in the local currencies of those countries. These foreign currency transactions are translated into U.S. dollars at the appropriate exchange rates when each transaction is executed. The net loss from foreign currency transactions amounted to \$2,131,804 and \$839,592 for the years ended December 31, 2018 and 2017, respectively, and is included in other expenses in the accompanying consolidated statements of operations and changes in net assets. The U.S. dollar is considered to be the functional and reporting currency of the Foundation.

Interest Rate Swap

The Foundation entered into interest rate swap agreements as a hedge against the variability in future interest payments due on certain long-term debts. The terms of the swap agreements effectively convert the variable rate interest payments due on the term notes to fixed rates through maturity (see Note 13). In accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification 815 (ASC 815), *Accounting for Derivative Instruments and Hedging Activities*, the interest rate swap is measured at fair value and recognized as either an asset or a liability in the balance sheets. The change in fair value of the swap is recognized as a gain or loss in the period of change.

Fair Value Measurements

Generally accepted accounting principles, which define fair value, establish a framework for measuring fair value and disclosures about fair value measurements. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. Assets and liabilities are measured at fair value using a three-level fair value hierarchy that ranks the quality and reliability of the information used to measure fair value. The three levels of inputs used to measure fair value are as follows:

Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the reporting date.

Level 2: Pricing inputs are other than quoted prices in active markets included in Level 1, which are either directly or indirectly observable as of the reporting date.

Level 3: Pricing inputs include significant inputs that are generally unobservable from objective sources. These inputs may be used with internally developed methodologies that result in management's best estimate of fair value.

An asset's or liability's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. All assets and liabilities for which the fair value measurement is based on significant unobservable inputs or instruments which trade infrequently and therefore have little or no price transparency are classified as Level 3.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Reclassifications

Certain amounts in the 2017 consolidated financial statements have been reclassified to conform to the 2018 presentation.

New Accounting Pronouncements

In August 2016, Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statement of Not-for-Profit Entities*. This accounting standard will change the presentation of net assets into two (2) categories: net assets with donor restrictions and net assets without donor restrictions. This accounting standard requires enhanced disclosures about the composition of net assets with donor restrictions at the end of the period and how the restrictions affect the use of the resources, qualitative information on how the not-for-profit manages its liquid resources and quantitative information that communicates the availability of the not-for-profit's financial assets at the balance sheet date to meet cash needs for general expenditures within one year of the balance sheet date, the amounts of expenses by both their natural classification and their functional classification, and methods used to allocate costs among program and support functions. This accounting standard also requires investments return to be reported net of external and direct internal investment expenses and use, in the absence of explicit donor stipulations, and the placed-in-service approach to be used for reporting expirations of restrictions on gifts of cash or other assets to be used to acquire or construct long-lived assets. The Foundation adopted ASU 2016-14 as of and for the year ended December 31, 2018. The ASU has been applied retrospectively to all periods presented.

In May 2014, FASB issued ASU 2014-09, *Revenue from Contracts with Customers*, requiring an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. This new standard will supersede most existing revenue recognition guidance, including industry-specific health care guidance when it becomes effective. This accounting standard permits use of either a full retrospective or retrospective with cumulative effect transition method. In August 2015, FASB issued ASU 2015-14, which defers the effective date of ASU 2014-09 one year making it effective for the Foundation for annual reporting periods beginning after December 31, 2018.

In February 2016, FASB issued ASU 2016-02, *Leases*. This accounting standard requires organizations that lease assets to recognize a right-of use asset and a liability, initially measured at the present value of the lease payments, in its balance sheet. Lessor accounting is largely unchanged from that applied under current GAAP. This accounting standard will also require additional disclosure about the amount, timing, and uncertainty of cash flows arising from leases. This accounting standard is effective for fiscal years beginning after December 15, 2018.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New Accounting Pronouncements (continued)

In August 2016, FASB issued ASU 2016-15, *Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments*. ASU 2016-15 provides guidance on how certain cash receipts and cash payments should be presented and classified in the statement of cash flows with the objective of reducing existing diversity in practice with respect to these items. The new standard will be effective for fiscal years beginning after December 15, 2017. The Foundation adopted the new accounting standard on January 1, 2018.

In November 2017, FASB issued ASU 2016-18, *Statement of Cash Flows: Restricted Cash*. This accounting standard requires that a statement of cash flows explain the change during the period in the total cash, cash equivalents and amounts generally described as restricted cash and 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. This accounting standard is effective for fiscal years beginning after December 15, 2017. The Foundation adopted the new accounting standards on January 1, 2018.

In January 2017, FASB issued ASU 2017-04, *Intangibles – Goodwill and Other: Simplifying the Test for Goodwill Impairment*. Under the new accounting standard, an organization should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An impairment charge will be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value. However, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. This accounting standard is effective for fiscal years beginning after December 15, 2020. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Foundation adopted the new accounting standard on January 1, 2017.

In June 2018, FASB issued ASU 2018-08, *Not-For-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. ASU 2018-08 provides guidance to clarify and improve the scope and the accounting guidance for contributions received and contributions made. The amendments in this Update should assist entities in (1) evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) within the scope of Topic 958, Not-for-Profit Entities, or as exchange (reciprocal) transactions subject to other guidance and (2) determining whether a contribution is conditional. The new standard will be effective for fiscal years beginning after December 15, 2018.

In August 2018, FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*. ASU 2018-13 modifies the disclosure requirements on fair value measurements in Topic 820, Fair Value Measurement, based on the concepts in the Concepts Statement, including the consideration of costs and benefits. The new standard will be effective for fiscal years beginning after December 15, 2019.

NOTE 1 DESCRIPTION OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New Accounting Pronouncements (continued)

In August 2018, FASB issued ASU 2018-15, *Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*. ASU 2018-15 helps entities evaluate the accounting for fees paid by a customer in a cloud computing arrangement (hosting arrangement) by providing guidance for determining when the arrangement includes a software license. The new standard will be effective for fiscal years beginning after December 15, 2020.

NOTE 2 NET PATIENT SERVICE REVENUE

The Foundation has agreements with third party payers that provide for payments to the Foundation at amounts that vary from its established rates. The difference between charges and the related payment amount for the years ended December 31 is reflected below:

	2018	2017
Gross patient service revenue	\$ 30,342,308	\$ 26,089,056
Contractual discounts and provision for bad debts	(22,081,464)	(16,777,181)
Net patient service revenue	\$ 8,260,844	\$ 9,311,874

A summary of the payment arrangements with major third-party payers follows:

Medi-Cal and Medicaid

The Medi-Cal and Medicaid programs accounted for approximately 18% and 7% of consolidated net patient service revenue in 2018 and 2017, respectively. Outpatient services rendered to Medi-Cal and Medicaid program beneficiaries are paid at prospectively determined rates for outpatient care.

Medicare

The Medicare program accounted for approximately 17% and 11% of consolidated net patient service revenue in 2018 and 2017, respectively. Healthcare services rendered to Medicare program beneficiaries are paid at prospectively determined rates for outpatient care. These rates vary according to a patient classification system that is based on clinical, diagnostic, and other factors.

Other Third-party Payers

The Foundation has also entered into payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations. These payers accounted for approximately 65% and 82% of consolidated net patient service revenue in 2018 and 2017, respectively. The basis for payment to the Foundation under these agreements includes, among others, discounts from established charges, and prospectively determined daily rates.

NOTE 3 PREMIUMS

Positive Healthcare

California Medicaid Primary Care Case Management (PCCM)

In April 1995, the Foundation contracted with the California Department of Health Care Services (DHCS) to provide capitated HIV healthcare to Medi-Cal beneficiaries. The capitated plan is known as Positive Healthcare (the Plan). Positive Healthcare has a comprehensive network of providers and offers the following contracted services: primary medical care, specialty consultation, outpatient services, pharmaceuticals, hospice, and long-term facility care to voluntary members of the plan. DHCS compensates the Foundation on a per member per month (PMPM) capitated basis. Acute inpatient services for members of the plan are the fiscal responsibility of DHCS.

Membership contracts with DHCS are on a monthly basis subject to cancellation by the DHCS or the member based on loss of Medi-Cal benefits, dissatisfaction with the program, death, relocation, or incarceration. Premiums are due monthly and are recognized as revenue during the period in which Positive Healthcare is obligated to provide services to members. As part of the contract, the Foundation and DHCS share net savings between the costs of providing services on an inpatient fee-for-service basis compared to the Foundation's plan experience.

The Foundation had a savings sharing and rate dispute with DHCS. In December 2017, the Foundation entered into a Settlement Agreement with DHCS whereby the Foundation agreed to pay DHCS \$624,103 in full and final settlement of all claims arising from and related to the 2009, 2010 and 2012 capitation rates, the 2007 to 2009 savings sharing calculation and prescription drugs approved by the Federal Drug Administration after January 1, 2007. In addition, the Foundation and DHCS agreed that all rates paid to the Foundation for the service periods through and including December 31, 2017 are deemed final rates, regardless of the status of formal notification, issuance of change orders or whether the rates were designated as preliminary or final rates.

The cost of health care services provided or contracted for is accrued in the period in which it is provided to a member based in part on estimates, including an accrual for medical services provided but not yet reported to the Foundation as of year-end.

Florida Medicaid HMO

In May 2010, AHF MCO of Florida, Inc. (AHF MCO) contracted with State of Florida Agency for Health Care Administration (FL AHCA) to provide Medicaid managed care services as Positive Healthcare to Medicaid beneficiaries living with a diagnosis of HIV/AIDS in Broward County. In September 2012, AHF MCO contracted with State of Florida AHCA to provide similar services in Dade County. In January 2014, FL AHCA and AHF MCO entered into a new contract to provide similar HMO services to Medicaid beneficiaries.

Beginning on July 1, 2014, Positive Healthcare began serving Medicaid beneficiaries in Broward, Dade and Monroe Counties. Positive Healthcare has a comprehensive network of contracted providers and offers the full range of Medicaid benefits, including contracted services: primary medical care, specialty consultation, outpatient services, pharmaceuticals and hospitalization. FL AHCA compensates the Foundation on a per member per month (PMPM) capitated basis, based on each member's diagnosis.

NOTE 3 PREMIUMS (CONTINUED)

Florida Medicaid HMO

Enrollment in this HMO is voluntary and subject to cancellation by FL AHCA or the member based on loss of Medicare benefits, dissatisfaction with the program, death, relocation, or incarceration. Premiums are due monthly and are recognized as revenue during the period in which Positive Healthcare is obligated to provide services to members.

The cost of health care services provided or contracted for is accrued in the period in which it is provided to a member based in part on estimates, including an accrual for medical services provided but not yet reported to the Foundation as of year-end.

As of February 2019, the Florida Medicaid HMO has been discontinued. The Foundation will continue to pay claims on a run-off basis. The Foundation does not expect the discontinuance to have a material financial impact.

Positive Healthcare Partners

California Medicare HMO, Florida Medicare HMO and Georgia Medicare HMO

In January 2006, the Foundation contracted with the Centers for Medicare and Medicaid Services (CMS) to provide a Medicare Advantage Part D Special Needs Plan to Medicare beneficiaries living with a diagnosis of HIV/AIDS in Los Angeles County. The Foundation established a California HMO to provide these services known as Positive Healthcare Partners. In January 2008, the Foundation contracted with CMS to provide a Medicare Advantage Part D Special Needs Plan to Medicare beneficiaries living with a diagnosis of HIV/AIDS in Broward and Dade Counties. The Foundation established an HMO to provide these services known as Positive Healthcare Partners. In April 2017, the Foundation received the Certificate of Authority from the State of Georgia Office of Commissioner of Insurance. In August 2017, the Foundation contracted with CMS to provide a Medicare Advantage Part D Special Needs Plan to Medicare beneficiaries living with a diagnosis of HIV/AIDS in Fulton County. The Plan began operations on January 1, 2018.

These HMOs have a comprehensive network of contracted providers and offers the full range of traditional Medicare Parts A, B, and D benefits, including the following contracted services: primary medical care, specialty consultation, outpatient services, pharmaceuticals, hospice, hospitalization, rehabilitation services, behavioral health and skilled nursing facility care to voluntary members of the plan. CMS compensates the Foundation on a per member per month (PMPM) capitated basis, based on each member's risk scoring as outlined in Medicare Advantage Risk Adjustment Policies.

Enrollment in these HMOs is voluntary and subject to cancellation by CMS or the member based on loss of Medicare benefits, dissatisfaction with the program, death, relocation, or incarceration. Premiums are due monthly and are recognized as revenue during the period in which Positive Healthcare Partners is obligated to provide services to members.

The cost of health care services provided or contracted for is accrued in the period in which it is provided to a member based in part on estimates, including an accrual for medical services provided but not yet reported to the Foundation as of year-end.

NOTE 3 PREMIUMS (CONTINUED)

Project AIDS Care (PAC)

The Foundation is contracted with the State of Florida Agency of Health Care Administration to provide services related to Project AIDS Care (PAC) Waiver Program. The program ended December 31, 2017. The amount recorded in 2018 were residual amounts due to the Foundation.

The net premiums earned under the above programs for the years ended December 31, 2018 and 2017 are as follows:

	2018	2017
Positive Healthcare Partners - Medicare (Florida) \$	88,469,321	\$ 79,491,275
Positive Healthcare - Medicaid (Florida)	50,652,919	55,184,841
Positive Healthcare Partners - Medicare (California)	42,797,668	43,038,781
Positive Healthcare - Medi-Cal (California)	12,137,898	14,064,229
Positive Healthcare Partners - Medicare (Georgia)	248,082	-
Project AIDS Care (Florida)	51,373	207,142
Net premiums earned	\$ 194,357,261	\$ 191,986,268

NOTE 4 GRANT REVENUE

Los Angeles County

Los Angeles County (the County) reimburses the Foundation for services provided to eligible beneficiaries that reside within the County. The County program accounted for approximately 13% and 14% of consolidated grant revenues in 2018 and 2017, respectively. For outpatient services, the Foundation is reimbursed at a contracted rate with final settlement determined after submission of annual cost reports by the Foundation and audits thereof by the County. The Foundation's County cost reports have been reviewed and settled with the County through February 2018.

Other Counties

Other significant grant revenue sources were generated from affiliates, ACQC and AID Atlanta. For the years ended December 31, 2018 and 2017, ACQC grant revenue accounted for 23% and 26%, respectively while AID Atlanta accounted for 13% and 13%, respectively, of consolidated grant revenues.

AIDS Healthcare Foundation
Notes to the Consolidated Financial Statements
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NOTE 5 AVAILABILITY AND LIQUIDITY

At December 31, the following represents the Foundation's financial assets:

Financial assets	<u>2018</u>	<u>2017</u>
Cash and cash equivalents	\$ 70,228,387	\$ 32,620,381
Accounts Receivable	86,604,343	80,576,388
Investments	<u>91,133,473</u>	<u>135,824,765</u>
Total financial assets	247,966,203	249,021,534
Less amounts not available to be used within one year:		
Long-term investments	(68,510,128)	(117,387,453)
Net assets with donor restrictions	357,556	303,652
Less net assets with purposes restrictions to be met in less than a year	<u>(357,556)</u>	<u>(303,652)</u>
Financial assets available to meet general expenditures over the next twelve months	\$ <u>179,456,075</u>	\$ <u>131,634,081</u>

As part of the Foundation's liquidity plan, the Foundation invests excess cash in short and long-term investments, including money market accounts, fixed income and equity securities. The Foundation has a \$30 million line of credit available to meet cash flow needs.

NOTE 6 INVENTORIES

At December 31, inventories consist of:

	<u>2018</u>	<u>2017</u>
Pharmacy drugs	\$ 31,027,103	\$ 26,480,809
Test kits inventory	1,686,231	2,325,674
Thrift store inventory	1,239,092	1,238,825
Condoms	<u>1,028,004</u>	<u>798,026</u>
	\$ <u>34,980,430</u>	\$ <u>30,843,334</u>

NOTE 7 ASSETS LIMITED AS TO USE

At December 31, the composition of assets limited as to use is set forth in the following table:

	2018	2017
Restricted deposits:		
Cash deposit held as collateral for Georgia Medicare HMO contract	\$ 3,000,000	\$ 3,000,000
Cash deposit held by the State of Georgia for Georgia Medicare HMO contract	1,000,000	1,000,000
Money market account restricted for Florida PHC	2,187,753	2,187,753
Cash deposits held by the State of Florida for Florida Medicare HMO contract	300,000	300,000
Money market mutual funds restricted for California Medicare HMO contract	340,358	340,358
Total assets limited as to use	\$ <u>6,828,111</u>	\$ <u>6,828,111</u>

NOTE 8 INVESTMENTS

At December 31, investments consist of:

	2018	2017
Short-term investments	\$ 12,643,285	\$ 18,437,312
Public equity	16,216,143	27,810,198
Fixed income	51,488,857	75,178,467
Hedge funds	514,331	2,636,863
Private equity	6,190,891	6,713,862
Asset allocation	1,542,440	3,547,113
Venture capital	2,537,526	1,500,950
	91,133,473	135,824,765
Less short-term portion	(22,623,345)	(18,437,312)
Long-term investments	\$ <u>68,510,128</u>	\$ <u>117,387,453</u>

AIDS Healthcare Foundation
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NOTE 8 INVESTMENTS (CONTINUED)

The following table sets forth by level within the fair value hierarchy, the Foundation's investments at fair value as of December 31, 2018:

	Fair Value Measurements at December 31, 2018 Using			Total
	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Short-term investments	\$ 12,643,284	\$ -	\$ -	\$ 12,643,284
Public equity				
Domestic	9,762,826	-	-	9,762,826
International	6,453,317	-	-	6,453,317
Fixed income	51,488,857	-	-	51,488,857
Hedge funds	-	514,331	-	514,331
Private equity	-	3,533,708	2,657,183	6,190,891
Asset allocation	1,542,440	-	-	1,542,440
Venture capital	-	-	2,537,527	2,537,527
Total	<u>\$ 81,890,724</u>	<u>\$ 4,048,039</u>	<u>\$ 5,194,710</u>	<u>\$ 91,133,473</u>

The following table sets forth by level within the fair value hierarchy, the Foundation's investments at fair value as of December 31, 2017:

	Fair Value Measurements at December 31, 2017 Using			Total
	Quoted Prices In Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Short-term investments	\$ 18,437,312	\$ -	\$ -	\$ 18,437,312
Public equity				
Domestic	20,215,172	-	-	20,215,172
International	7,595,026	-	-	7,595,026
Fixed income	75,178,467	-	-	75,178,467
Hedge funds	959,696	1,663,130	14,037	2,636,863
Private equity	-	4,307,375	2,406,487	6,713,862
Asset allocation	3,547,113	-	-	3,547,113
Venture capital	-	-	1,500,950	1,500,950
Total	<u>\$ 125,932,786</u>	<u>\$ 5,970,505</u>	<u>\$ 3,921,474</u>	<u>\$ 135,824,765</u>

The Foundation utilizes an external investment advisor to oversee the valuation process of the Foundation's Level 3 investments. The advisor is responsible for approving the valuation processes and procedures, conducting periodic reviews of the valuation policies, and evaluating the overall fairness and consistent application of the valuation policies. These valuations are required to be supported by market data, third-party pricing sources, industry accepted pricing models, counterparty prices, or other methods the advisor deems to be appropriate, including the use of internal proprietary pricing models.

AIDS Healthcare Foundation
Notes to the Consolidated Financial Statements
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NOTE 8 INVESTMENTS (CONTINUED)

A reconciliation of investments in which significant unobservable inputs (Level 3) for the years ended December 31, 2018 and 2017 were used in determining fair value is as follows:

	<u>2018</u>	<u>2017</u>
Level 3 investments, beginning of year	\$ 3,921,474	3,140,468
Increase in unrealized appreciation on investments	250,696	59,052
Purchases	1,036,577	950,000
Dispositions	(14,037)	(228,046)
Level 3 investments, end of year	\$ <u>5,194,710</u>	\$ <u>3,921,474</u>
Increase in unrealized appreciation on investments for the year relating to Level 3 investments held at December 31	\$ <u>250,696</u>	\$ <u>36,098</u>

NOTE 9 PROPERTY AND EQUIPMENT

At December 31, property and equipment is composed of:

	<u>2018</u>	<u>2017</u>
Land	\$ 72,626,845	\$ 48,881,045
Buildings	78,073,790	49,785,579
Leasehold improvements	25,084,428	23,108,933
Furniture and fixtures	8,421,856	7,746,521
General equipment	22,793,220	18,295,774
Vehicles	9,440,474	8,228,645
Computer software	19,627,549	18,454,552
Computer equipment	19,953,348	18,082,015
Low value assets	1,510,638	1,392,056
Assets under construction	9,770,709	5,822,544
Total	<u>267,302,857</u>	<u>199,797,664</u>
Accumulated depreciation and amortization	<u>(74,324,823)</u>	<u>(61,370,873)</u>
Property and equipment, net	\$ <u>192,978,034</u>	\$ <u>138,426,791</u>

Provision for depreciation and amortization of property and equipment amounted to \$13,415,299 and \$11,564,866 in 2018 and 2017, respectively.

Real Estate Properties at Fair Value

During 2018 (except for Baltimore Hotel property which was appraised in 2019), the Foundation had several land and buildings (properties) appraised to determine the properties' current fair value. Five properties with a book value of \$24,592,622 as of December 31, 2018, have not been appraised including two in the United States and three in Kenya and Uganda.

AIDS Healthcare Foundation
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NOTE 9 PROPERTY AND EQUIPMENT (CONTINUED)

Real Estate Properties at Fair Value (Continued)

The schedule below summarizes the comparison of the net book value of the properties at December 31, 2018 with the appraised fair values:

Location	State	Appraisal Date	Net Book Value	Fair Value
Carl Bean - 2146 W. Adams Blvd	CA	7/31/2018	\$ 3,002,816	\$ 7,900,000
Linn House - 1001 Martel Ave	CA	7/31/2018	3,767,607	11,600,000
Condo - 6735 Yucca St #411	CA	8/1/2018	662,056	795,000
6500 Sunset Blvd	CA	7/31/2018	5,912,211	8,000,000
PHD 1710 N. La Brea Ave/1725 El Cerritto Ave	CA	7/31/2018	5,837,251	7,475,000
Atwater - 3160 Glendale Blvd	CA	8/1/2018	2,391,875	3,450,000
Madison - 423 & 427 East 7th St	CA	7/31/2018	9,507,444	13,250,000
SOS 6516 Sunset Blvd	CA	7/31/2018	4,917,589	4,610,000
King Edward 121 E. 5th St	CA	7/31/2018	16,239,527	11,150,000
501 S. Los Angeles St (Baltimore Hotel)	CA	3/29/2019	21,101,179	21,500,000
2601 34th St	FL	9/18/2018	3,877,763	3,100,000
2097 Wilton Dr	FL	9/14/2018	1,724,811	1,850,000
700 & 750 SE 3rd Ave	FL	9/5/2018	10,702,937	11,400,000
1785 Sunrise Blvd	FL	9/14/2018	2,251,690	2,280,000
229/237 NE 24th St	FL	9/15/2018	1,712,607	2,200,000
2900 Biscayne Blvd	FL	9/14/2018	4,800,594	6,240,000
4300 Bayou Blvd Pensacola	FL	8/31/2018	858,176	850,000
1349 N. Mills Ave Orlando	FL	9/5/2018	2,235,850	2,300,000
2400 Biscayne Blvd	FL	9/14/2018	7,119,493	9,100,000
16800 NW 22nd Blvd	FL	9/10/2018	7,278,936	6,050,000
409/411/501/505 SE 8th Ave	FL	9/5/2018	3,697,661	7,000,000
2125 Illinois/2231 McGregor Ft. Myers	FL	8/31/2018	387,816	915,000
735 Piedmont Ave NE	GA	10/1/2018	1,935,684	1,825,000
1220 High St	OH	8/6/2011	4,184,441	3,700,000
			<u>\$ 126,108,013</u>	<u>\$ 148,540,000</u>

The appraised values of the real estate properties have been prepared giving consideration to the income capitalization and sales comparison approaches of estimating property value.

Under the income capitalization approach, the anticipated future benefits or income stream is capitalized and/or discounted to its present value to estimate fair value. This is accomplished by either direct capitalization or yield capitalization (discounted cash flow analysis).

NOTE 9 PROPERTY AND EQUIPMENT (CONTINUED)

Real Estate Properties at Fair Value (Continued)

Direct capitalization analysis uses a single year's net operating income divided by an appropriate capitalization rate to estimate value. Yield capitalization or discounted cash flow analysis uses several future years of net operating income, with reversion, discounted by an appropriate yield rate. The sales comparison approach compares recent transactions to the appraised property. Adjustments are made for conditions of sale, property rights, financing, market conditions, locations and physical differences. This approach is highly dependent on an active sales market with an adequate amount of comparable sales data.

Since the resulting valuation are based on estimates, the appraised values reflected in the schedule above can materially differ from the values that would be determined by negotiations held between parties in a sales transaction.

NOTE 10 CLAIMS PAYABLE

Claims payable is reviewed periodically, with any necessary adjustments reflected during the current period in the results of operations. While the ultimate amount of claims payable and related expenses are dependent on future developments, it is management's opinion that the liability that has been established is adequate to cover such costs.

The summary of changes in claims payable for the years ended December 31, 2018 and 2017 is as follows:

	2018	2017
Claims payable at beginning of year	\$ 17,618,697	\$ 25,269,225
Incurred hospital and medical services claims:		
Current year	204,869,888	191,196,237
Prior years	(5,599,475)	(7,388,135)
Total incurred	199,270,412	183,808,102
Paid hospital and medical services claims:		
Current year	(184,430,348)	(174,680,121)
Prior years	(10,235,140)	(16,778,509)
Total paid	(194,665,489)	(191,458,630)
Claims payable at end of year	\$ 22,223,621	\$ 17,618,697

As of December 31, 2018, and 2017, the liability for unpaid claims and claims adjustment expenses was \$22,223,621 and \$17,618,697, respectively. The estimated ultimate claims and claims adjustment expenses incurred decreased by approximately \$5.6 million related to prior years. The decrease is generally the result of ongoing analysis of recent claim payments and claim development trends. Original estimates are increased or decreased as additional information becomes known regarding individual claims.

AIDS Healthcare Foundation
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NOTE 11 LINE OF CREDIT

The Foundation has a line of credit agreement with a bank, expiring on May 16, 2019, that provides for secured borrowings up to \$30 million, at a rate per annum equal to the LIBOR plus 2%. There was no outstanding balance on the line of credit as of December 31, 2018 and 2017. The Foundation is subject to certain financial covenants relating to net assets, net income, and a specified debt ratio.

NOTE 12 LONG-TERM DEBT

At December 31, long-term debt consists of:

	2018	2017
Wells Fargo Public Financing Authority Bond of \$18,746,162 bearing interest at 3.46% per annum compounded annually on the outstanding balance. Principal and interest is payable on the 1st of each month commencing April 2015 with the final installment consisting of all remaining unpaid principal due and payable in full on March 1, 2034.	\$ 15,115,750	\$ 16,487,460
Wells Fargo Equipment Loan of \$2,027,979 bearing interest at 4.39% per annum compounded annually on the outstanding balance. Monthly principal and interest payments of \$37,706 are due on the 1st of each month commencing April 15, 2014 with a final installment due and payable on March 15, 2019.	112,296	549,379
Wells Fargo Term Note (Term Note) of \$10,000,000 bearing interest at 4% above LIBOR per annum compounded annually on the outstanding balance. Principal and interest is payable on the 1st of each month commencing December 2014 in installments of \$119,048 through October 1, 2021, with a final installment consisting of all remaining unpaid principal due and payable in full on October 8, 2021.	4,166,667	5,595,238
Wells Fargo Series A Loan of \$19,435,000 bearing a variable interest rate per annum compounded monthly on the outstanding balance. Principal is payable on the 1st of each month commencing in February 2022, with the final installment consisting of all remaining unpaid principal due and payable in full on January 1, 2039.	19,435,000	-
Wells Fargo Series B Loan of \$2,495,000 bearing a variable interest rate per annum compounded monthly on the outstanding balance. Principal is payable on the 1st of each month commencing in February 2019, with the final installment consisting of all remaining unpaid principal due and payable in full on January 1, 2023.	2,495,000	-
	41,324,713	22,632,077
Current portion	(2,948,538)	(2,616,154)
Noncurrent portion	38,376,175	20,015,923
Less: debt issuance costs	(617,129)	(492,526)
Long-term debt	\$ 37,759,046	\$ 19,523,397

NOTE 12 LONG-TERM DEBT (CONTINUED)

Scheduled annual principal maturities of long-term debt, net of debt issuance costs, are as follows:

Year ending December 31	Amount
2019	\$ 2,948,538
2020	2,976,275
2021	2,869,746
2022	1,626,010
2023	1,697,826
Thereafter	28,589,190
Total \$	40,707,584

Wells Fargo PFA Bond

In March 2014, the Foundation extinguished all its outstanding debt as of December 31, 2013 by obtaining new loan agreements with Wells Fargo. The new loans have maturity dates ranging from two and half (2.5) to seven (7) years and bear interest ranging from 3.9% to 4.61% per annum. The new loans are collateralized by the Foundation's assets, including without limitation, accounts receivables and other rights to payment, general intangibles, inventories, equipment and fixtures, equity interest in all of its Subsidiaries, and a lien of first priority on certain real property described in the loan agreement.

On February 6, 2015, the Foundation and Wells Fargo amended the new loan agreements to delete AHF MCO of Florida, Inc.'s name from the list of guarantors.

In March 2015, the Foundation entered into agreements with Wells Fargo and the Public Finance Authority (PFA). Under the terms of the agreements, PFA issued the \$18.7 million Public Finance Authority Revenue Bonds (AIDS Healthcare Foundation Project), Series 2015, pursuant to the terms of the Indenture of Trust dated March 1, 2015 between PFA and Wells Fargo. Wells Fargo loaned the proceeds of the Bonds to the Foundation. The Foundation used the proceeds to refinance a portion of its existing debt and to pay certain costs incurred in connection with the issuance of the Bonds.

On March 14, 2017, the Foundation and Wells Fargo amended the above loan agreement and the line of credit (see Note 11). The amended and restated agreements provide for, among other terms, the increase in allowed value of permitted acquisitions, provision of a borrowing base certificate, and extension of the line of credit to May 16, 2019.

On December 20, 2018, the Foundation entered into agreements with Wells Fargo for the issuance of Series 2018A (\$19.4 million) and Series 2018B (\$2.5 million) loans. The Foundation intends to use the loan proceeds for the financing and refinancing of the acquisition, construction, improvement and operation of the Foundation's low-income housing projects.

AIDS Healthcare Foundation
Notes to the Consolidated Financial Statements
Years ended December 31, 2018 and 2017

NOTE 13 INTEREST RATE SWAP AGREEMENTS

The Foundation executed interest rate swap agreements with Wells Fargo Bank to manage debt service costs on its variable rate long-term debt by achieving a synthetic fixed rate payment in the swap counterparty and receiving a variable rate payment from the swap counterparty that effectively offsets the payment on the underlying variable rate debt.

The details of the swap agreements for the year ended December 31, 2018 are as follows:

	Public Finance		Series A	Series B
	Bond	Term Note	Loan	Loan
Outstanding notional amount	\$ 15,115,750	\$ 4,166,667	\$ 19,435,000	\$ 2,495,000
Fixed interest rate	2.16%	1.86%	2.641%	2.815%
Floating rate option	70% of USD-Libor-BBA	USD-Libor-BBA	80.375% of USD-Libor-BBA	USD-Libor-BBA
Floating rate day count fraction	Actual/360	Actual/360	Actual/360	Actual/360
Trade date	3/17/2014	10/8/2014	12/20/2018	12/20/2018
Effective date	3/17/2014	10/8/2014	12/20/2018	12/20/2018
Termination date	3/17/2021	10/8/2021	12/1/2028	12/1/2021

At December 31, 2018 and 2017, the fair value of the swap liability was \$354,345 and \$164,186, respectively. The fair values were the quoted market prices at December 31 of each year. The swap counterparty was rated A+ by Standard & Poor's as of December 31 of each year.

NOTE 14 NET ASSETS WITH DONOR RESTRICTIONS

At December 31, net assets with donor restrictions that are available for future periods are as follows:

	<u>2018</u>	<u>2017</u>
Housing	\$ 9,400	\$ 78,069
Program support	<u>348,156</u>	<u>225,583</u>
Total	<u>\$ 357,556</u>	<u>\$ 303,652</u>

NOTE 15 BUSINESS AND ASSET ACQUISITIONS

In 2017, the Foundation acquired one pharmacy, located in Astoria, NY. Intangibles totaling \$3,500,000 was recognized as a result of this acquisition.

In 2017, the Foundation acquired two practices, located in New York, NY. Goodwill totaling \$603,844 was recognized as a result of these acquisitions.

Supplemental disclosure of investing and financing activities

In connection with the above business and asset acquisitions, the Foundation expended cash of \$0 in 2018 and \$3,500,000 in 2017.

NOTE 16 EMPLOYEE RETIREMENT PLAN

The Foundation sponsors a defined contribution retirement plan under Section 401(k) of the Internal Revenue Code: AHF Savings and Investment Plan (the Plan). All classes of employees, except for per diem and temporary employees, are eligible to participate in the Plan. An employee is eligible for participation in the months following 90 days from the date of employment. The Plan is subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA). The Plan is administered by the employer and all contributions are held in accounts maintained by the Plan custodian.

Each year, participants may contribute pre-tax annual compensation as defined in the Plan, subject to certain limitations, with the contributions and earnings thereon being nontaxable until withdrawn from the Plan. Participants may also contribute amounts representing distributions from other qualified defined benefit or contribution plans. The Foundation may contribute up to \$5,000 per participant depending on the number of years of service. The Foundation's matching contribution expense for the years ended December 31, 2018 and 2017 amounted to \$3,926,977 and \$2,921,890, respectively.

NOTE 17 CONCENTRATIONS OF CREDIT RISK

a) The Foundation grants credit without collateral to its patients and patients insured under third-party agreements. At December 31, the mix of receivables from patients, third-party payers and grants was as follows:

	2018	2017
Private Insurance	56.76%	56.77%
AIDS Drug Assistance Program	7.73%	7.38%
Department of Health and Human Services	5.13%	12.63%
Other Grants	19.29%	15.70%
Medi-Cal/Medicaid	2.42%	3.45%
Centers for Medicare and Medicaid Services	8.35%	3.72%
Agency for Health Care Administration	0.15%	0.28%
Medicare (Fee for Service)	0.18%	0.07%
Total	100.00%	100.00%

b) The Foundation maintains its cash accounts at banks and financial institutions located in the United States and other countries. Bank accounts in other countries are subject to rules and regulations in the respective countries and amounts insured vary accordingly. At times, cash and cash equivalent balances at certain banks and financial institutions may exceed insurable amounts. The Foundation believes it mitigates this risk by monitoring the financial stability of institutions holding material cash balances.

NOTE 18 COMMITMENTS AND CONTINGENCIES

Operating Leases

The Foundation leases certain equipment and facilities under non-cancelable operating lease agreements expiring at various dates through June 2027. Total rental expense for all operating leases was \$16,197,051 and \$16,060,116 in 2018 and 2017, respectively.

NOTE 18 COMMITMENTS AND CONTINGENCIES

Operating Leases (continued)

The following is a schedule of future minimum lease payments under operating leases as of December 31, 2018 that have initial or remaining lease terms in excess of one year:

Year ending December 31	Amount
2019	\$ 8,930,105
2020	7,824,945
2021	7,099,471
2022	5,797,351
2023	3,471,177
Thereafter	5,474,726
Total	\$ 38,597,775

Insurance Coverages

The Foundation maintains claims-made medical malpractice insurance for up to \$3,000,000 per occurrence and general liability insurance for up to \$1,000,000 per occurrence and \$3,000,000 annual aggregate. The Foundation also maintains such other insurance policies as management has deemed prudent and necessary, including property, directors' and officers' liability, employment practices liability, flood insurance, errors and omissions, and crime.

Litigation

The Foundation is involved in litigation arising from the normal course of business. After consultation with legal counsel, management estimates that these matters will be resolved without material effect on the Foundation's financial position.

Government Regulation

The Foundation is subject to extensive regulation by numerous governmental authorities, including federal, state, and local jurisdictions. Although the Foundation believes that it is currently in compliance with applicable laws, regulations, and rules, some of such laws are broadly written and subject to interpretation by courts or administrative authorities. Specifically, in the health care industry, government agencies have recently focused considerable attention and resources to the detection and prosecution of fraudulent activities under Medicare and Medicaid program regulations.

While the Foundation believes that it is in compliance with applicable regulations, there can be no assurance that a third party, governmental agency, or private party will not contend that certain aspects of the Foundation's operations or procedures are subject to, or are not in compliance with such laws, regulations, or rules or that the state or federal regulatory agencies or courts would interpret such laws, regulations, and rules in the Foundation's favor. The sanctions for failure to comply with such laws, regulations, or rules could include exclusion from the Medicare and Medicaid programs, significant fines, and criminal penalties.

NOTE 18 COMMITMENTS AND CONTINGENCIES (CONTINUED)

Government Regulation (continued)

The Foundation participates in a number of federally funded grant programs. These programs are subject to program compliance audits by the grantors or their representatives. The Foundation has received a final report for contract year 2008/2009 from the Los Angeles (LA) County Auditor Controller identifying a potential disallowance of \$1.7 million of claimed costs. In addition, the Foundation has received a final report for contract years 2011/2012 and 2012/2013 from the LA County Auditor Controller identifying potential disallowance of \$3.5 million of claimed costs. This dispute was the subject of a lawsuit that was dismissed in May 2017. LA County has nonetheless requested payment from the Foundation of approximately \$5.2 million to compensate it for payments it made to the federal government. The Foundation disputes it received any amounts in violation of federal law or that any repayments are owed by it to LA County. This case was settled in January 2019 with the Foundation agreeing to provide \$5.03 million worth of in-kind HIV and STD services to the benefit of the County over a four year period.

NOTE 19 CHARITY CARE

The Foundation provides care to patients who meet certain criteria under its charity care policy. The Foundation determines costs associated with providing charity care by aggregating the applicable direct and indirect costs, including salaries, wages and benefits, supplies and other operating expenses based on data from its accounting system. The costs of caring for charity care patients for the years ended December 31, 2018 and 2017 amounted to \$74,331,704 and \$63,135,560, respectively. Funds received from gifts and grants to subsidize charity services provided for the years ended December 31, 2018 and 2017 amounted to \$2,296,257 and \$1,360,385, respectively.

NOTE 20 SUBSEQUENT EVENTS

The Foundation has evaluated events or transactions that occurred subsequent to the balance sheet date through April 30, 2019, the date the accompanying financial statements were available to be issued, for potential recognition or disclosure in the financial statements and determined that no subsequent matters required disclosure or adjustment to the accompanying consolidated financial statements.

**Report of Independent Auditors on Internal Control Over Financial Reporting and
on Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance With *Government Auditing Standards***

**Board of Directors
AIDS Healthcare Foundation**

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 consolidated financial statements of AIDS Healthcare Foundation, which comprise the consolidated balance sheet as of December 31, 2018, and the related consolidated statements of operations and changes in net assets, functional expenses and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated April 30, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered AIDS Healthcare Foundation'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 opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of AIDS Healthcare Foundation's internal control. Accordingly, we do not express an opinion on the effectiveness of AIDS Healthcare Foundation'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.



Compliance and Other Matters

As part of obtaining reasonable assurance about whether AIDS Healthcare Foundation's consolidated 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 consolidated 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* when considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Vaqueria & Company LLP". The signature is written in a cursive, flowing style.

**Glendale, California
April 30, 2019**

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