

THE HILL CENTER, INC.

Financial Statements

June 30, 2017 and 2016

CONTENTS

| | |
|-----------------------------------|---------|
| INDEPENDENT AUDITORS' REPORT | 1 - 2 |
| FINANCIAL STATEMENTS | |
| Statements of Financial Position | 3 - 6 |
| Statements of Activities | 7 - 8 |
| Statements of Functional Expenses | 9 -10 |
| Statements of Cash Flows | 11 |
| NOTES TO FINANCIAL STATEMENTS | 12 - 25 |

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees
The Hill Center, Inc.
Durham, North Carolina

We have audited the accompanying financial statements of The Hill Center, Inc. (a nonprofit organization), which comprise the statements of financial position as of June 30, 2017 and 2016, and the related statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the 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 The Hill Center, Inc. as of June 30, 2017 and 2016, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 1 to the financial statements, The Hill Center, Inc. has retroactively adopted the Financial Accounting Standards Board's accounting policies related to investments measured using net asset value per share as a practical expedient and investment disclosures. Our opinion is not modified with respect to that matter.

Thomas, Judy & Dicks, P.A.

August 28, 2017

THE HILL CENTER, INC.
STATEMENTS OF FINANCIAL POSITION
June 30, 2017 and 2016

| | 2017 | | | Total |
|--|----------------------|---------------------------|---------------------------|----------------------|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | |
| <u>ASSETS</u> | | | | |
| Current Assets: | | | | |
| Cash and Cash Equivalents | \$ 1,022,883 | \$ 1,321,579 | \$ 920 | \$ 2,345,382 |
| Tuition Receivable - Net of Allowance for Doubtful Accounts of \$16,000 in 2017 and 2016 | 150,197 | | | 150,197 |
| Other Accounts Receivable | 30,344 | | | 30,344 |
| Prepaid Expenses | 80,781 | | | 80,781 |
| Pledges Receivable - Current | 107,100 | 198,530 | | 305,630 |
| Investments | 2,005,805 | 2,403,279 | 5,943,523 | 10,352,607 |
| Total Current Assets | 3,397,110 | 3,923,388 | 5,944,443 | 13,264,941 |
| Property and Equipment: | | | | |
| Land | 201,331 | | | 201,331 |
| Land Improvements | 50,000 | | | 50,000 |
| Building and Improvements | 9,207,579 | | | 9,207,579 |
| Equipment | 1,441,970 | | | 1,441,970 |
| Furniture and Fixtures | 276,741 | | | 276,741 |
| Software | 116,689 | | | 116,689 |
| Work in Progress | 11,294,310 | | | 11,294,310 |
| Less Accumulated Depreciation | 4,135,017 | | | 4,135,017 |
| Net Property and Equipment | 7,159,293 | | | 7,159,293 |
| Other Assets: | | | | |
| Pledges Receivable - Long Term Portion, Net of Allowance for Doubtful Accounts of \$2,594 in 2017 and \$4,284 in 2016 | | 49,277 | | 49,277 |
| Total Other Assets | | 49,277 | | 49,277 |
| Total Assets | \$ 10,556,403 | \$ 3,972,665 | \$ 5,944,443 | \$ 20,473,511 |

2016

| <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Total</u> |
|----------------------|-----------------------------------|-----------------------------------|----------------------|
| \$ 1,017,736 | \$ 633,638 | \$ 775 | \$ 1,652,149 |
| 125,099 | | | 125,099 |
| 32,248 | | | 32,248 |
| 87,392 | | | 87,392 |
| 479,808 | 387,002 | | 866,810 |
| <u>1,772,345</u> | <u>1,933,344</u> | <u>5,908,518</u> | <u>9,614,207</u> |
| <u>3,514,628</u> | <u>2,953,984</u> | <u>5,909,293</u> | <u>12,377,905</u> |
| 201,331 | | | 201,331 |
| 50,000 | | | 50,000 |
| 9,207,579 | | | 9,207,579 |
| 1,441,970 | | | 1,441,970 |
| 276,741 | | | 276,741 |
| <u>979,037</u> | | | <u>979,037</u> |
| <u>12,156,658</u> | | | <u>12,156,658</u> |
| <u>3,727,002</u> | | | <u>3,727,002</u> |
| <u>8,429,656</u> | | | <u>8,429,656</u> |
| | <u>101,398</u> | | <u>101,398</u> |
| | <u>101,398</u> | | <u>101,398</u> |
| <u>\$ 11,944,284</u> | <u>\$ 3,055,382</u> | <u>\$ 5,909,293</u> | <u>\$ 20,908,959</u> |

See Accompanying Notes

THE HILL CENTER, INC.
STATEMENTS OF FINANCIAL POSITION
June 30, 2017 and 2016
(Continued)

| <u>LIABILITIES AND NET ASSETS</u> | 2017 | | | |
|---|-------------------|---------------------------|---------------------------|-------------------|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| Current Liabilities: | | | | |
| Accounts Payable | \$ 96,093 | \$ | \$ | \$ 96,093 |
| Accrued Salaries and Other Expenses | 93,602 | | | 93,602 |
| Accrued Interest Payable | | | | |
| Revenue Bonds Payable, Current Portion | 168,789 | | | 168,789 |
| Deferred Revenue - Tuition and Fees | 968,780 | | | 968,780 |
| Deferred Revenue - Grants | | | | |
| Total Current Liabilities | 1,327,264 | | | 1,327,264 |
| Revenue Bonds Payable | 3,340,880 | | | 3,340,880 |
| Total Liabilities | 4,668,144 | | | 4,668,144 |
| Net Assets: | | | | |
| Unrestricted | | | | |
| Undesignated | 214,343 | | | 214,343 |
| Designated | 2,005,805 | | | 2,005,805 |
| Investment in Plant, Net of Debt | 3,668,111 | | | 3,668,111 |
| Temporarily Restricted | | 3,972,665 | | 3,972,665 |
| Permanently Restricted | | | 5,944,443 | 5,944,443 |
| Total Net Assets | 5,888,259 | 3,972,665 | 5,944,443 | 15,805,367 |
| Total Liabilities and Net Assets | \$ 10,556,403 | \$ 3,972,665 | \$ 5,944,443 | \$ 20,473,511 |

2016

| <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Total</u> |
|----------------------|-----------------------------------|-----------------------------------|----------------------|
| \$ 162,654 | \$ | \$ | \$ 162,654 |
| 295,205 | | | 295,205 |
| 1,649 | | | 1,649 |
| 200,000 | | | 200,000 |
| 630,141 | | | 630,141 |
| 350,000 | | | 350,000 |
| <u>1,639,649</u> | | | <u>1,639,649</u> |
| <u>3,698,476</u> | | | <u>3,698,476</u> |
| <u>5,338,125</u> | | | <u>5,338,125</u> |
| 434,159 | | | 434,159 |
| 1,772,345 | | | 1,772,345 |
| 4,399,655 | | | 4,399,655 |
| | 3,055,382 | | 3,055,382 |
| | | 5,909,293 | 5,909,293 |
| <u>6,606,159</u> | <u>3,055,382</u> | <u>5,909,293</u> | <u>15,570,834</u> |
| <u>\$ 11,944,284</u> | <u>\$ 3,055,382</u> | <u>\$ 5,909,293</u> | <u>\$ 20,908,959</u> |

See Accompanying Notes

THE HILL CENTER, INC.
STATEMENTS OF ACTIVITIES
Years Ended June 30, 2017 and 2016

| | 2017 | | | |
|--|--------------|---------------------------|---------------------------|---------------|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| Revenue: | | | | |
| Tuition and Fees | \$ 3,565,036 | \$ | \$ | \$ 3,565,036 |
| Less: Financial Aid | 274,104 | | | 274,104 |
| | 3,290,932 | | | 3,290,932 |
| Contributions | 317,536 | 1,971,039 | 35,150 | 2,323,725 |
| Outreach Student Enrichment Revenue | 773,566 | | | 773,566 |
| Outreach Professional Development Revenue | 292,641 | | | 292,641 |
| Investment Returns | 234,804 | 887,857 | | 1,122,661 |
| Other Income | 34,568 | | | 34,568 |
| | 4,944,047 | 2,858,896 | 35,150 | 7,838,093 |
| Net Assets Released from Restrictions | 1,941,613 | (1,941,613) | | |
| | 6,885,660 | 917,283 | 35,150 | 7,838,093 |
| Expenses and Losses: | | | | |
| Program Services: | | | | |
| Instruction | 5,042,929 | | | 5,042,929 |
| Supporting Services: | | | | |
| Administration | 1,103,847 | | | 1,103,847 |
| Fundraising | 333,721 | | | 333,721 |
| Impairment Loss on Property and Equipment | 1,123,063 | | | 1,123,063 |
| | 7,603,560 | | | 7,603,560 |
| Change in Net Assets | (717,900) | 917,283 | 35,150 | 234,533 |
| Net Assets, Beginning of Year | 6,606,159 | 3,055,382 | 5,909,293 | 15,570,834 |
| Net Assets, End of Year | \$ 5,888,259 | \$ 3,972,665 | \$ 5,944,443 | \$ 15,805,367 |

2016

| Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
|---------------------|---------------------------|---------------------------|----------------------|
| \$ 3,455,938 | \$ | \$ | \$ 3,455,938 |
| <u>260,472</u> | | | <u>260,472</u> |
| 3,195,466 | | | 3,195,466 |
| 224,501 | 1,554,813 | 400 | 1,779,714 |
| 896,082 | | | 896,082 |
| 274,348 | | | 274,348 |
| (7,763) | (48,046) | | (55,809) |
| <u>38,550</u> | | | <u>38,550</u> |
| 4,621,184 | 1,506,767 | 400 | 6,128,351 |
| <u>1,669,695</u> | <u>(1,669,695)</u> | | |
| <u>6,290,879</u> | <u>(162,928)</u> | <u>400</u> | <u>6,128,351</u> |
| 4,990,709 | | | 4,990,709 |
| 1,057,985 | | | 1,057,985 |
| 283,793 | | | 283,793 |
| <u>6,332,487</u> | | | <u>6,332,487</u> |
| (41,608) | (162,928) | 400 | (204,136) |
| <u>6,647,767</u> | <u>3,218,310</u> | <u>5,908,893</u> | <u>15,774,970</u> |
| <u>\$ 6,606,159</u> | <u>\$ 3,055,382</u> | <u>\$ 5,909,293</u> | <u>\$ 15,570,834</u> |

See Accompanying Notes

THE HILL CENTER, INC.
STATEMENT OF FUNCTIONAL EXPENSES
Year Ended June 30, 2017

| | Program Services | Supporting Services | | Total |
|--|---------------------|---------------------|-------------------|---------------------|
| | Instruction | Administration | Fundraising | |
| Salaries | \$ 3,146,071 | \$ 532,973 | \$ 216,513 | \$ 3,895,557 |
| Pension Plan Contributions | 140,904 | 23,982 | 5,842 | 170,728 |
| Other Employee Benefits | 349,230 | 102,109 | 21,121 | 472,460 |
| Payroll Taxes | 238,193 | 36,011 | 15,611 | 289,815 |
| Accounting Fees | | 26,023 | | 26,023 |
| Legal Fees | 1,310 | | | 1,310 |
| Advertising | 42,500 | 3,755 | | 46,255 |
| Consulting and Professional Fees | 67,542 | 1,459 | | 69,001 |
| Supplies and Instructional Materials | 78,728 | 6,164 | 369 | 85,261 |
| Contracted Services | 70,323 | | 4,334 | 74,657 |
| Telephone | 34,312 | 8,679 | 291 | 43,282 |
| Postage and Shipping | 2,423 | 5,615 | 3,567 | 11,605 |
| Rental Fees | 36,241 | | | 36,241 |
| Repairs and Maintenance | 40,330 | 47,604 | 13,189 | 101,123 |
| Printing and Publications | 31,347 | | 6,150 | 37,497 |
| Travel | 26,769 | 2,401 | 1,805 | 30,975 |
| Conferences, Conventions and Meetings | 38,646 | | | 38,646 |
| Facilities Expense | 114,837 | 19,034 | 392 | 134,263 |
| Utilities | 240,734 | 53,394 | 3,364 | 297,492 |
| Depreciation | 306,712 | 94,928 | 6,374 | 408,014 |
| Interest Expense | | 38,227 | | 38,227 |
| Miscellaneous | 35,777 | 101,489 | 34,799 | 172,065 |
| Total Expenses | \$ 5,042,929 | \$ 1,103,847 | \$ 333,721 | \$ 6,480,497 |

See Accompanying Notes

THE HILL CENTER, INC.
STATEMENT OF FUNCTIONAL EXPENSES
Year Ended June 30, 2016

| | Program Services | Supporting Services | | Total |
|--|---------------------|---------------------|-------------------|---------------------|
| | Instruction | Administration | Fundraising | |
| Salaries | \$ 3,028,396 | \$ 569,968 | \$ 182,076 | \$ 3,780,440 |
| Pension Plan Contributions | 142,192 | 23,798 | 7,374 | 173,364 |
| Other Employee Benefits | 347,933 | 47,827 | 12,992 | 408,752 |
| Payroll Taxes | 237,829 | 41,706 | 13,534 | 293,069 |
| Accounting Fees | | 25,226 | | 25,226 |
| Legal Fees | 11,040 | 1,125 | | 12,165 |
| Advertising | 27,015 | 916 | 455 | 28,386 |
| Consulting and Professional Fees | 53,461 | 18,951 | | 72,412 |
| Supplies and Instructional Materials | 110,883 | 6,888 | 314 | 118,085 |
| Contracted Services | 79,989 | | 21,068 | 101,057 |
| Telephone | 43,189 | 4,647 | 476 | 48,312 |
| Postage and Shipping | 612 | 9,373 | 777 | 10,762 |
| Rental Fees | 36,409 | | | 36,409 |
| Repairs and Maintenance | 39,340 | 41,952 | 9,061 | 90,353 |
| Printing and Publications | 38,266 | | 3,784 | 42,050 |
| Travel | 38,071 | 12,672 | 1,383 | 52,126 |
| Conferences, Conventions and Meetings | 49,008 | | | 49,008 |
| Facilities Expense | 54,415 | 48,033 | 340 | 102,788 |
| Utilities | 251,569 | 27,166 | 2,800 | 281,535 |
| Depreciation | 366,146 | 48,184 | 6,576 | 420,906 |
| Interest Expense | | 16,713 | | 16,713 |
| Miscellaneous | 34,946 | 112,840 | 20,783 | 168,569 |
| Total Expenses | \$ 4,990,709 | \$ 1,057,985 | \$ 283,793 | \$ 6,332,487 |

See Accompanying Notes

THE HILL CENTER, INC.
STATEMENTS OF CASH FLOWS
Years Ended June 30, 2017 and 2016

| | 2017 | 2016 |
|--|--------------|--------------|
| Cash Flows from Operating Activities: | | |
| Change in Net Assets | \$ 234,533 | \$ (204,136) |
| Adjustments to Reconcile Change in Net Assets to Net Cash Used in Operating Activities: | | |
| Depreciation | 408,014 | 420,906 |
| Impairment Loss on Property and Equipment | 1,123,063 | |
| Amortization of Bond Issuance Costs | 11,193 | 11,193 |
| Net Realized and Unrealized (Gains) Losses on Investments | (1,019,413) | 185,338 |
| Contributions Restricted for Long-Term Purposes | (2,246,782) | (1,482,149) |
| Changes in Assets and Liabilities that Provided (Used) Cash: | | |
| Tuition Receivable | (25,098) | (35,013) |
| Other Accounts Receivable | 1,904 | 9,923 |
| Prepaid Expenses | 6,611 | (21,555) |
| Pledges Receivable | 613,301 | (416,147) |
| Accounts Payable | (66,561) | 81,659 |
| Accrued Salaries and Other Expenses | (201,603) | (6,484) |
| Accrued Interest Payable | (1,649) | 1,649 |
| Deferred Revenue - Tuition and Fees | 338,639 | (234,457) |
| Deferred Revenue - Grants | (350,000) | 350,000 |
| Net Cash Used in Operating Activities | (1,173,848) | (1,339,273) |
| Cash Flows from Investing Activities: | | |
| Purchases of Property and Equipment | (260,714) | (610,551) |
| Net Investment Activity, Purchases of Investments and Proceeds from Sales of Investments | 281,013 | 255,787 |
| Net Cash Provided (Used) by Investing Activities | 20,299 | (354,764) |
| Cash Flows from Financing Activities: | | |
| Contributions Restricted for Long-Term Purposes | 2,246,782 | 1,482,149 |
| Payments on Bonds Payable | (400,000) | |
| Net Cash Provided by Financing Activities | 1,846,782 | 1,482,149 |
| Net Change in Cash and Cash Equivalents | 693,233 | (211,888) |
| Cash and Cash Equivalents, Beginning of Year | 1,652,149 | 1,864,037 |
| Cash and Cash Equivalents, End of Year | \$ 2,345,382 | \$ 1,652,149 |
| Supplemental Disclosure of Cash Flow Information | | |
| Cash Paid During the Year for Interest | \$ 28,683 | \$ 3,871 |

See Accompanying Notes

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

1. Summary of Significant Accounting Policies

Operations

The Hill Center, Inc. ("Hill Center") is an independent day school that offers half-day programs to students in pre-kindergarten through grade twelve with diagnosed learning disabilities or attention deficit disorders. The Hill Center also offers student enrichment and professional development programs. The financial statements of the Hill Center have been prepared on the accrual basis of accounting.

Financial Statement Presentation

The Hill Center has adopted Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 958-205, *Financial Statements of Not-for-Profit Organizations*. The Hill Center is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. In addition, the Hill Center is required to present a statement of cash flows.

The Hill Center has adopted FASB ASC 958-605, *Accounting for Contributions Received and Contributions Made*. Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Cash Equivalents

For purposes of the statements of cash flows, the Hill Center considers short-term, highly liquid investments that are readily convertible to known amounts of cash with an original maturity at date of purchase of three months or less to be cash equivalents. The Hill Center had cash equivalents of \$1,271,598 and \$1,100,320 at June 30, 2017 and 2016, respectively.

Tuition Receivable

Tuition receivable represents uncollateralized enrollee obligations for tuition and fees, due within 30 days of the invoice date. The carrying amount of accounts receivable is reduced by an allowance that reflects management's best estimate of uncollectible balances. Management reviews each past due balance for the amount that will not be collected, then further applies historical collection rates to the total of receivable balances in determining the amount of the allowance. Tuition receivable is written off when deemed uncollectible.

Recognition of Grant Support

The Hill Center recognizes grants to the extent that eligible grant costs are incurred. Receivables are recognized to the extent costs have been incurred, but not reimbursed. Deferred revenue represents grant advances which exceed eligible costs incurred.

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

1. Summary of Significant Accounting Policies (Continued)

Pledges Receivable

Contributions are recognized when the donor makes a promise to give to the Hill Center that is, in substance, unconditional. An allowance for uncollectible promises to give is recorded based on an analysis of collection histories and on reviews of the credit worthiness of major donors. Donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets.

Investments

Investments consist primarily of assets invested in marketable equity funds and bond funds. The Hill Center accounts for investments in accordance with FASB ASC 958-320, *Accounting for Certain Investments Held By Not-for-Profit Organizations*. This standard requires that investments in equity funds with readily determinable fair value and all investments in bond funds be measured at fair value in the statements of financial position. Fair value of marketable equity funds and bond funds is based on quoted market prices. The realized and unrealized gain or loss on investments is reflected in the statements of changes in net assets.

Investments are exposed to various risks such as significant world events, interest rate, credit, and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in fair value of investments will occur in the near term and that such changes could materially affect the amounts reported in the statements of financial position.

Investments held in trust by others consist of the Hill Center's share of certain trusts for which the Hill Center has an irrevocable right to the income from the trusts but will never receive any portion of the trusts' corpus.

Property and Equipment

It is the policy of the Hill Center to capitalize all capital assets costing more than \$5,000. Property and equipment purchased are recorded at cost at the date of acquisition or at the approximate fair market value at date of donation in the case of gifts. Improvements or betterments of a permanent nature are capitalized. Expenditures for maintenance and repairs are charged to expense as incurred. The costs of assets retired or otherwise disposed of, and the related accumulated depreciation, are eliminated from the accounts in the year of disposal. Gains or losses resulting from property disposals are credited or charged to operations upon disposal. Property and equipment are depreciated using the straight-line method over the following estimated useful lives:

| | |
|-----------------------------------|---------------|
| Land Improvements | 10 years |
| Building and Improvements | 5 to 50 years |
| Equipment, Furniture and Fixtures | 3 to 10 years |
| Software | 3 years |

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

1. Summary of Significant Accounting Policies (Continued)

Property and Equipment (Continued)

Depreciation expense for the years ended June 30, 2017 and 2016 was \$408,014 and \$420,906, respectively.

Impairment of Assets

Accounting principles generally accepted in the United States of America ("GAAP") require that long-lived assets and certain identifiable tangibles held and used by an entity be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amounts of an asset may not be recoverable. During 2017, the Hill Center recognized an impairment loss of \$1,123,063 on work in progress of software costs. During 2017, the Hill Center determined that the commercial viability of the software was limited and calculated the estimated realizable value. There was no impairment loss recognized in 2016.

Unearned Tuition and Fees

Tuition and registration fees collected in advance are recognized over the related school term.

Advertising

Advertising costs are expensed as incurred. Advertising expense was \$46,255 and \$28,386 for the years ended June 30, 2017 and 2016, respectively.

Income Taxes

The Hill Center is exempt from income taxes as a not-for-profit organization under Internal Revenue Service ("IRS") code section 501(c)(3). During the years ended June 30, 2017 and 2016, the Hill Center reported no unrelated business taxable income which is defined by the IRS as gross income derived from any unrelated trade or business that is not substantially related to the organization's tax-exempt purpose. Accordingly, no provision for income taxes has been recorded.

The Hill Center adopted the provisions of FASB ASC 740, *Accounting for Uncertainty in Income Taxes*. Under this provision, an organization must recognize the tax benefit associated with tax taken for tax return purposes when it is more likely than not the position will be sustained. The implementation had no impact on the Hill Center's financial statements. The Hill Center does not believe there are any material uncertain tax positions and, accordingly, it will not recognize any liability for unrecognized tax benefits. The Hill Center is subject to routine audits by taxing jurisdictions; however there are currently no audits for any tax years in progress. At June 30, 2017, the Hill Center has no uncertain tax positions that qualify for either recognition or disclosure in the financial statements.

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

1. Summary of Significant Accounting Policies (Continued)

Use of Estimates and Assumptions

The preparation of the Hill Center's financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the statements of financial position and the reported amounts of revenues and expenses included in the statements of activities. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to prior year presentation to conform to the current year presentation with no effect on previously reported change in net assets or net assets.

During 2017, the Hill Center adopted an amendment requiring deferred finance costs to be presented in the statement of financial position as a direct reduction of the related debt liability rather than as an asset.

New Accounting Pronouncements

In April 2015, the FASB issued an amendment that modifies the presentation of deferred finance costs. The amendment requires deferred finance costs be presented in the statement of financial position as a direct reduction of the related debt liability rather than as an asset. The Hill Center adopted this amendment, which required retrospective application, during 2017. The adoption of this guidance resulted in the reclassification of net bond issuance costs of \$131,526 from "Other Assets" to "Revenue Bonds Payable" in the statement of financial position as of June 30, 2016 and \$11,173 from "Amortization Expense" to "Interest Expense" in the statement of functional expenses for the year ended June 30, 2016.

In May 2015, the FASB issued Accounting Standard Update ("ASU") No. 2015-07 ("ASU 2015-07"), *"Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or its Equivalent)."* ASU 2015-07 removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using net asset value per share as a practical expedient. The Hill Center has adopted ASU 2015-07 as of and for the year ended June 30, 2017. Accordingly, investments for which fair value is measured using net asset value per share as a practical expedient have not been categorized within the fair value hierarchy.

2. Concentration of Credit Risk

The Hill Center occasionally maintains deposits in excess of federally insured limits. Accounts at each institution are insured by the Federal Deposit Insurance Corporations up to \$250,000. FASB ASC 825, *Financial Instruments*, identifies these items as a concentration of credit risk requiring disclosure, regardless of risk. The uninsured balance at June 30, 2017 was \$131,982. The risk is managed by maintaining all deposits in high quality financial institutions.

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

3. Pledges Receivable

Pledges receivable represent unconditional promises to give from various organizations and individuals. Pledges are recorded after discounting to the present value of the future cash flows using a discount rate of 5% for the years ended June 30, 2017 and 2016.

Pledges receivable at June 30 are as follows:

| | 2017 | 2016 |
|-------------------------------------|------------|------------|
| Receivable in Less Than One Year | \$ 305,630 | \$ 866,810 |
| Receivable in More Than One year | 60,000 | 120,000 |
| | 365,630 | 986,810 |
| Less Discounts to Present Value | (8,129) | (14,318) |
| Less Allowance for Doubtful Pledges | (2,594) | (4,284) |
| | \$ 354,907 | \$ 968,208 |

4. Endowment Fund

The Hill Center's endowment consists of 21 individual funds established for a variety of purposes. Its endowment includes both donor restricted endowment funds and funds designated by the Hill Center to function as endowments. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds, including funds designated by the Hill Center to function as endowments are classified and reported based on the existence or absence of donor-imposed restrictions.

The Hill Center has interpreted the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Hill Center classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Hill Center in a manner consistent with the standards of prudence prescribed by UPMIFA.

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

4. Endowment Fund (Continued)

Endowment net assets as of June 30 consist of the following:

| | 2017 | | |
|------------------|---------------------------|---------------------------|---------------------|
| | Temporarily Restricted | Permanently Restricted | Total |
| Board designated | \$ 2,403,279 | \$ | \$ 2,403,279 |
| Donor designated | | 5,943,523 | 5,943,523 |
| Total | <u>\$ 2,403,279</u> | <u>\$ 5,943,523</u> | <u>\$ 8,346,802</u> |

| | 2016 | | |
|------------------|---------------------------|---------------------------|---------------------|
| | Temporarily Restricted | Permanently Restricted | Total |
| Board designated | \$ 1,933,344 | \$ | \$ 1,933,344 |
| Donor designated | | 5,908,518 | 5,908,518 |
| Total | <u>\$ 1,933,344</u> | <u>\$ 5,908,518</u> | <u>\$ 7,841,862</u> |

Changes in the endowment net assets for the years ended June 30, 2017 and 2016 are as follows:

| | Temporarily Restricted | Permanently Restricted | Total |
|--|---------------------------|---------------------------|---------------------|
| Endowment Fund Net Assets, June 30, 2015 | \$ 2,342,867 | \$ 5,908,518 | \$ 8,251,385 |
| Investment Return | (48,046) | | (48,046) |
| Appropriation of Endowment Assets for Expenditure | (361,477) | | (361,477) |
| Endowment Fund Net Assets, June 30, 2016 | 1,933,344 | 5,908,518 | 7,841,862 |
| Investment Return | 887,857 | | 887,857 |
| Contributions | | 35,005 | 35,005 |
| Appropriation of Endowment Assets for Expenditure | (417,922) | | (417,922) |
| Endowment Fund Net Assets, June 30, 2017 | <u>\$ 2,403,279</u> | <u>\$ 5,943,523</u> | <u>\$ 8,346,802</u> |

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

4. Endowment Fund (Continued)

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below what the donor requires the Hill Center to retain as permanently restricted. Deficiencies of this nature result from unfavorable market fluctuations and would be included in temporarily restricted net assets. As of June 30, 2017 and 2016, there were no deficiencies.

The Hill Center has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under this policy, the endowment assets are invested in an allocation of approximately 60 - 80% equity exposure and 20 - 40% in fixed income exposure.

It is the long-term policy of the Hill Center to annually withdraw and transfer to the operating budget 4.5% of a trailing three-year average of the endowment's market value. At the Board's discretion, for certain periods the spending rate may be set higher or lower than 4.5%, however, under no circumstances will the spending rate be higher than 6.5%, while the minimum spending rate is 0%. It is the policy of the Hill Center to protect the endowment so that the corpus shall remain perpetually intact.

5. Investments

The following schedule summarizes the investment return and its classification in the statements of activities for the years ended June 30:

| | 2017 | | | |
|---|---------------------|-----------------------------------|-----------------------------------|---------------------|
| | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Total</u> |
| Investment Income, Net of Fees of \$45,929 | \$ 25,445 | \$ 77,802 | \$ | \$ 103,247 |
| Realized and Unrealized Gains | <u>209,359</u> | <u>810,055</u> | <u> </u> | <u>1,019,414</u> |
| | <u>\$ 234,804</u> | <u>\$ 887,857</u> | <u>\$</u> | <u>\$ 1,122,661</u> |
| | 2016 | | | |
| | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Total</u> |
| Investment Income, Net of Fees of \$44,586 | \$ 29,789 | \$ 100,848 | \$ | \$ 130,637 |
| Realized and Unrealized Losses | <u>(37,552)</u> | <u>(148,894)</u> | <u> </u> | <u>(186,446)</u> |
| | <u>\$ (7,763)</u> | <u>\$ (48,046)</u> | <u>\$</u> | <u>\$ (55,809)</u> |

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

5. Investments (Continued)

The composition of investments at June 30 is as follows:

| | Fair Value | |
|--|--------------|--------------|
| | 2017 | 2016 |
| Equity Funds | \$ 4,322,783 | \$ 3,718,323 |
| Bond Funds | 1,801,527 | 1,820,881 |
| Investments in Trusts Held by Outside Agencies | 4,228,297 | 4,075,003 |
| | \$10,352,607 | \$ 9,614,207 |

6. Fair Value Measurements

FASB ASC 820, *Fair Value Measurements*, establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under FASB ASC 820 are described as follows:

- Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

- Level 2 Inputs to the valuation methodology include:
 - Quoted prices for similar assets or liabilities in active markets;
 - Quoted prices for identical or similar assets or liabilities in inactive markets;
 - Inputs other than quoted prices that are observable for the asset or liability;
 - Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

- Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Hill Center believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

6. Fair Value Measurements (Continued)

The following tables set forth the level within the fair value hierarchy, the Hill Center's investments at fair value as of June 30, 2017 and 2016:

| | Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1) | Total |
|---|--|---------------|
| <u>June 30, 2017</u> | | |
| Investments in Trusts: | | |
| <i>STIF and Money Market</i> | \$ 74,182 | \$ 74,182 |
| <i>Equity Securities</i> | 2,056,305 | 2,056,305 |
| <i>Mutual Funds</i> | 2,097,810 | 2,097,810 |
| Total Assets in Fair Value Hierarchy | 4,228,297 | 4,228,297 |
| Investments Measured at Net Asset Value | | 6,124,310 |
| Investments at Fair Value | \$ 4,228,297 | \$ 10,352,607 |
| | | |
| | Fair Value Measurements Using Quoted Prices in Active Markets for Identical Assets (Level 1) | Total |
| <u>June 30, 2016</u> | | |
| Investments in Trusts: | | |
| <i>STIF and Money Market</i> | \$ 93,402 | \$ 93,402 |
| <i>Equity Securities</i> | 2,424,477 | 2,424,477 |
| <i>Mutual Funds</i> | 1,557,124 | 1,557,124 |
| Total Assets in Fair Value Hierarchy | 4,075,003 | 4,075,003 |
| Investments Measured at Net Asset Value | | 5,539,204 |
| Investments at Fair Value | \$ 4,075,003 | \$ 9,614,207 |

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

7. Revenue Bonds Payable

In March 2008, the Hill Center issued revenue bonds in the amount of \$5,000,000 to finance the construction of a new building, improvements to the existing building, and purchase of equipment. These revenue bonds are payable interest only monthly at an adjustable rate (0.04% at June 30, 2017) not to exceed 12%; principal payments due annually; supported by a standby letter of credit from the Hill Center's bank; final maturity date July 1, 2028. The balance of revenue bonds payable, net of bond issuance costs, at June 30, 2017 and 2016 was \$3,509,669 and \$3,898,474, respectively.

Subsequent to year-end, the revenue bonds were refinanced. See Note 13 for the terms of the refinanced note. Future maturities of the revenue bonds payable based on the terms of the refinanced debt are as follows:

| <u>Years Ending June 30</u> | <u>Amount</u> |
|---------------------------------------|----------------------------|
| 2018 | \$ 168,789 |
| 2019 | 207,600 |
| 2020 | 213,243 |
| 2021 | 219,071 |
| 2022 | 225,027 |
| Thereafter | 2,596,270 |
| Less: Unamortized Bond Issuance Costs | <u>(120,331)</u> |
| | <u><u>\$ 3,509,669</u></u> |

The revenue bonds agreement provides for certain restrictive covenants. At June 30, 2017, the covenants under the former agreement are not applicable and the covenants under the new agreement are not in effect until the next fiscal year.

8. Restrictions on Assets

The financial statements report amounts separately by class of net assets:

- a. Unrestricted net assets are not subject to donor-imposed stipulations and are currently available for use in the operations of the Hill Center under the direction of the board.

Designated net assets are those funds that the Board of Trustees has set aside for specific purposes in the amount of \$2,005,805 and \$1,772,345 as of June 30, 2017 and 2016, respectively.

Investment in Plant are those resources that have been invested in land, buildings and equipment (net of related debt) in the amount of \$3,668,111 and \$4,399,655 as of June 30, 2017 and 2016, respectively.

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

8. Restrictions on Assets (Continued)

- b. Temporarily restricted net assets are those stipulated by donors for specific operating purposes or those not currently available for use until commitments regarding their use have been fulfilled.

Temporarily restricted net assets are composed of the following as of June 30:

| | <u>2017</u> | <u>2016</u> |
|--|-------------------------|-------------------------|
| George Watts Hill Foundation, Held in Trust | \$ 526,913 | \$ 448,373 |
| Hill Center Endowment, Held in Trust | 541,846 | 467,090 |
| Glaxo Student Scholarship Fund | 354,955 | 315,145 |
| Buck Family Fund | 48,254 | 36,277 |
| Timothy Whiting Memorial Scholarship Fund | 36,127 | 28,825 |
| Lucy Davis Memorial Scholarship Fund | 9,120 | 6,995 |
| Anonymous Financial Aid Fund | 42,652 | 32,473 |
| Margaret Holt Brown Fund | 5,244 | 3,976 |
| Kirby Faculty Development Fund | 245,808 | 185,750 |
| Kirby Financial Aid Fund | 35,993 | 27,142 |
| Byron and Sissy Thomas Family Fund | 6,322 | 4,778 |
| Bruce Heim Foundation Endowment | 10,792 | 8,057 |
| Brumley Family Memorial Endowment | 7,332 | 5,302 |
| Financial Aid Endowment | 181,418 | 130,163 |
| Master Mentor Program Endowment | 138,945 | 93,239 |
| Fields Family NC Teacher | 27,065 | 9,355 |
| Fields Family Financial Aid | 8,571 | 4,278 |
| Glaxo Fund Endowment | 86,759 | 62,110 |
| Peyton Strickland Memorial Scholarship Fund | 87,795 | 64,016 |
| Waynell Morris Endowment Fund | 431 | |
| Heard Financial Aid Endowment | <u>937</u> | |
| Total Appreciation of Temporarily Restricted Net Assets | 2,403,279 | 1,933,344 |
| Programs: | | |
| Grants and Gifts | <u>1,569,386</u> | <u>1,122,038</u> |
| TOTAL | <u>\$ 3,972,665</u> | <u>\$ 3,055,382</u> |

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

8. Restrictions on Assets (Continued)

- c. Permanently restricted net assets are those stipulated by donors that they be maintained permanently by the Hill Center. Generally, the donors of these assets permit the Hill Center to use all or part of the income earned on related investments for general or specific purposes.

Permanently restricted net assets are composed of the following as of June 30:

| | <u>2017</u> | <u>2016</u> |
|---|-------------------------|-------------------------|
| George Watts Hill Foundation, held in trust | \$ 1,110,371 | \$ 1,110,371 |
| Hill Center Endowment, held in trust | 2,049,168 | 2,049,168 |
| Glaxo Student Scholarship Fund | 135,514 | 135,514 |
| Buck Family Fund | 100,000 | 100,000 |
| Timothy Whiting Memorial Scholarship Fund | 50,415 | 50,315 |
| Lucy Davis Memorial Scholarship Fund | 17,015 | 17,015 |
| Anonymous Financial Aid Fund | 83,972 | 83,972 |
| Margaret Holt Brown Fund | 10,288 | 10,288 |
| Kirby Faculty Development Fund | 500,156 | 500,156 |
| Kirby Financial Aid Fund | 75,000 | 75,000 |
| Byron and Sissy Thomas Family Fund | 12,700 | 12,700 |
| Bruce Heim Foundation Endowment | 25,000 | 25,000 |
| Brumley Family Memorial Endowment | 18,643 | 18,643 |
| Financial Aid Endowment | 523,330 | 523,330 |
| Peyton Strickland Memorial Scholarship Fund | 202,866 | 202,821 |
| Master Mentor / Training Endowment | 500,000 | 500,000 |
| Fields Family NC Teacher | 200,000 | 200,000 |
| Fields Family Financial Aid | 45,000 | 45,000 |
| Glaxo Fund Endowment | 250,000 | 250,000 |
| Waynell Morris Fund Endowment | 25,000 | |
| Heard Financial Aid Endowment | <u>10,005</u> | |
| TOTAL | <u>\$ 5,944,443</u> | <u>\$ 5,909,293</u> |

9. Grant Awards

During the last several years, the Hill Center has received commitments for grants. The grants are not recorded as revenue in the statements of activities until costs are incurred because the grants are contingent upon approval of the progress of the programs. \$2,280,697 and \$1,603,387 were received from the grants during the years ended June 30, 2017 and 2016, respectively. \$0 and \$350,000 of these amounts are included in deferred revenue-grants in the statements of financial position at June 30, 2017 and 2016, respectively. The Hill Center received grant commitments of \$258,530 and \$883,200 during the years ended June 30, 2017 and 2016, respectively.

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

10. Pension Plan

The Hill Center participates in a multi-employer defined contribution pension plan for all academic and non-academic personnel. The Hill Center matches employees' contributions from 5% to 7.5% of gross salary, based on years of service. Total pension expense for the years ended June 30, 2017 and 2016 was \$170,728 and \$173,364, respectively.

11. Lease Commitments

The Hill Center has entered into several non-cancelable operating leases for various pieces of equipment. Rent expense totaled \$64,630 and \$62,729 for the years ended June 30, 2017 and 2016, respectively.

Future minimum payment requirements on operating leases are as follows:

| Year Ending <u>June 30</u> | <u>Amount</u> |
|-------------------------------|------------------|
| 2018 | \$ 46,502 |
| 2019 | 14,263 |
| 2020 | <u>3,781</u> |
| | <u>\$ 64,546</u> |

12. Commitments and Contingencies

Grant Awards

The Hill Center has grants for specific purposes that are subject to periodic reviews by grantor agencies. Such reviews could result in requests for reimbursement by grantor agencies for costs which may be disallowed as appropriate expenditures under grant terms. The Hill Center's management believes disallowances, if any, will be insignificant.

Standby Letter of Credit

As discussed in Note 7, the Hill Center has secured the revenue bonds payable with a standby letter of credit issued by a bank totaling \$3,630,000 as of June 30, 2017. There were no outstanding amounts on the letter of credit as of June 30, 2017 and 2016. The letter of credit is secured by the assets of the Hill Center.

THE HILL CENTER, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2017 and 2016

13. Subsequent Events

Management evaluates events occurring subsequent to the date of the financial statements in determining the accounting for and disclosure of transactions and events that affect the financial statements. Subsequent events have been evaluated through August 28, 2017, which is the date the financial statements were available to be issued.

In August 2017, the Hill Center refinanced its revenue bonds payable with a new lender. The revenue bonds were refinanced for \$3,700,000, with monthly payments of \$25,003, at an interest rate of 2.69%, and maturing in August 2032. The future maturities schedule in Note 7 reflects the payments based on the terms of the refinanced debt.