HILLCREST EDUCATIONAL CENTERS, INC.

Financial Statements

June 30, 2018

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
HILLCREST EDUCATIONAL CENTERS, INC.
788 South Street
Pittsfield, MA 01201

Report on the Financial Statements

We have audited the accompanying financial statements of Hillcrest Educational Centers, Inc. (a nonprofit organization), which comprise the statement of financial position as of June 30, 2018, and the related statements of activities, functional expenses, and cash flows for the year 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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.

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Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hillcrest Educational Centers, Inc. as of June 30, 2018, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited Hillcrest Educational Centers, Inc.'s 2017 financial statements, and we expressed an unmodified opinion on those audited financial statements in our report dated October 30, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2017, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 1, 2018, on our consideration of Hillcrest Educational Centers, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Hillcrest Educational Centers, Inc.'s internal control over financial reporting and compliance.

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ADELSON & COMPANY PC
Pittsfield, MA

November 1, 2018

HILLCREST EDUCATIONAL CENTERS, INC.
STATEMENT OF FINANCIAL POSITION
JUNE 30,

		2018		Comparative 2017
ASSETS				
Current assets				
Cash and equivalents	$	29,622	$	85,688
Accounts receivable, net		4,577,025		4,103,701
Grants receivable		18,945		24,601
Pledge receivable		76,489		50,000
Inventory		17,495		20,894
Prepaid expenses		864,921		766,141
Total current assets		5,584,497		5,051,025
Long-term investments		7,768,708		6,919,116
Property and equipment, net		14,963,575		12,831,080
Investments held for deferred compensation plan		209,630		162,883
Due from Hillcrest Dental Care, Inc.		94,048		109,723
TOTAL ASSETS	$	28,620,458	$	25,073,827
LIABILITIES AND NET ASSETS				
Current liabilities				
Accounts payable	$	776,660	$	764,411
Accrued expenses		3,222,603		2,526,240
Deposits held in custody for others		12,535		10,935
Deferred income		123,447		234,202
Notes payable due within one year		686,832		661,302
Total current liabilities		4,822,077		4,197,090
Other liabilities		209,630		162,883
Notes payable, less current portion		11,855,579		10,558,959
TOTAL LIABILITIES		16,887,286		14,918,932
Net assets				
Unrestricted		3,964,464		3,160,779
Unrestricted - board designated		7,768,708		6,919,116
Temporarily restricted		---		75,000
Total net assets		11,733,172		10,154,895
TOTAL LIABILITIES AND NET ASSETS	$	28,620,458	$	25,073,827

HILLCREST EDUCATIONAL CENTERS, INC.
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30,

	Unrestricted	Temporarily Restricted	Total 2018	Comparative Total 2017
REVENUE AND SUPPORT				
Tuition and fees	$ 32,345,624		$ 32,345,624	$ 29,047,071
Psychological services	136,525		136,525	149,403
Food care program credits	210,402		210,402	196,986
Grants	98,345		98,345	133,504
Contributions	93,932		93,932	88,728
Special events, net	105,159		105,159	114,096
Interest income	219		219	223
Rental income	152,399		152,399	118,736
Management fee income	211,170		211,170	184,819
Other income	42,589		42,589	49,249
TOTAL REVENUE AND SUPPORT	33,396,364	---	33,396,364	30,082,815
EXPENSES				
Program services:				
Highpoint Center	9,484,403		9,484,403	8,564,990
Intensive Treatment Unit	7,049,569		7,049,569	6,809,485
Housatonic Day Academy	2,869,682		2,869,682	2,185,942
ASD Unit Program	8,713,313		8,713,313	7,929,038
Psychological Services	186,201		186,201	145,792
Total program services:	28,303,168	---	28,303,168	25,635,247
Support services:				
Management and general	4,549,678		4,549,678	3,970,788
Fund-raising	172,169		172,169	119,415
TOTAL EXPENSES	33,025,015	---	33,025,015	29,725,450
CHANGE IN NET ASSETS FROM OPERATING ACTIVITIES	371,349	---	371,349	357,365
NON-OPERATING ACTIVITIES				
Investment income (loss), net	863,605		863,605	856,440
Contributions for capital project	343,323		343,323	107,050
Releases from restrictions for capital project	75,000	(75,000)	---	---
TOTAL NON-OPERATING ACTIVITIES	1,281,928	(75,000)	1,206,928	963,490
CHANGE IN NET ASSETS	1,653,277	(75,000)	1,578,277	1,320,855
Net assets, beginning	10,079,895	75,000	10,154,895	8,834,040
NET ASSETS, ENDING	$ 11,733,172	$ ---	$ 11,733,172	$ 10,154,895

HILLCREST EDUCATIONAL CENTERS, INC.
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30,

	2018	Comparative 2017
CASH FLOWS FROM OPERATING ACTIVITIES		
CHANGE IN NET ASSETS	$ 1,578,277	$ 1,320,855
Adjustments to reconcile change in net assets		
to net cash provided (used) by operating activities:		
Depreciation	997,708	943,286
Amortization of bond issue costs	15,038	14,600
(Gain) loss on sale of property	(1,600)	---
Realized and unrealized (gain) loss on investments	(795,075)	(778,590)
(Increase) decrease in operating assets:		
Accounts receivable	(473,324)	(1,115,724)
Grants receivable	5,656	(27,959)
Pledge receivable	(26,489)	(50,000)
Inventory	3,399	(630)
Prepaid expenses	(98,780)	(8,265)
Investments held for deferred compensation plan	(46,747)	(32,922)
Increase (decrease) in operating liabilities:		
Accounts payable and accrued expenses	708,612	785,273
Deposits held in custody for others	1,600	1,550
Deferred income	(110,755)	(2,496)
Other liabilities	46,747	32,922
Contributions restricted for capital project	(317,323)	(57,050)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	1,486,944	1,024,850
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale of long-term investments	800,667	692,157
Purchase of long-term investments	(855,184)	(895,752)
Proceeds from note receivable	15,675	15,675
Proceeds from sale of property and equipment	1,600	---
Additions of property and equipment	(3,130,203)	(2,787,443)
Contributions restricted for capital project	317,323	57,050
Cash restricted for capital project	---	981,366
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	(2,850,122)	(1,936,947)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase (decrease) in line of credit	(50,658)	(730,156)
Proceeds from issuance of long-term debt	1,577,299	1,852,027
Principal payments on long-term debt	(219,529)	(440,302)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	1,307,112	681,569
INCREASE (DECREASE) IN CASH AND EQUIVALENTS	(56,066)	(230,528)
Cash and equivalents, beginning	85,688	316,216
CASH AND EQUIVALENTS, ENDING	$ 29,622	$ 85,688
SUPPLEMENTAL DATA		
Interest paid	$ 497,694	$ 438,538

See notes to financial statements.

HILLCREST EDUCATIONAL CENTERS, INC.

STATEMENT OF FUNCTIONAL EXPENSES

FOR THE YEAR ENDED JUNE 30,

2018	Program Services: Highpoint Center	Program Services: Intensive Treatment Unit	Program Services: Housatonic Day Academy	Program Services: ASD Unit Program	Program Services: Psychological Services	Program Services: Total Program Services	Support Services: Management and General	Support Services: Fund-raising	Total 2018
Employee compensation and related expenses	$ 8,006,371	$ 6,032,320	$ 2,300,906	$ 7,297,373	$ 142,453	$ 23,779,423	$ 2,801,154	$ 108,783	$ 26,689,360
Occupancy	435,101	311,935	205,105	527,918		1,480,059	195,592		1,675,651
Program operating expenses	629,095	394,839	231,825	532,730	43,748	1,832,237	225,131	1,652	2,059,020
Administrative expenses	121,901	107,537	73,831	135,913		439,182	1,047,966	61,734	1,548,882
Other expenses						---	54,394		54,394
Depreciation	291,935	202,938	58,015	219,379		772,267	225,441		997,708
Total	$ 9,484,403	$ 7,049,569	$ 2,869,682	$ 8,713,313	$ 186,201	$ 28,303,168	$ 4,549,678	$ 172,169	$ 33,025,015

Comparative 2017	Program Services: Highpoint Center	Program Services: Intensive Treatment Unit	Program Services: Housatonic Day Academy	Program Services: ASD Unit Program	Program Services: Psychological Services	Program Services: Total Program Services	Support Services: Management and General	Support Services: Fund-raising	Comparative Total 2017
Employee compensation and related expenses	$ 7,127,144	$ 5,875,733	$ 1,713,696	$ 6,556,709	$ 112,715	$ 21,385,997	$ 2,527,655	$ 102,607	$ 24,016,259
Occupancy	433,918	306,003	71,255	432,263		1,243,439	199,523		1,442,962
Program operating expenses	590,900	343,654	308,669	564,117	33,077	1,840,417	157,754	899	1,999,070
Administrative expenses	112,895	90,350	40,779	120,486		364,510	924,532	15,909	1,304,951
Other expenses						---	18,922		18,922
Depreciation	300,133	193,745	51,543	255,463		800,884	142,402		943,286
Total	$ 8,564,990	$ 6,809,485	$ 2,185,942	$ 7,929,038	$ 145,792	$ 25,635,247	$ 3,970,788	$ 119,415	$ 29,725,450

See notes to financial statements.

HILLCREST EDUCATIONAL CENTERS, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2018

NOTE 1 - NATURE OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities

Hillcrest Educational Centers, Inc. is a not-for-profit corporation organized under Chapter 180 of the laws of the Commonwealth of Massachusetts. The Organization primarily offers educational and residential services to special needs children ranging from six through twenty-two years of age. The Organization also operates a day program for school age children with special needs. The Organization operates its programs from multiple campuses which offer specialized services for specific groups of special needs children.

Income Taxes

The Organization is exempt from federal taxes under Section 501(c)(3) of the Internal Revenue Code and state taxes under applicable state law. In addition, the Organization qualifies for the charitable contribution deduction under Section 170(b)(I)(A)(ii) and has been classified as an organization that is not a private foundation.

Management has evaluated significant tax positions against the criteria established by professional standards and believes there are no such tax positions requiring accounting recognition. The Organization's tax returns are subject to examination by taxing authorities for all years ending on or after June 30, 2015.

Basis of Accounting and Financial Statement Presentation

The financial statements of the Organization have been prepared on the accrual basis of accounting. The Organization 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.

Revenue Recognition

Contract and grant revenues are recognized when expenses, eligible for reimbursement under the terms of the award, are incurred. The Organizations' students are supported by the Commonwealth of Massachusetts Departments of Child, Youth and Family Services, Department of Education, and various Massachusetts cities and towns. Additional support is also provided by out-of-state agencies, cities and towns for students that reside outside of Massachusetts. The majority of the Organization's revenue is from the Commonwealth of Massachusetts and the states of Connecticut and New York. The Organization is subject to the regulations and rate formulas of the Massachusetts Operational Services Division. Revenue is recorded at the Organization's rate of reimbursement as certified by the Commonwealth of Massachusetts.

Contributions

The Organization accounts for contributions received as increases in unrestricted, temporarily restricted, or permanently restricted net assets, depending on the existence or nature of any donor restrictions. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. If a restriction is fulfilled in the same time period in which the contribution is received, the Organization reports the support as unrestricted.

Promises to Give

Unconditional promises to give are recognized as contribution revenue in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Promises to give are recorded at net realizable value if expected to be collected in one year and at fair value if expected to be collected in more than one year.

NOTE 1 - (Continued)

Conditional promises to give are recognized when the conditions on which they depend are substantially met. The Organization uses an allowance method for promises to give based upon management's analysis of the accounts and prior collection experience.

Cash and Equivalents
For the purpose of the statement of cash flows, the Organization considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

Accounts Receivable
Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a charge to bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance have not been material to the financial statements.

Inventory
Inventory is stated at the lower of cost or net realizable value and consists of food at the residential sites and supplies.

Investments
Investments are presented in the financial statements at fair value, Level 1 input, as described below. Unrealized gains and losses are included in the change in net assets. Restricted gains and investment income whose restrictions are met in the same period are recognized and reported as unrestricted revenue and gains.

Level 1 Fair Value Measurement
Fair values for long-term investments are measured on a recurring basis and are determined by quoted market prices and other relevant information generated by market transactions.

Property and Equipment
The Organization capitalizes all expenditures for property and equipment with a useful life greater than one year and a cost in excess of $2,500. Depreciation of buildings and equipment is provided over the estimated useful lives of the assets using the straight-line method. Donated equipment is recorded at fair market value at the date of the donation. Purchased equipment is recorded at cost.

Impairment of Long-Lived Assets
Long-lived assets held and used by the Organization are reviewed for impairment whenever events or changes in the circumstances indicate that the carrying amount of an asset may not be recoverable. In the event that facts and circumstances indicate that the cost of any long-lived assets may be impaired, an evaluation of recoverability would be performed. No impairments were recorded during the year ended June 30, 2018.

Retirement Plan
The Organization is a member of Hillcrest Educational Foundation, Inc.'s 403(b) retirement plan, which covers all eligible employees. Participating employees are allowed to contribute to the plan. Contributions, which are made at the discretion of the Board of Directors of Hillcrest Educational Centers, Inc., were $865,346 and $606,363 for 2018 and 2017, respectively.

The Organization entered into Supplemental Executive Retirement Plan (SERP) deferred compensation agreements with its President and CEO and Executive Director. The SERP is a non-governmental 457(b) plan which is limited to groups of highly compensated executives. The 457(b) account remains the property of the Organization and is subject to the claims of creditors until benefits are paid. The 457(b) funds may be withdrawn as benefits at any time following the end of employment with the Organization. The benefits are taxable when paid. The expense of this plan is being recognized over the period of employment of the President and CEO and Executive Director, including $18,500 and $15,000 for the year ended June 30, 2018, respectively. The total liability as of June 30, 2018 was $209,630.

NOTE 1 - (Continued)

Cost Allocation
An indirect cost allocation plan established under the simplified allocation method is utilized in which all costs that are not chargeable directly to a program are allocated to each program based upon direct salaries and fringe benefits charged directly to each program.

Functional Allocation of Expenses
The costs of providing program and support activities have been summarized on a functional basis in the Statement of Activities. Accordingly, certain costs have been allocated, using management's estimates, among the program and supporting activities benefited.

Advertising and Marketing
The Organization expenses advertising and marketing costs as incurred. Advertising and marketing expense was $87,882 and $70,819 for the years ended June 30, 2018 and 2017, respectively.

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

Subsequent Events
Management has evaluated subsequent events through November 1, 2018 the date which the financial statements were available for issue, and has determined that there are no additional adjustments or disclosures required.

Summarized Comparative Financial Information
The financial information for the year ended June 30, 2017, presented for comparative purposes, is not intended to be a complete financial statement presentation. Certain items in the prior year totals may have been reclassified to conform to the current year presentation.

NOTE 2 - CONCENTRATION OF CREDIT RISK

Financial instruments, which potentially subject the Organization to concentrations of credit risk, consist principally of cash. The Organization maintains its cash in various bank deposit accounts, which at times may exceed federally insured limits. Bank deposits at June 30, 2018 of $137,321 were fully insured. The Organization has not experienced any losses in such accounts. Also, the Organization has a material concentration of credit risk with respect to significant accounts receivables that are due from state and federal contracts through the Commonwealth of Massachusetts, Connecticut and New York.

NOTE 3 - ACCOUNTS RECEIVABLE CONSISTED OF THE FOLLOWING AT JUNE 30:

	2018	Comparative 2017
Student tuition and fees	$ 4,467,159	$ 3,914,391
Hillcrest Dental Care, Inc.	34,384	32,516
Other	163,080	260,546
Subtotal	4,664,623	4,207,453
Allowance for doubtful accounts	(87,598)	(103,752)
Accounts receivable, net	$ 4,577,025	$ 4,103,701

NOTE 4 - LONG-TERM INVESTMENTS CONSISTED OF THE FOLLOWING AT JUNE 30:

Investment fair values are measured on a recurring basis and determined by quoted market prices and other relevant information generated by market transactions (Level 1).

Investments, which are board-designated endowment funds (see Note 8), are comprised of the following groups as reported at fair value.

	2018		Comparative 2017	
	Fair Value	Cost	Fair Value	Cost
Invested cash	$ 244,506	$ 244,506	$ 562,351	$ 562,351
Corporate stock	6,012,314	3,513,594	5,120,065	3,189,900
Municipal and corporate bonds	1,021,544	1,035,596	687,359	691,300
Mutual funds	490,344	339,219	549,341	426,061
Total	$ 7,768,708	$ 5,132,915	$ 6,919,116	$ 4,869,612

The following summarizes the relationship between fair values and cost of investment assets:

	Fair Value	Cost	Unrealized Appreciation (Loss)
Balance at end of year	$ 7,768,708	$ 5,132,915	$ 2,635,793
Balance at beginning of year	6,919,116	4,869,612	2,049,504
Increase in unrealized appreciation			$ 586,289

Investment income consisted of the following for the year ended June 30:

	2018	Comparative 2017
Interest and dividends	$ 117,541	$ 120,567
Realized gains (losses)	208,786	(70,310)
Investment fees	(49,011)	(42,717)
Subtotal	277,316	7,540
Unrealized gains (losses)	586,289	848,900
Investment income (loss), net	$ 863,605	$ 856,440

NOTE 5 - PROPERTY AND EQUIPMENT CONSISTED OF THE FOLLOWING AT JUNE 30:

	2018	Comparative 2017
Land	$ 2,416,024	$ 2,416,024
Buildings	9,992,660	6,179,971
Building improvements	11,829,874	11,562,523
Life safety improvements	738,820	732,515
Office furniture and equipment	1,658,663	1,263,996
Residential furnishings	1,372,550	1,302,777
Equipment	2,271,256	2,158,015
Vehicles	45,500	45,500
Construction in progress	428,182	1,967,734
Total	30,753,529	27,629,055
Accumulated depreciation	(15,789,954)	(14,797,975)
Property and equipment, net	$ 14,963,575	$ 12,831,080

Depreciation expense was $997,708 and $943,286 for the years ended June 30, 2018 and 2017.

NOTE 6 - LEASE OBLIGATIONS

The Organization leases vehicles and equipment under various operating leases which expire through fiscal year 2024. Total lease expense for all operating leases was $216,373 and $187,928 for the years ended June 30, 2018 and 2017, respectively.

Approximate future lease commitments payable during the years ending June 30 are as follows:

2019	$ 160,837
2020	152,954
2021	129,789
2022	57,855
2023	24,246
Thereafter	11,970
Total	$ 537,651

NOTE 7 - NOTES PAYABLE CONSISTED OF THE FOLLOWING AT JUNE 30:

	2018	Comparative 2017
$5,000,000 Series A bond payable to bank dated June 2014, payable in monthly installments of principal and interest, estimated at $22,882 monthly. Secured by a mortgage on land and buildings as well as an assignment of rents and leases on specified real properties. The interest rate is fixed at 3.47% through June 2024 at which time the bond is required to be purchased by the Borrower in accordance with the bond agreement (Bondowners' Option to Put Bonds). The bond matures in June 2044. The Organization also entered into an Interest Rate Swap agreement with the lender (see below).	$ 4,587,925	$ 4,692,691
$4,053,581 multiple advance Series B bond payable to bank dated June 2014, monthly installments of principal and interest, estimated at $19,569 monthly. Secured by a mortgage on land and buildings as well as an assignment of rents and leases on specified real properties. The interest rate is fixed at 3.74% through June 2024 at which time the bond is required to be purchased by the Borrower in accordance with the bond agreement (Bondowners' Option to Put Bonds). The bond matures in June 2044. The Organization also entered into an Interest Rate Swap agreement with the lender (see below).	3,881,314	3,965,858
$4,260,000 multiple advance term note to bank dated June 2014, payable beginning in July 2018 in monthly payments of principal and interest based on a 30-year amortization period estimated at $20,012 monthly, with the remaining balance due in full on the maturity date June 2024. Secured by the Organization's investment account. The Organization shall maintain in said investment account assets having a minimum fair market value of not less than the outstanding principal balance of associated Note, from time to time divided by 70%. The interest rate is fixed at 4.25%.	4,038,000	2,460,701
$3,000,000 revolving line of credit, due on demand. Secured by all of the Organization's accounts, inventories, equipment, general intangibles, investment property, financial assets, documents, instruments, deposit accounts, letter of credit rights and chattel paper and products and proceeds of the foregoing. Interest is at the current One Month Libor rate plus 2.00%, adjusting monthly. The interest rate was 4.08% at June 30, 2018 (3.03% at June 30, 2017).	381,942	432,600

(Continued)

NOTE 7 - (Continued)

	2018	Comparative 2017
$120,000 multiple advance term note to bank dated February 2015, payable in monthly payments of principal and interest in the amount of $2,672. Secured by certain cameras and recording systems and all personal properly of the Organization. The interest rate is fixed at 3.25% through maturity in February 2020.	39,221	69,440
Total notes payable	12,928,402	11,621,290
Amortizable costs of issuance	(385,991)	(401,029)
Total notes payable less amortizable costs of issuance	12,542,411	11,220,261
Amount due within one year	686,832	661,302
Amount due after one year	$ 11,855,579	$ 10,558,959

The above debt matures during the years ending June 30,

2019	$ 686,832
2020	292,371
2021	295,319
2022	306,754
2023	318,633
Thereafter	11,028,493
Total	$ 12,928,402

Debt issuance costs are amortized over the life of the related underlying debt and are reported as interest expense in the Statement of Activities included in administrative expenses.

Interest Rate Swap Agreement
The organization entered into an Interest Rate Swap Transaction (hedge) agreement with the Bank for its $5,000,000 Series A and $4,000,000 Series B tax-exempt bonds and is as follows:

The tax exempt bonds are variable rate obligations. The interest rate is calculated as (i) 0.68 times (ii) the sum of (a) the LIBOR Rate plus (b) two hundred twenty-five basis points (2.25%). The hedge is a variable-to-fixed rate swap and is primarily interest based and is swapped to be a 10 year fixed rate.

The Organization is the *fixed interest rate payer* and is paying a fixed interest rate per annum on each of the bonds for the next 10 years through June 2024. The Bank is the *floating interest rate payer*.

NOTE 8 - BOARD-DESIGNATED ENDOWMENT

The Board of Directors has designated certain funds to function as an endowment. They represent amounts that have been segregated by the Board of Directors for a period of time to provide income to support the Organization's mission. Since the designations are voluntary and may be reversed by the Board at any time, the board-designated endowment is not considered restricted. Accordingly, generally accepted accounting principles require them to be reported as part of the unrestricted class of net assets.

NOTE 8 - (Continued)

Return Objectives and Risk Parameters
The Organization has adopted investment and spending policies, approved by the Board of Directors, for its board-designated endowment assets that attempts to provide a predictable stream of funding to programs supported by its board-designated endowment funds while also maintaining the purchasing power of those assets over the long-term. Under this policy, the board-designated endowment assets are invested in a manner that is intended to produce results that exceed the price yield results of the S&P 500 index for its equity component and the Lehman Aggregate Bond Index for it fixed income component while assuming a moderate level of investment risk. Actual returns in any given year may vary from this amount.

Strategies Employed for Achieving Objectives
To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy
The Organization's policy is to reinvest all earnings of the board-designated endowment assets. Any expenditure from the endowment assets must be supported by the Investment Committee and approved by the full Board of Directors. The Organization's effort is to ensure that the future growth of the endowment assets is sufficient to offset normal inflation plus reasonable spending, thereby preserving the constant dollar value and purchasing power of the endowment assets held for future generations as well as to provide additional real growth through new gifts and investment return.

The unrestricted net assets designated by the board for investment are $7,768,708 and $6,919,116 as June 30, 2018 and 2017, respectively. The composition of the board-designated endowment assets are disclosed in Note 4 on page 11.

Changes in the board-designated endowment consisted of the following for the year ended June 30:

	2018	Comparative 2017
Board-designated endowment net assets, beginning of year	$ 6,919,116	$ 5,885,933
Investment return:		
Investment income	117,541	120,567
Realized and unrealized gains (losses)	795,075	778,590
Investment fees	(49,011)	(42,717)
Total investment return, net	863,605	856,440
Contributions	52,361	176,743
Withdrawals	(66,374)	---
Subtotal	(14,013)	176,743
Board-designated endowment net assets, end of year	$ 7,768,708	$ 6,919,116

NOTE 9 - TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purpose or periods at June 30:

	2018	Comparative 2017
St. Mark's School:		
Interactive Media Wall	$ ---	$ 25,000
Information Technology	---	50,000
Total	$ ---	$ 75,000

NOTE 10 - NET ASSETS RELEASED FROM RESTRICTION

Net assets were released from restrictions during the year ended June 30 by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by the donors.

	2018	Comparative 2017
Girls Circle	$ ---	$ 25,000
St. Mark's School:		
Interactive Media Wall	25,000	---
Information Technology	50,000	---
Total	$ 75,000	$ 25,000

NOTE 11 - SURPLUS (DEFICIT) REVENUE RETENTION

The Commonwealth of Massachusetts' Not-For-Profit Contractor Surplus Revenue Retention Policy pursuant to 808 CMR 1.03(7) of the Compliance, Reporting and Auditing for Human and Social Services regulations, allows a non-profit contractor (the Organization) to retain, for future use, a portion of annual surplus in an unrestricted net asset account. This net surplus, from the revenues and expenses associated with services provided to purchasing agencies which are subject to 808 CMR 1.00 may not exceed 20% of said revenue annually. Surpluses may be used by the Organization for any of its established charitable purposes, provided that no portion of the surplus may be used for any non-reimbursable cost set forth in 808 CMR 1.05.

The amount of the Organization's annual surplus is within the 20% threshold, and therefore, no liability to the Commonwealth exists.

NOTE 12 - RENTAL INCOME

The Organization leases property it owns on an at-will basis to certain employees who work in the Organization's programs. Rental income was $47,039 and $42,736 during fiscal year 2018 and 2017, respectively.

In 2018, the Organization entered into a 60-month lease agreement with Guidewire, Inc. (tenant) to rent the property located at 1450 West Housatonic Street in Pittsfield, Massachusetts. Monthly installments are due on the first day of each month in the amount of $7,655. The tenant shall have the right to extend the lease for two additional 5 year terms. Rental income for the year ended June 30, 2018 was $22,964. Minimum lease income expected to be received from the tenant for the years ended June 30 are as follows:

2019	$	91,856
2020		91,856
2021		91,856
2022		91,856
2023		68,892
Total	$	436,316

NOTE 13 - COMMITMENTS AND CONTINGENT LIABILITIES

The Organization receives support from state and federal contracts. The contracts require audits of both the financial operation of the programs and compliance with the terms of the agreements. Such audits could result in the disallowance of some costs charged to the contract and, therefore, create a liability to the funding source. Liabilities resulting from these audits, if any, will be recorded in the period in which the amount of the liability is ascertained. Management believes that any adjustment which might result from such an audit would be immaterial.

NOTE 14 - SPECIAL EVENTS ACTIVITIES FOR THE YEARS ENDED JUNE 30 WERE AS FOLLOWS:

	2018		
	Golf Tournament	St. Patrick's Day Event	Total
Special event revenues			
Ticket sales and fees	$ 25,149	$ 10,141	$ 35,290
Sponsorships	68,791	52,562	121,353
Total event revenues	93,940	62,703	156,643
Cost of direct benefits to donors			
Rent and facility costs	15,316	8,157	23,473
Other direct expenses	20,231	7,780	28,011
Total cost of direct benefits to donors	35,547	15,937	51,484
Special events, net	$ 58,393	$ 46,766	$ 105,159

NOTE 14 - (Continued)

	Comparative 2017		
	Golf Tournament	St. Patrick's Day Event	Total
Special event revenues			
Ticket sales and fees	$ 26,682	$ 7,486	$ 34,168
Sponsorships	66,648	58,761	125,409
Total event revenues	93,330	66,247	159,577
Cost of direct benefits to donors			
Rent and facility costs	15,030	8,473	23,503
Other direct expenses	15,009	6,969	21,978
Total cost of direct benefits to donors	30,039	15,442	45,481
Special events, net	$ 63,291	$ 50,805	$ 114,096

NOTE 15 - RELATED PARTY TRANSACTIONS

A member of the Board of Directors is the Vice President of an automobile association. During fiscal year 2018, the Organization incurred $1,394 ($1,394 in 2017) of membership fees to the Automobile Association.

A member of the Board of Directors is also a board member at three local medical centers with which the Organization does business. The Organization incurred $38,816 of expenses for services by the centers during fiscal year 2018 ($46,091 in 2017).

A member of the Board of Directors owns a local electrical contracting company with which the Organization does business. The Organization incurred $80,754 of expenses in fiscal year 2018 ($51,904 in 2017).

The President and Chief Executive Officer is a Corporator of a local health care organization in which the Organization engages in business activity and incurred $29,678 of expenses during fiscal year 2018 ($35,723 in 2017).

In 2018, the Executive Vice President and Chief Financial Officer were directors of the Berkshire County Kids Place with which the Organization provided business support and staff training. The Organization received $25,000 in fiscal year 2018 ($25,000 in 2017) for services provided.

NOTE 16 - COMMONLY CONTROLLED ENTITY

Hillcrest Educational Foundation, Inc.

Hillcrest Educational Foundation, Inc. has been created to become the sole member of Hillcrest Educational Centers, Inc., Hillcrest Dental Care, Inc. and Berkshire County Kids' Place and Violence Prevention Center, Inc. (Kids' Place). Its mission is to support the affiliated organizations. Each affiliated organization has its own non-profit tax exempt status and is governed by its own separate Board of Directors. This corporate structure allows each affiliate to benefit from the combined resources of the entire membership. These resources are typically in the form of Operational Management Agreements and, in some cases, Fund Management Agreements. The corporate structure allows, under certain circumstances, with board approval and in accordance with the agreements, transfers of funds between certain affiliates. In accordance with the provisions of the Fund Management Agreement, no contribution was accrued and payable from Hillcrest Educational Centers, Inc. to Hillcrest Educational Foundation, Inc. in fiscal years 2018 and 2017.

NOTE 16 - (Continued)

Transactions between Hillcrest Educational Center, Inc. and Hillcrest Dental Care, Inc.

Facilities Lease Agreement
A facilities lease agreement has been entered into between Hillcrest Educational Centers, Inc. (Landlord) and Hillcrest Dental Care, Inc. (Tenant), in which Hillcrest Dental Care, Inc. will pay Hillcrest Educational Centers, Inc. a base rent of $6,333 per month. The lease commenced on July 1, 2011 and expires on June 30, 2020. The lease agreement can be extended for an additional nine consecutive periods of five years each. Total lease income received from Hillcrest Dental Care, Inc. was $76,000 for each of the years ending June 30, 2018 and 2017.

Management Agreement
A management agreement exists between Hillcrest Educational Centers, Inc. (Manager) and Hillcrest Dental Care, Inc. (Licensee), in which Hillcrest Dental Care, Inc. will pay Hillcrest Educational Centers, Inc. an annual management fee to cover the cost of executive, financial and administrative and general support. The determination of the fee is based upon the Manager's projected costs and any other costs of providing the services, including reimbursement for the cost of all salaries, benefits and any other actual and direct costs of providing the services by the Manager. The agreement commenced on July 1, 2011 and expires on June 30, 2020. The agreement shall renew automatically for successive five year terms unless terminated pursuant to the terms of the agreement. Total management fee income received in fiscal year 2018 was $211,170 ($184,819 in 2017).

Minimum facilities lease and management fee income expected to be received for the years ended June 30 are as follows:

	Facilities Lease Agreement	Management Agreement	Total
2019	$ 76,000	$ 111,815	$ 187,815
2020	76,000	111,815	187,815
Total	$ 152,000	$ 223,630	$ 375,630

Dental Equipment Agreement
On June 30, 2013, Hillcrest Educational Centers, Inc. sold dental equipment and office furniture to Hillcrest Dental Care, Inc. in exchange for a receivable of $156,747. As of June 30, 2018 the outstanding balance was $94,048 ($109,723 as of June 30, 2017).

Transactions between Hillcrest Educational Center, Inc. and Kids' Place
Hillcrest Educational Centers, Inc. (Hillcrest) and Kids' Place are two separate and distinct non-profit organizations. While the organizations are under common control, Hillcrest has no economic interest in Kids' Place. Inter-agency activity during the year ended June 30, 2018 consisted of Hillcrest providing administrative and accounting services for which a management fee was charged.

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CERTIFIED PUBLIC ACCOUNTANTS
Established 1938

Richard F. LaFleche, CPA
Vincent T. Viscuso, CPA
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INDEPENDENT AUDITORS' REPORT 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

To the Board of Directors of
HILLCREST EDUCATIONAL CENTERS, INC.
788 South Street
Pittsfield, MA 01201

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Hillcrest Educational Centers, Inc. (a nonprofit organization), which comprise the statement of financial position as of June 30, 2018, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated November 1, 2018.

Internal Control Over Financial Reporting
In planning and performing our audit of the financial statements, we considered Hillcrest Educational Centers, Inc.'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 financial statements, but not for the purpose of expressing an opinion on the effectiveness of Hillcrest Educational Centers, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control.

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

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

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

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

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Pittsfield, MA

November 1, 2018