

MONTANA HEALTHCARE FOUNDATION

Financial Statements

For the Year Ended December 31, 2017

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Independent Auditor's Report

**To the Board of Trustees
Montana Healthcare Foundation
Bozeman, Montana**

We have audited the accompanying financial statements of Montana Healthcare Foundation (the Foundation), which comprise the statement of financial position as of December 31, 2017, and the related statements of activities and change in net assets 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.

Auditor's 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. 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.



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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Foundation as of December 31, 2017, and the change in its net assets and its cash flow 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 the Foundation's 2016 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated May 11, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Clark Nuber P.S.

Certified Public Accountants
May 10, 2018

MONTANA HEALTHCARE FOUNDATION

Statement of Financial Position

December 31, 2017

(With Comparative Totals for 2016)

	<u>2017</u>	<u>2016</u>
Assets:		
Cash and cash equivalents	\$ 9,034,403	\$ 15,761,635
Investments	156,513,783	120,732,727
Fixed assets, net	115,535	
Prepays and other assets	<u>106,488</u>	<u>93,720</u>
Total Assets	<u>\$ 165,770,209</u>	<u>\$ 136,588,082</u>
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued liabilities	\$ 39,904	\$ 37,465
Grants payable	<u>1,238,209</u>	<u>964,711</u>
Total Liabilities	1,278,113	1,002,176
Net Assets:		
Unrestricted:		
Undesignated	116,380,854	92,385,906
Board designated quasi-endowment	<u>45,707,601</u>	<u>40,200,000</u>
Total unrestricted	162,088,455	132,585,906
Temporarily restricted	<u>2,403,641</u>	<u>3,000,000</u>
Total Net Assets	<u>164,492,096</u>	<u>135,585,906</u>
Total Liabilities and Net Assets	<u>\$ 165,770,209</u>	<u>\$ 136,588,082</u>

See accompanying notes.

MONTANA HEALTHCARE FOUNDATION

**Statement of Activities and Changes in Net Assets
For the Year Ended December 31, 2017
(With Comparative Totals for 2016)**

	Unrestricted	Temporarily Restricted	2017	2016
Revenues, Gains and Other Support:				
Grants and contributions	\$ 10,025,000	\$ -	\$ 10,025,000	\$ 33,000,000
Interest and dividends	1,547,043		1,547,043	1,311,651
Realized and unrealized gains on investments	24,402,167		24,402,167	4,552,636
Other income	5,995		5,995	50,000
Releases	596,359	(596,359)		
Total Revenues, Gains and Other Support	36,576,564	(596,359)	35,980,205	38,914,287
Expenses:				
Program services-				
Grants and initiatives	5,346,235		5,346,235	3,392,691
Other program related expenses	917,151		917,151	528,995
Total program expenses	6,263,386		6,263,386	3,921,686
Management and general-				
Investment related expenses	408,883		408,883	391,728
Administrative	401,746		401,746	405,105
Total management and general	810,629		810,629	796,833
Total Expenses	7,074,015		7,074,015	4,718,519
Change in Net Assets	29,502,549	(596,359)	28,906,190	34,195,768
Net assets, beginning of year	132,585,906	3,000,000	135,585,906	101,390,138
Net Assets, End of Year	\$ 162,088,455	\$ 2,403,641	\$ 164,492,096	\$ 135,585,906

See accompanying notes.

MONTANA HEALTHCARE FOUNDATION

**Statement of Cash Flows
For the Year Ended December 31, 2017
(With Comparative Totals for 2016)**

	<u>2017</u>	<u>2016</u>
Cash Flows From Operating Activities:		
Change in net assets	\$ 28,906,190	\$ 34,195,768
Adjustments to reconcile change in net assets to net cash provided by operating activities-		
Realized and unrealized gains on investments	(24,402,167)	(4,552,636)
Changes in assets and liabilities:		
Prepaid expenses and other assets	(12,768)	(18,962)
Accounts payable and accrued liabilities	2,439	(12,694)
Grants payable	273,498	134,971
	<u>4,767,192</u>	<u>29,746,447</u>
Net Cash Provided by Operating Activities	4,767,192	29,746,447
Cash Flows From Investing Activities:		
Purchase of investments	(28,640,848)	(31,277,849)
Proceeds from sale of investments	17,261,959	10,092,463
Purchase of fixed assets	(115,535)	
	<u>(11,494,424)</u>	<u>(21,185,386)</u>
Net Cash Used by Investing Activities	(11,494,424)	(21,185,386)
Net Change in Cash and Cash Equivalents	(6,727,232)	8,561,061
Cash and cash equivalents, beginning of year	<u>15,761,635</u>	<u>7,200,574</u>
Cash and Cash Equivalents, End of Year	<u>\$ 9,034,403</u>	<u>\$ 15,761,635</u>
Supplementary Disclosure of Cash Flow Information:		
Cash paid during the year for excise taxes	\$ 27,000	\$ 10,760

See accompanying notes.

MONTANA HEALTHCARE FOUNDATION

Notes to Financial Statements For the Year Ended December 31, 2017

Note 1 - Nature of Activities and Significant Accounting Policies

Nature of Activities - Montana Healthcare Foundation (the Foundation) is dedicated to improving the health and well-being of all Montanans. The Foundation contributes to a healthier state by making strategic investments that support access to quality and affordable health services, conducting evidence-driven research and analysis, and addressing the upstream influences on health and illness. The Foundation is a 501(c)3 private foundation.

Some Montanans face particularly difficult barriers to health. Health disparities (the higher rates of illness and death that are consistently documented among certain subgroups) are all too common among certain racial and ethnic groups, the social and economic disadvantaged, and young children and older adults. Across all our work, we place an emphasis on reducing health disparities and building healthier Montana communities.

The Foundation was created as a result of the 2013 sale of Blue Cross Blue Shield of Montana. In accordance with state law, the assets from this sale were transferred to a charitable trust to be managed for public benefit. MHCF spends the income from trust investments (roughly 5% of the total value of the trust each year) so that it can serve as a permanent, stable, and reliable resource for improving health in the state.

A summary of the Foundation's significant accounting policies follows:

Basis of Presentation - Net assets and revenues, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Foundation and changes therein are classified and reported as follows:

Unrestricted Net Assets - Net assets that are not subject to externally imposed restrictions. Changes in this category of net assets include restricted contributions whose donor-imposed restrictions were met during the fiscal year. The Foundation has designated approximately \$45.7 million and \$40.2 million of its unrestricted net assets as a quasi-endowment, as of December 31, 2017 and 2016, respectively.

Temporarily Restricted Net Assets - Net assets subject to externally imposed restrictions that may or will be met either by actions of the Foundation and/or the passage of time. The Foundation had temporarily restricted net assets of approximately \$2.4 million and \$3.0 million, as of December 31, 2017 and 2016, respectively.

Permanently Restricted Net Assets - Permanently restricted net assets include net assets received by donations wherein the donors imposed a permanent restriction on the use of the gift. There were no permanently restricted net assets as of December 31, 2017 and 2016.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets are reported as transfers between the applicable classes of net assets.

Contributions - Contributions are recognized as revenues in the period received.

MONTANA HEALTHCARE FOUNDATION

**Notes to Financial Statements
For the Year Ended December 31, 2017**

Note 1 - Continued

Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities, at the date of the financial statements, as well as the reported amounts of revenues and expenses, including functional allocations, during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents - For purposes of the statement of cash flows, the Foundation considers all cash and other highly liquid investments with initial maturities of three months or less to be cash equivalents, other than those included in the investment portfolio.

Investments - Investments are stated at fair value, with both realized and unrealized gains and losses recorded in the statements of activities and changes in net assets as increases or decreases in unrestricted net assets, unless their use is temporarily or permanently restricted by explicit donor restrictions or law. Fair value of investments with readily determinable market values is based on quoted market prices. The estimated fair value of certain alternative investments for which quoted market prices are not available, is based on valuations provided by the external investment managers and the management of the investees. The Foundation reviews and evaluates the values provided by the investment managers and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these investments existed.

Investments are made according to the Investment Policy Statement adopted by the Foundation's Board of Trustees. These guidelines provide for investments in equities, fixed income, emerging markets and other investments with performance measured against appropriate indices. Outside parties are contracted with by the Foundation for the purpose of providing investment management and consulting.

Investment securities, in general, are exposed to various risks, including interest rate, credit and overall market volatility. Due to the level of risk associated with certain long-term investments, it is reasonably probable that changes in the values of these investments will occur in the near term and that such changes could materially affect the amounts reported in the balance sheets.

Dividend income is recorded on the ex-dividend date. Interest income is recorded on an accrual basis when earned.

Fixed Assets - Fixed assets are recorded at cost if purchased or fair value if donated. The Foundation capitalizes all items over \$25,000 that provide a future benefit. Depreciation is provided on a straight-line basis over the estimated useful lives as follows:

Software	3 years
Equipment	3 - 5 years
Leasehold improvements	Lesser of 7 years or lease term
Furniture/fixtures	10 years

MONTANA HEALTHCARE FOUNDATION

Notes to Financial Statements For the Year Ended December 31, 2017

Note 1 - Continued

Concentrations - Financial instruments that potentially subject the Foundation to concentrations of credit and market risk consist primarily of cash and investments. Cash and investments held by financial institutions exceed federally insured limits. Management anticipates no material effect to the Foundation's financial position as a result of these concentrations.

For the years ended December 31, 2017 and 2016, 99% of the Foundation's contribution and grant funding came from one organization, and 100% of the Foundation's contribution and grant funding came from two organizations, respectively.

Grants - Grants made and unconditional promises to make future grants are recognized the earlier of when made or when the promise is conveyed. Grants payable over more than one year are recorded at their discounted present value using a risk adjusted rate of return. Changes in discounts are recognized over the period of the promise as adjustments to grant expenses.

Functional Allocation of Expenses - The cost of providing the various programs and other activities has been summarized on a functional basis in the statement of activities and changes in net assets. Accordingly, certain costs have been allocated among the programs and supporting services benefitted.

Comparative Totals - The financial information includes certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. GAAP. Accordingly, such information should be read in conjunction with the Foundation's financial statements for the year ended December 31, 2016, from which the summarized information was derived.

Subsequent Events - The Foundation's management has evaluated subsequent events through May 10, 2018 the date on which the financial statements were available to be issued.

Note 2 - Excise Taxes and Required Charitable Grants

The Foundation has obtained tax-exempt status from federal income tax under Section 501(c)(3) of the Internal Revenue Code (IRC). However, the Foundation is a private foundation as defined in the IRC, and is therefore subject to an excise tax on its net investment income.

The Foundation is also required under the IRC to make minimum charitable distributions based on the fair value of its assets. Charitable distributions made in excess of the required minimum in any year may be used to reduce the minimum distributions required in future years, subject to a five-year carryover limitation. Failure to make the minimum charitable distributions could result in additional taxes and possible penalties.

MONTANA HEALTHCARE FOUNDATION

Notes to Financial Statements For the Year Ended December 31, 2017

Note 3 - Investments

Investments consisted of the following at December 31:

	<u>2017</u>	<u>2016</u>
Investments valued at fair value based on market quotes-		
Money markets	\$ 8,256,084	\$ 12,510,629
Bond mutual fund	20,528,260	20,258,898
Equity mutual funds	<u>72,816,185</u>	<u>51,310,942</u>
	101,600,529	84,080,469
Nonmarketable securities	<u>54,913,254</u>	<u>36,652,258</u>
Total Investments	<u>\$ 156,513,783</u>	<u>\$ 120,732,727</u>

Investment return consisted of the following for the years ended December 31:

	<u>2017</u>	<u>2016</u>
Interest and dividends	\$ 1,547,043	\$ 1,311,651
Realized and unrealized gains on investments	<u>24,402,167</u>	<u>4,552,636</u>
Total Investment Return	<u>\$ 25,949,210</u>	<u>\$ 5,864,287</u>

Investment management fees totaled \$308,912 and \$317,116 for the years ended December 31, 2017 and 2016, respectively.

Note 4 - Fair Value Measurements

U.S. GAAP has established a framework that requires fair value to be determined based on the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants.

To increase consistency and comparability in fair value measurements, U.S. GAAP uses a fair value hierarchy which prioritizes the inputs to valuation approaches into three broad levels based on observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Foundation's market assumptions. These two types of inputs create the following fair value hierarchy:

Level 1 - Inputs are unadjusted and represent quoted prices in active markets for identical assets at the measurement date;

Level 2 - Inputs are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in inactive markets, and model-derived valuations whose inputs are observable; or

MONTANA HEALTHCARE FOUNDATION

**Notes to Financial Statements
For the Year Ended December 31, 2017**

Note 4 - Continued

Level 3 - Inputs are unobservable and reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and/or the risk inherent in the inputs to the model.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2017 and 2016.

Money Markets - Money market funds are valued at cost plus accrued interest, which approximates fair value.

Bond and Equity Mutual Funds - Valued at the closing price reported on the active market in which the securities are traded.

Nonmarketable Securities - Valued at the NAV as reported by the general partner or investment manager unless specific evidence indicates that NAV should be adjusted. This may involve significant unobservable inputs. The valuation methods utilized by the investment managers are subject to regular review by the Foundation.

Management determines the Foundation's fair value measurements valuation policies and procedures, including those reported at NAV. The Foundation's Board of Trustees assesses and approves these policies and procedures.

During the year ended December 31, 2017, the Foundation implemented ASU 2015-07, *Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or its Equivalent)*, which removes the requirement that investments for which fair value is measured using the NAV per share, or its equivalent, be categorized in the fair value hierarchy. The fair value amounts presented in the tables below are intended to permit reconciliation of the fair value hierarchy to the line items presented in the statement of financial position.

Fair values of assets measured on a recurring basis were as follows:

	Fair Value Measurements as of December 31, 2017			
	Level 1	Level 2	Level 3	Total
Money markets	\$ 8,256,084	\$ -	\$ -	\$ 8,256,084
Bond mutual fund	20,528,260			20,528,260
Equity mutual funds-				
U.S. large cap	10,610,711			10,610,711
U.S. small cap	37,285,790			37,285,790
International	24,919,684			24,919,684
Total Investments in the Fair Value Hierarchy	\$ 101,600,529	\$ -	\$ -	101,600,529
Investments measured at NAV				54,913,254
Total Investments at Fair Value				\$ 156,513,783

MONTANA HEALTHCARE FOUNDATION

Notes to Financial Statements
For the Year Ended December 31, 2017

Note 4 - Continued

	Fair Value Measurements as of December 31, 2016			
	Level 1	Level 2	Level 3	Total
Money markets	\$ 12,510,629	\$ -	\$ -	\$ 12,510,629
Bond mutual fund	20,258,898			20,258,898
Equity mutual funds-				
U.S. large cap	27,424,924			27,424,924
U.S. small cap	8,108,112			8,108,112
International	15,777,906			15,777,906
Total Investments in the Fair Value Hierarchy	\$ 84,080,469	\$ -	\$ -	84,080,469
Investments measured at NAV				36,652,258
Total Investments at Fair Value				\$ 120,732,727

The table below summarizes significant terms of the agreements with certain investment companies for nonmarketable investments. There are no significant redemption restrictions or unfunded commitments on other types of investments.

Asset Class	Fair Value December 31, 2017	Unfunded Commitments	Redemption Frequency	Redemption Notice Period	Other Restrictions
Hedge funds*	\$ 13,225,429	\$ -	Monthly - 3 years	30 days	None
Offshore corporation	16,187,462		Monthly	30 days	None
Partnership and trust	22,142,312		Monthly	7 - 30 days	None
Private equity	3,358,051	14,031,541	None	None	None
	\$ 54,913,254	\$ 14,031,541			

* One of the funds included here is in the process of liquidation as of December 31, 2017.

MONTANA HEALTHCARE FOUNDATION

**Notes to Financial Statements
For the Year Ended December 31, 2017**

Note 4 - Continued

Asset Class	Fair Value December 31, 2016	Unfunded Commitments	Redemption Frequency	Redemption Notice Period	Other Restrictions
Hedge funds*	\$ 10,031,495	\$ -	Monthly - 3 years	30 days	None
Offshore corporation	9,312,691		Monthly	30 days	None
Partnership and trust	17,308,072		Monthly	7 - 30 days	None
	\$ 36,652,258	\$ -			

* One of the funds included here is in the process of liquidation as of December 31, 2016.

Note 5 - Fixed Assets

Fixed assets consist of the following at December 31:

	2017	2016
Software	\$ 50,820	\$ -
Leasehold improvements	64,715	
	115,535	
Less accumulated depreciation		
Fixed Assets, Net	\$ 115,535	\$ -

No depreciation expense was incurred during the years ended December 31, 2017 and 2016.

Note 6 - Grants Payable

Grants authorized but unpaid at year end are reported as liabilities. Grants authorized are payable as follows:

For the Year Ending December 31,

2018	\$ 1,238,209
	\$ 1,238,209

There were no conditional grants authorized as of December 31, 2017 and 2016. There is no discount to present value as of December 31, 2017 and 2016, as all grants are payable in the next year.

MONTANA HEALTHCARE FOUNDATION

Notes to Financial Statements For the Year Ended December 31, 2017

Note 7 - Temporarily Restricted Net Assets

At December 31, 2017 and 2016, temporarily restricted net assets consisted of one contribution restricted for use related to improving substance abuse prevention and treatment in Montana.

Note 8 - Commitments

Operating Lease - The Foundation entered into a lease for office space that began August 14, 2014, and terminates on April 14, 2020. Monthly payments began at \$1,869 and increase to \$2,103 over the term of the lease. The Foundation entered into another lease for additional office space that began on May 15, 2017 and terminates on April 14, 2019, with an option to renew for an additional year with 90 days written notice. Monthly payments are \$2,301 per month over the term of the lease. Future minimum lease payments are as follows:

For the Year Ending December 31,

2018	\$	74,742
2019		55,885
2020		<u>14,011</u>
	\$	<u><u>144,638</u></u>

Rental expense for the years ended December 31, 2017 and 2016, totaled \$88,044 and \$63,844, respectively, and included CAM charges incurred during the year.

Employment Agreement - Effective January 1, 2017, the Foundation entered into two employments agreements with key members of management that expire on December 31, 2018 and December 31, 2021. The agreement would require a final payout to the employee for the Foundation to terminate the agreement prior to expiration without cause.

Note 9 - Retirement Plan

The Foundation has established a SIMPLE IRA Plan. All employees are eligible with enrollment at the start of each calendar year. The Foundation matches up to 100% of employees' contributions up to 3% of participants' eligible compensation. Matching expense totaled \$16,013 and \$13,010 for the years ended December 31, 2017 and 2016, respectively.

Note 10 - Related Party Transactions

The Foundation paid stipends totaling \$144,000 to Board Trustees during the years ended December 31, 2017 and 2016.

Note 11 - Quasi-Endowment

During the year ended December 31, 2016, the Foundation established a quasi-endowment to preserve the initial \$40,200,000 of assets transferred to the Foundation upon formation. The Foundation had \$45.7 million and \$40.2 million of its unrestricted net assets as a quasi-endowment, as of December 31, 2017 and 2016, respectively.

MONTANA HEALTHCARE FOUNDATION

**Notes to Financial Statements
For the Year Ended December 31, 2017**

Note 11 - Continued

Changes to quasi-endowment net assets are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, December 31, 2016	\$ 40,200,000	\$ -	\$ -	\$ 40,200,000
Endowment investment income-				
Investment fees	(92,893)			(92,893)
Interest and dividends	465,215			465,215
Realized and unrealized gain	7,338,038			7,338,038
Total endowment investment income	7,710,360			7,710,360
Appropriation of endowment for expenditure	(2,202,759)			(2,202,759)
Endowment Net Assets, December 31, 2017	<u>\$ 45,707,601</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 45,707,601</u>
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, December 31, 2015	\$ -	\$ -	\$ -	\$ -
Contributions	40,200,000			40,200,000
Endowment Net Assets, December 31, 2016	<u>\$ 40,200,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 40,200,000</u>

Return Objectives and Risk Parameters - The Foundation has adopted investment policies for endowment assets that attempts to earn a return that preserves the trust assets in perpetuity and maximizes the income available to fulfill the Foundation's charitable purpose. The endowment assets are diversified among several asset classes to achieve the Foundation's return goal while maintaining acceptable levels of risk.

Strategies Employed for Achieving Objectives - To satisfy its long-term return goal, the Foundation relies on a total return strategy in which investment returns are achieved through both income and net realized and unrealized capital gains. The Foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return goal.

Spending Policy - The Foundation's policy for its quasi-endowment is to spend 5% of a rolling 12 quarter average of the endowment balance. In 2017, the Foundation began allocating investment earnings related to the quasi-endowment.