

**Mosaic and Affiliates**  
Omaha, Nebraska

**Consolidated Financial Statements**  
**June 30, 2010 and 2009**

**Together with Independent Auditor's Report**

## Mosaic and Affiliates

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## Independent Auditor's Report

To the Board of Directors  
Mosaic and Affiliates  
Omaha, Nebraska:

We have audited the accompanying consolidated balance sheets of Mosaic and Affiliates as of June 30, 2010 and 2009, and the related consolidated statements of operations and changes in net assets and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mosaic and Affiliates as of June 30, 2010 and 2009, and the results of their operations, changes in their net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued for the year ended June 30, 2010 a report dated October 15, 2010 on our consideration of Mosaic and Affiliates' internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal controls over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

*Seim, Johnson, Sestak + Quist, LLP*

Omaha, Nebraska,  
October 15, 2010.

## Mosaic and Affiliates

### Consolidated Balance Sheets June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 12,129,157	15,030,395
Short-term investments	1,540,825	1,488,751
Current portion of investments limited as to use	516,453	477,008
Receivables -		
Program services, net of estimated uncollectibles of \$434,453 and \$395,445 in 2010 and 2009, respectively	19,614,182	20,243,079
Pledges	101,224	144,310
Affiliates	204,298	270,193
Other	498,539	626,778
Other current assets	232,711	167,537
Prepaid expenses	<u>1,002,075</u>	<u>505,317</u>
Total current assets	35,839,464	38,953,368
Investments, primarily investments limited as to use, net of current portion	43,756,090	29,323,253
Property and equipment, net	65,684,407	55,916,469
Other assets, net	<u>14,135,889</u>	<u>10,831,745</u>
Total assets	<u>\$ 159,415,850</u>	<u>135,024,835</u>
<b>LIABILITIES AND NET ASSETS</b>		
Current liabilities:		
Current portion of -		
Long-term debt	\$ 3,438,002	2,170,215
Obligations under capital leases	216,860	241,912
Annuity payment liability	181,587	165,000
Accounts payable	3,163,046	2,397,589
Notes payable	747,000	747,000
Other accrued expenses	11,313,070	10,951,774
Deferred revenue	320,460	321,594
Estimated third-party payor settlements - Medicaid	<u>950,338</u>	<u>797,168</u>
Total current liabilities	<u>20,330,363</u>	<u>17,792,252</u>
Long-term liabilities:		
Long-term debt, net of current portion	31,501,686	18,900,803
Obligations under capital leases, net of current portion	1,116,556	1,333,415
Annuity payment liability, net of current portion	2,261,313	2,346,043
Refundable fees	1,396,348	1,382,057
Liability for post-retirement benefits	<u>1,757,709</u>	<u>1,567,331</u>
Total long-term liabilities	<u>38,033,612</u>	<u>25,529,649</u>
Total liabilities	<u>58,363,975</u>	<u>43,321,901</u>
Commitments and contingencies		
Net assets:		
Unrestricted	78,683,323	73,187,501
Temporarily restricted	19,046,831	15,439,969
Permanently restricted	<u>3,321,721</u>	<u>3,075,464</u>
Total net assets	<u>101,051,875</u>	<u>91,702,934</u>
Total liabilities and net assets	<u>\$ 159,415,850</u>	<u>135,024,835</u>

See notes to consolidated financial statements

## Mosaic and Affiliates

### Consolidated Statements of Operations and Changes in Net Assets For the Year Ended June 30, 2010, with Comparative Totals for 2009

	2010			2009 Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
REVENUE, GAINS AND OTHER SUPPORT:				
Net program service revenue	\$ 181,157,506	--	--	181,157,506
Gifts and grants	3,105,590	389,361	33,252	3,528,203
Estates	2,898,743	--	215,015	3,113,758
Other revenue	4,032,839	3,627,996	--	7,660,835
Investment income (loss), net	2,257,853	23,990	1,121	2,282,964
Gain (loss) on disposal of property and equipment, net	(106,289)	--	--	(106,289)
Change in value of split-interest agreements	(131,686)	(553)	(3,598)	(135,837)
Total revenue, gains and other support	193,214,556	4,040,794	245,790	197,501,140
EXPENSES:				
Salaries and wages	102,564,375	--	--	102,564,375
Employee benefits	30,381,130	--	--	30,381,130
Supplies	3,264,534	--	--	3,264,534
Occupancy	4,836,785	--	--	4,836,785
Purchased and professional services	18,258,326	--	--	18,258,326
Rentals and leases	6,660,090	--	--	6,660,090
Interest	954,948	--	--	954,948
Food	2,940,959	--	--	2,940,959
Insurance	2,456,399	--	--	2,456,399
Cost of goods sold - Spectrum	1,826,638	--	--	1,826,638
Telephone	1,153,714	--	--	1,153,714
Travel	1,288,031	--	--	1,288,031
Transportation	1,916,311	--	--	1,916,311
Repairs and maintenance	1,260,554	--	--	1,260,554
Employee-related expenses	621,716	--	--	621,716
Other	4,331,719	--	--	4,331,719
Depreciation	4,494,276	--	--	4,494,276
Amortization	426,195	--	--	426,195
Total expenses	189,636,700	--	--	189,636,700
NET INCOME (LOSS)	3,577,856	4,040,794	245,790	7,864,440
NET ASSETS RELEASED FROM RESTRICTION FOR THE PURCHASE OF PROPERTY AND EQUIPMENT	483,932	(483,932)	--	--
CHANGE IN NET UNREALIZED GAINS AND LOSSES ON OTHER THAN TRADING SECURITIES	1,464,938	--	467	1,465,405
POSTRETIREMENT BENEFIT RELATED CHANGES OTHER THAN NET PERIODIC COST	19,096	--	--	19,096
RECLASSIFICATION OF NET ASSETS	(50,000)	50,000	--	--
INCREASE (DECREASE) IN NET ASSETS	5,495,822	3,606,862	246,257	9,348,941
NET ASSETS, BEGINNING OF YEAR	73,187,501	15,439,969	3,075,464	91,702,934
NET ASSETS, END OF YEAR	\$ 78,683,323	19,046,831	3,321,721	101,051,875

See notes to consolidated financial statements

## Mosaic and Affiliates

### Consolidated Statements of Operations and Changes in Net Assets For the Year Ended June 30, 2009

	2009			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
REVENUE, GAINS AND OTHER SUPPORT:				
Net program service revenue	\$ 184,005,128	--	--	184,005,128
Gifts and grants	2,047,450	418,723	75,740	2,541,913
Estates	1,416,319	--	15,639	1,431,958
Other revenue	2,357,391	4,314,662	--	6,672,053
Investment income, net	(6,365,072)	--	(3,024)	(6,368,096)
Gain on disposal of property and equipment, net	34,284	--	--	34,284
Change in value of split-interest agreements	101,987	--	--	101,987
Total revenue, gains and other support	<u>183,597,487</u>	<u>4,733,385</u>	<u>88,355</u>	<u>188,419,227</u>
EXPENSES:				
Salaries and wages	102,743,229	--	--	102,743,229
Employee benefits	28,464,802	--	--	28,464,802
Supplies	3,816,402	--	--	3,816,402
Occupancy	4,746,029	--	--	4,746,029
Purchased and professional services	18,493,278	--	--	18,493,278
Rentals and leases	6,951,327	--	--	6,951,327
Interest	1,048,158	--	--	1,048,158
Food	3,106,913	--	--	3,106,913
Insurance	2,097,116	--	--	2,097,116
Cost of goods sold - Spectrum	2,980,058	--	--	2,980,058
Telephone	1,151,805	--	--	1,151,805
Travel	1,775,323	--	--	1,775,323
Transportation	2,003,635	--	--	2,003,635
Repairs and maintenance	1,245,909	--	--	1,245,909
Employee-related expenses	1,791,870	--	--	1,791,870
Other	4,465,445	--	--	4,465,445
Depreciation	4,158,829	--	--	4,158,829
Amortization	408,128	--	--	408,128
Total expenses	<u>191,448,256</u>	<u>--</u>	<u>--</u>	<u>191,448,256</u>
NET INCOME (LOSS)	(7,850,769)	4,733,385	88,355	(3,029,029)
NET ASSETS RELEASED FROM RESTRICTION FOR THE PURCHASE OF PROPERTY AND EQUIPMENT	704,632	(704,632)	--	--
CHANGE IN NET UNREALIZED GAINS AND LOSSES ON OTHER THAN TRADING SECURITIES	1,748,623	--	809	1,749,432
POSTRETIREMENT BENEFIT RELATED CHANGES OTHER THAN NET PERIODIC COST	79,617	--	--	79,617
INTERFUND TRANSFER, NET	(1,033,078)	1,033,078	--	--
INCREASE (DECREASE) IN NET ASSETS	(6,350,975)	5,061,831	89,164	(1,199,980)
NET ASSETS, BEGINNING OF YEAR	79,538,476	10,378,138	2,986,300	92,902,914
NET ASSETS, END OF YEAR	<u>\$ 73,187,501</u>	<u>15,439,969</u>	<u>3,075,464</u>	<u>91,702,934</u>

See notes to consolidated financial statements

## Mosaic and Affiliates

### Consolidated Statements of Cash Flows For the Years Ended June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Change in net assets	\$ 9,348,941	(1,199,980)
Adjustments to reconcile the change in net assets to net cash provided by operating activities -		
Depreciation	4,494,276	4,158,829
Amortization	426,195	408,128
(Gain) loss on disposal of property and equipment, net	106,289	(34,284)
Change in liability for post-retirement benefits	190,378	214,739
Change in deferred compensation liability	--	(238,531)
Change in value of split-interest agreements	135,837	(101,987)
Net realized and unrealized (gains) losses on other than trading securities	(2,822,359)	5,871,027
Restricted gifts, grants, estates and capital advances, net	(637,628)	(510,102)
(Increase) decrease in current assets -		
Receivables -		
Program services	628,897	(2,879,561)
Other	128,239	322,365
Other current assets	(65,174)	69,403
Prepaid expenses	(496,758)	(4,695)
Increase (decrease) in current liabilities -		
Accounts payable	594,898	(817,456)
Other accrued expenses	361,296	(178,451)
Deferred revenue	(1,134)	262
Estimated third-party payor settlements - Medicaid	153,170	34,682
Net cash provided by operating activities	<u>12,545,363</u>	<u>5,114,388</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Proceeds from the sale of property and equipment	76,696	449,785
Purchases of property and equipment	(14,274,640)	(8,008,038)
(Purchase of) withdrawals from investments, net	(11,701,997)	755,912
(Investments in) sales of affiliates, net	209,881	(1,510,540)
Net cash used in investing activities	<u>(25,690,060)</u>	<u>(8,312,881)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net borrowings (payments) on revolving credit agreements	(1,328,367)	2,265,803
Proceeds from issuance of long-term debt	17,122,000	3,169,217
Payments on long-term debt	(1,924,963)	(4,502,064)
Payments on obligations under capital leases	(241,911)	(222,008)
Incurrence of annuity payment obligations	218,456	230,863
Payments on annuity payment obligations	(422,436)	(471,591)
Other asset additions, net	(4,280,899)	(260,083)
Payments from affiliates	65,895	67,166
Refundable fees received (returned), net	14,291	(208,750)
Restricted gifts, grants, estates and capital advances, net	1,021,393	1,254,040
Net cash provided by financing activities	<u>10,243,459</u>	<u>1,322,593</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(2,901,238)	(1,875,900)
CASH AND CASH EQUIVALENTS - Beginning of year	<u>15,030,395</u>	<u>16,906,295</u>
CASH AND CASH EQUIVALENTS - End of year	<u>\$ 12,129,157</u>	<u>15,030,395</u>

See notes to consolidated financial statements

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### (1) Organization

Mosaic and Affiliates (Mosaic) is a not-for-profit integrated organization that provides living and care facilities and vocational services to people with intellectual disabilities or other special needs related to their health, education, care and support. These services are provided within the states of Connecticut, Delaware, Tennessee, Iowa, Illinois, Indiana, Nebraska, Kansas, Texas, Colorado, Arizona, and New Mexico. The consolidated financial statements of Mosaic include the accounts of the following entities:

- Mosaic
- The Mosaic Foundation
- Mosaic Housing Corp I
- Mosaic Housing Corp II
- Mosaic Housing Corp III
- Mosaic Housing Corp IV
- Mosaic Housing Corp V, Inc.
- Mosaic Housing Corp VII
- Mosaic Housing Corp VIII
- Mosaic Housing Corp IX
- Mosaic Housing Corp X
- Mosaic Housing Corp XI
- Mosaic Housing Corp XII
- Mosaic Housing Corp XIII
- Mosaic Housing Corp XIV
- Mosaic Housing Corp XV
- Mosaic Housing Corp XVI
- Mosaic Housing Corp XVII
- Mosaic Housing Corp XVIII
- Mosaic Housing Corp XIX
- Mill Towne, Inc.
- The Oaks of Dunn County, Inc.
- Mosaic Illinois Housing 1
- Mosaic Illinois Housing 2
- Mosaic Illinois Housing of Macomb
- Mosaic Illinois Housing of Rockford
- Spectrum Medical Equipment, Inc.

Significant intercompany accounts and transactions have been eliminated in the consolidation.

Mosaic is affiliated with the Evangelical Lutheran Church of America. With such affiliation, Mosaic is solely responsible for its own management and affairs.

#### (2) Summary of Significant Accounting Policies

The following is a summary of significant accounting policies of Mosaic. These policies are in accordance with accounting principles generally accepted in the United States of America.

##### A. *Use of Estimates*

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America 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 consolidated financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

##### B. *Cash and Cash Equivalents*

Cash and cash equivalents for purposes of the consolidated statement of cash flows include investments in highly liquid debt instruments with original maturities of three months or less.

Supplemental disclosures of cash flow information include:

	<u>2010</u>	<u>2009</u>
Interest paid	\$ <u>794,970</u>	<u>1,028,253</u>

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### C. *Investments*

Investments in equity securities and mutual funds with readily determinable fair values and all investments in debt securities are measured at fair value in the consolidated balance sheet. Investment income or loss (including realized gains and losses on investments, interest and dividends) is included in net income unless the income or loss is restricted by donor or law. Unrealized gains and losses on investments are excluded from net income unless the investments are trading securities. Periodically, Mosaic reviews its investment portfolio to determine whether any unrealized losses are other than temporary. During 2010 and 2009, investment declines determined to be other-than-temporary were \$356,006 and \$305,080, respectively.

#### D. *Contribution Receivable from Remainder Trusts*

The Foundation has been named beneficiary of several irrevocable charitable remainder trust agreements in which the Foundation will receive certain funds upon termination of each trust. The Foundation recognizes contribution revenue in the period in which the trusts are established or when they receive notice of the trust's existence and when the amount contributed is measurable. The contributions and associated receivables are recorded by discounting the future gift amount to its net present value.

#### E. *Program Service Receivables*

Mosaic reports program service receivables for services rendered at net realizable amounts after determining the estimated allowance for doubtful accounts and contractual adjustments from third-party payors. Management reviews client receivables by payor class and applies percentages relative to account age and historical collection information to determine the adequacy of the bad debt allowance. Management utilizes calculation estimates based on applicable third-party reimbursement methodologies to determine contractual adjustments.

Payment for services is expected within thirty to sixty days of receipt of the billing. Any amounts deemed uncollectible are written off on a monthly basis. Mosaic does not charge interest on outstanding balances owed.

#### F. *Investments Limited as to Use*

By Board - Investments set aside by the Board of Directors (Board) for future capital improvements over which the Board retains control and may, at its discretion, subsequently use for other purposes.

By Donor - Investments limited as to use by donor includes assets the donor has restricted for endowment or specific purposes.

Under Bond Indenture Agreement - Investments set aside in accordance with terms of the various revenue bond agreements. This includes project funds, debt service funds and reserve funds.

Under Deferred Compensation Agreements - Investments set aside in accordance with the terms of the executive deferred compensation agreements (Agreements). The Agreements allow for the executive to direct the investment of the assets. See Note 14 regarding the Agreements.

Under Regulatory Agreements - Investments restricted under regulatory agreements with Housing and Urban Development.

These investments are recorded at fair value. Amounts required to meet current liabilities of Mosaic have been reclassified in the consolidated balance sheet.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### G. *Property and Equipment*

Property and equipment acquisitions are stated at cost. Mosaic's capitalization policy is \$1,000 or the applicable state required Medicaid amount if other than \$1,000. Depreciation is provided on the straight-line method based upon the estimated useful lives of each class of depreciable asset as follows:

Land improvements	15 – 25 years
Buildings and improvements	15 – 25 years
Equipment and furnishings	3 – 15 years
Transportation equipment	3 years

Gifts of cash that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, expirations of donor restrictions are released when the acquired long-lived assets are placed into service.

When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is expensed as incurred; significant renewals and betterments are capitalized.

#### H. *Goodwill*

In 2008, Mosaic purchased Spectrum and Spectrum purchased another company. On June 30, 2010, Mosaic purchased a company that provided adult day services for people with developmental and intellectual disabilities. As of June 30, 2010 and 2009, unamortized goodwill related to these purchases of \$5,851,209 and \$1,967,451, respectively, is included in other assets in the consolidated balance sheets. Goodwill is amortized over a fifteen year useful life as determined by management. Amortization expense of \$115,022 is included in the consolidated statements of operations and changes in net assets as of June 30, 2010 and 2009.

#### I. *Annuity Payment Liability*

The Foundation has received several charitable gift annuities for which the Foundation is required to make specified payments in accordance with gift annuity agreements. The Foundation recognizes the agreements in the period in which the contract is executed. Assets received are recorded at fair value and an annuity payment liability is recognized at the present value of future cash flows expected to be paid. Unrestricted contribution revenue is recognized as the difference between these two amounts. Adjustments to the annuity liability to reflect an increase of the discount rate in life expectancy are recognized as changes in the value of split-interest agreements.

#### J. *Refundable Fees*

Fees paid by a resident upon entering into a reservation agreement for an apartment unit at Mosaic's Senior Living facility in Osage, Iowa are refundable to the resident upon termination of the reservation agreement.

The Oaks of Dunn County, Inc. (The Oaks) is a non-profit housing project for seniors of varying income levels in Menomonie, Wisconsin. Fees paid by the original 27 residents that entered into a reservation agreement for an apartment unit at The Oaks are refundable to the resident upon termination of the agreement. For all residents after the first 27, fees paid upon entering a reservation agreement are reduced on an annual basis by 5%, up to 50% of the original deposit, and used to offset living expenses. Any remaining deposit is refunded upon termination of the agreement by the resident.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### K. *Deferred Revenue*

Deferred revenue at June 30, 2010 and 2009 consists of advances from the following:

	<u>2010</u>	<u>2009</u>
Connecticut Department of Mental Retardation	\$ 320,460	320,460
Other payors	<u>--</u>	<u>1,134</u>
	<u>\$ 320,460</u>	<u>321,594</u>

#### L. *Net Assets*

Mosaic maintains the following classes of net assets:

Unrestricted - Represents net assets that are not subject to donor-imposed restrictions.

Temporarily Restricted - Represents net assets subject to donor-imposed stipulations that may or will be met either by actions of Mosaic and/or the passage of time.

Permanently Restricted - Represents net assets subject to donor-imposed stipulations that they be maintained permanently by Mosaic. Generally, the donors of these assets permit Mosaic to use all of the interest and dividends earned on related investments for general or specific purposes of Mosaic.

#### M. *Donor-Restricted Funds*

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets.

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year received are reported as unrestricted contributions in the accompanying consolidated financial statements.

Unconditional promises to give that are expected to be collected within one year are recorded at net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using risk-free interest rates applicable to the years in which the promises are received. Amortization of the discounts is included in contribution revenue.

#### N. *Net Program Service Revenue*

Net program service revenue is reported at the estimated net realizable amounts from clients, third-party payors and others for services rendered. Revenue under third-party payor agreements is subject to audit or prospective adjustment and can be subject to retroactive adjustment. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### O. *Income Taxes*

All consolidated affiliated entities, except for Mosaic Housing Corp V, Inc. and Spectrum Medical Equipment, Inc., are not-for-profit corporations as described in Section 501(c)(3) or 501(c)(2) of the Internal Revenue Code and are exempt from federal income taxes on related income pursuant to Section 501(a) of the Code. The Internal Revenue Service has established standards to be met to maintain Mosaic's tax exempt status. In general, such standards require Mosaic to meet a community benefits standard and comply with various laws and regulations.

Mosaic Housing Corp V, Inc. is a for-profit taxable corporation and had no material operations or income.

Spectrum Medical Equipment, Inc. (Spectrum) is a for-profit taxable corporation. Spectrum had an operating loss during 2010 and 2009. Income tax refunds and deferred tax liabilities are included in other receivables and other accrued expenses, respectively, on the consolidated balance sheets.

Mosaic accounts for uncertainties in accounting for income tax assets and liabilities using guidance included in FASB ASC 740, *Income Taxes*. Mosaic recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. At June 30, 2010 and 2009, Mosaic had no uncertain tax positions accrued.

#### P. *Fair Value of Financial Statements*

Mosaic applies the provisions included in ASC Topic 820 for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the financial statements. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. At June 30, 2010, there were no nonfinancial assets or liabilities measured at fair value in the financial statements on a nonrecurring basis.

Financial instruments consist of cash and cash equivalents, short-term investments, patient accounts receivable, investments limited as to use, current liabilities and long-term debt obligations. Management's estimate of fair value of short-term investments and investments limited as to use is described in Note 5. The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, patient accounts receivable and current liabilities approximate fair value due to the short-term nature of these financial statements. The carrying value of long-term debt obligations approximates fair value since the interest rates closely reflect current market rates.

#### Q. *Performance Indicator*

The consolidated statement of operations and changes in net assets includes net income as a performance indicator. Changes in net assets which are excluded from the performance indicator, consistent with industry practice, include change in net unrealized gains and losses on other than trading securities.

#### R. *Conditional Asset Retirement Obligations*

Mosaic recognizes the fair value of liabilities for legal obligations associated with asset retirements in the period in which it is incurred, in accordance with ASC Topic 410 Subtopic 20, *Asset Retirement Obligations*. Over time, the obligation is accreted to its present value each period. Upon settlement of the obligation, any difference between the cost to settle the asset retirement obligation and the liability recorded is recognized as a gain or loss in the consolidated statement of operations. Mosaic assessed the impact of the interpretation and determined that it did not have an obligation that required recognition at June 30, 2010 or 2009.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### S. *Subsequent Events*

Mosaic considered events occurring through October 15, 2010 for recognition or disclosure in the financial statements as subsequent events. That date is the date the financial statements were available to be issued.

#### T. *Reclassification*

Certain amounts in the 2009 financial statements have been reclassified to conform to the 2010 reporting format.

### (3) **Net Program Service Revenue**

Mosaic has agreements with third-party payors that provide payments based on contracted rates. The majority of Mosaic's support comes from state agencies for the provision of services to Title XIX - Medicaid eligible individuals and Medicaid waiver individuals. The majority of the contracted rates are based on prospective payment methodologies, with the remainder made on limited cost based methodologies. Laws and regulations governing the Medicaid program are extremely complex and subject to interpretation. Certain programs can be subject to retroactive adjustment. As a result, there is at least a reasonable possibility that recorded estimates could change in the future.

### (4) **Investments, Primarily Investments Limited as to Use and Short-Term Investments**

Investments are presented in the consolidated balance sheets at fair value. The composition of investments at June 30, 2010 and 2009 is as follows:

	<u>2010</u>	<u>2009</u>
Short-term investments	\$ <u>1,540,825</u>	<u>1,488,751</u>
Current portion of investments limited as to use	\$ <u>516,453</u>	<u>477,008</u>
Investments, primarily limited as to use -		
By board	24,244,351	19,834,368
By donor	4,435,290	3,882,563
Under bond indenture agreements	9,649,571	1,166,094
Under regulatory agreements	511,910	345,544
Other	<u>5,431,421</u>	<u>4,571,692</u>
	44,272,543	29,800,261
Less amounts required for current obligations	<u>(516,453)</u>	<u>(477,008)</u>
	\$ <u>43,756,090</u>	<u>29,323,253</u>

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

Investment income (loss) is composed as follows:

	2010			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividends	\$ 926,011	--	--	926,011
Net realized gains on other than trading securities	1,687,848	23,990	1,121	1,712,959
Realized losses on investments determined to be other-than-temporarily impaired	(356,006)	--	--	(356,006)
	2,257,853	23,990	1,121	2,282,964
Changes in net unrealized gains on other than trading securities	1,464,938	--	467	1,465,405
Total investment income	\$ 3,722,791	23,990	1,588	3,748,369

  

	2009			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividends	\$ 1,252,363	--	--	1,252,363
Net realized gains on other than trading securities	(7,312,355)	--	(3,024)	(7,315,379)
Realized losses on investments determined to be other-than-temporarily impaired	(305,080)	--	--	(305,080)
	(6,365,072)	--	(3,024)	(6,368,096)
Changes in net unrealized gains on other than trading securities	1,748,623	--	809	1,749,432
Total investment loss	\$ (4,616,449)	--	(2,215)	(4,618,664)

#### (5) Fair Value

##### Fair Value Measurements

Mosaic adopted ASC Topic 820 Subtopic 10 on July 1, 2008 for fair value measurements of financial assets and financial liabilities and for fair value measurements of nonfinancial items that are recognized or disclosed at fair value in the financial statements on a recurring basis. ASC Topic 820 Subtopic 10 establishes 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 measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that Mosaic has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly through either corroboration or observable market data.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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- Level 3 inputs are unobservable inputs for the asset or liability. Therefore, unobservable inputs shall reflect the entity's own assumptions about the assumptions that market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety

The financial statements as of and for the year ended June 30, 2010 do not include any nonrecurring fair value measurements relating to assets and liabilities for which Mosaic has adopted the provisions of ASC 820.

The following methods and assumptions were used to estimate the fair value for each financial instrument measured at fair value:

Cash and Cash Equivalents - Money market funds included with cash and cash equivalents are recorded at fair value using quoted market prices.

Fixed Income Securities - Investments in fixed income securities are comprised of certificates of deposit, U.S. government treasury securities, U.S. government agency obligations, and corporate bonds and notes. U.S. government treasury and agency obligations are classified as Level 1 if they trade with sufficient frequency and volume to enable the organization to obtain pricing information on an ongoing basis. The remaining fixed income securities are classified as Level 2 based on multiple sources of information, which may include market data and/or quoted market prices from either markets that are not active or are for the same or similar assets in active markets.

Equity Securities, Exchange Traded and Closed End Funds, and Mutual Funds - The fair value of equity securities, exchange traded and closed end funds, and mutual funds is the market value based on quoted market prices, when available, or market prices provided by recognized broker dealers.

Cash Surrender Value of Life Insurance - The fair value of cash surrender value of life insurance is classified as Level 2 as it is the amount that could be realized under the insurance contract upon discontinuance or surrender of the contract before its maturity.

Property Held for Investment - The fair value of property held for investment is classified as Level 3 as there is no observable market data.

For the fiscal years ended June 30, 2010 and 2009, the application of valuation techniques applied to similar assets and liabilities has been consistent.



## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

A reconciliation of fair value measurements classified as Level 3 for the year ended June 30, 2010 is as follows:

		<u>2010</u>
Beginning balance, property held for investment	\$	375,940
Transfer of land to affiliate		<u>(28,792)</u>
Ending balance, property held for investment	\$	<u>347,148</u>

#### (6) Property and Equipment

Property and equipment as of June 30, 2010 and 2009, is summarized as follows:

		<u>2010</u>	<u>2009</u>
Land and land improvements	\$	10,185,084	9,442,349
Buildings and improvements		87,761,374	79,723,795
Equipment and furnishings		13,516,770	12,838,917
Transportation equipment		2,655,914	2,534,154
Construction in process		<u>7,080,371</u>	<u>2,689,203</u>
		121,199,513	107,228,418
Less - Accumulated depreciation		<u>(55,515,106)</u>	<u>(51,311,949)</u>
	\$	<u>65,684,407</u>	<u>55,916,469</u>

Depreciation expense of \$4,494,276 and \$4,158,829 for June 30, 2010 and 2009, respectively, is included in the accompanying consolidated statement of operations and changes in net assets.

Construction in progress primarily consists of costs related to the building of living and care facilities for individuals with special needs for various housing projects. At June 30, 2010 the total commitment on these projects approximated \$3,080,000. These projects are primarily being funded through government grants and private donations, with expected completion in 2010.

Mosaic signed an agreement in March 2009 with the state of Nebraska to build eleven intermediate care facilities or medical support units at various locations around Nebraska. The total construction cost is estimated at \$12.2 million. Four units were completed before June 30, 2010. The remaining seven units are scheduled to be completed by March 2011. These projects are primarily being funded through bond issues and low income housing tax credits.

#### (7) Other Assets, Net

Other assets for Mosaic at June 30, 2010 and 2009, are comprised of the following:

		<u>2010</u>	<u>2009</u>
Unamortized costs, net	\$	5,952,844	2,098,142
Contributions receivable from remainder trusts		1,483,195	1,811,817
Pledges receivable, net of current portion		29,936	36,822
Gift annuities receivable		148,141	153,310
Capital contribution to Bethphage Residential Services Limited Partnership (BRSLP)		703,017	703,017
Investment in BICO, Ltd. (BICO)		5,818,756	5,978,403
Investment in HRB Aircraft, Inc. (HRBAI)		<u>--</u>	<u>50,234</u>
	\$	<u>14,135,889</u>	<u>10,831,745</u>

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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Mosaic Housing Corp V, Inc. is the general partner of BRSLP, a Nebraska limited partnership. This partnership was formed to acquire, finance, build, own, maintain, improve, operate, lease and, if appropriate or desirable, sell or otherwise dispose of an apartment complex which will provide housing for low income individuals with disabilities. Mosaic's capital contribution in BRSLP is recognized by Mosaic using the equity method of accounting.

Mosaic owns all of the issued common stock of BICO, which was incorporated under the laws of Bermuda and is registered as a Class 1 insurer under The Insurance Act of 1978. BICO insures Mosaic for the deductible portion of U.S. workers' compensation and general liability risks. The investment is recognized by Mosaic using the equity method of accounting. A loss from investment in BICO of \$159,647 and a gain of \$1,510,540 for 2010 and 2009, respectively, is included with employee benefits in the consolidated statement of operations and changes in net assets. During 2010 and 2009, Mosaic paid premiums for worker's compensation and other insurance to BICO amounting to \$4,687,765 and \$4,745,310, respectively. BICO paid to Mosaic management fees of \$749,200 and \$500,000 in 2010 and 2009, respectively. The management fees are included in other revenue in the consolidated statements of operations and changes in net assets.

A summary of BICO's balance sheets as of June 30, 2010 and 2009 and statements of income and retained earnings for the years then ended is as follows:

	<u>2010</u>	<u>2009</u>
Assets	\$ <u>13,501,277</u>	<u>12,328,087</u>
Liabilities	7,682,520	6,374,037
Shareholder's equity	<u>5,818,757</u>	<u>5,954,050</u>
Total liabilities and shareholder's equity	<u>13,501,277</u>	<u>12,328,087</u>
Net premiums earned	4,687,765	4,745,310
Losses incurred	(3,887,274)	(2,583,544)
General and administrative expenses	(1,022,402)	(779,652)
Investment income	<u>86,618</u>	<u>128,423</u>
Net income (loss)	(135,293)	1,510,537
Retained earnings, beginning of year	<u>5,704,050</u>	<u>4,193,513</u>
Retained earnings, end of year	\$ <u>5,568,757</u>	<u>5,704,050</u>

In 2009, Mosaic owned all the issued common stock of HRBAI, which provides air transportation services. The investment was recognized by Mosaic using the equity method of accounting. During 2010, Mosaic dissolved HRBAI.

Mosaic does not consolidate the accounting of BRSLP, BICO or HRBAI due to their relative insignificance in relation to Mosaic's consolidated financial statements and operations.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### (8) Notes Payable

Notes payable at June 30, 2010 and 2009 consisted of the following:

	<u>2010</u>	<u>2009</u>
Working capital	\$ 747,000	747,000

Mosaic has working capital loans dated March 15, 1991, due upon demand in the amount of \$747,000 from CIL Realty, Incorporated (CIL). Management does not anticipate these notes to be demanded until the lease obligation is satisfied. Mosaic has granted a security interest in all of its contract rights and accounts receivable in connection with its service delivery in certain group homes financed through a capital lease with CIL as described in Note 9.

The note called for payments of interest only for the first 10 years; these payments ended in 2001. The note further provides that no interest shall accrue after 10 years, and the principal on the note shall be forgiven at such time as Mosaic has met its entire lease obligation as described in Note 9.

#### (9) Long-Term Liabilities

##### Long-Term Debt

A summary of long-term debt at June 30, 2010 and 2009 is as follows:

	<u>2010</u>	<u>2009</u>
Hospital Authority No. 1 of Kearney County, Nebraska Revenue Bonds, Series 2003, due through January 2018, payable in varying annual installments, interest rate of 5.49%, paid semiannually.	\$ 1,393,558	1,529,030
Hospital Authority No. 2 of Douglas County, Nebraska Revenue Refunding Bonds, Series 2008, due through 2013, payable in varying annual installments, interest rates ranging from 3.25% to 3.50%, paid semiannually.	1,605,000	2,105,000
Hospital Authority No. 1 of Kearney County, Nebraska Revenue Bonds, Series 2008, due through 2013, payable in varying installments, interest rate of 4.13%, paid semiannually	660,744	863,608
Real Estate Term Loans, due through 2012, payable in annual installments of \$9,123, interest rates of 3.00%, paid monthly.	203,643	313,119
Village of Rantoul, Illinois Revenue Bonds, Series 2000, due through December 2015, payable in varying annual installments, interest rate of 6.61%, paid semiannually.	711,942	816,187
City of Winfield, Kansas Revenue Bonds, Series A 1999, due through February 2016, payable in varying annual installments, interest rate of 5.66%, paid semiannually.	415,624	472,344
City of Winfield, Kansas Revenue Bonds, Series B 1999, due through February 2016, payable in varying annual installments, interest rate of 5.66%, paid semiannually.	141,637	160,966
City of Osage, Iowa Revenue Bonds, Series 1996, due through March 2020, payable in varying annual installments, interest rate of 4.50%, paid monthly.	990,664	1,070,504

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
City of Garden City, Kansas Economic Development Revenue Bonds, Series 2005, due through June 2020, payable in varying annual installments, interest rate of 5.11%, paid semiannually.	621,754	668,370
Hospital Authority No. 1 of Gage County, Nebraska Revenue Bonds, Series 2010, due through March 2025, payable in semi-annual installments of \$92,258, interest rate of 5.95%, paid semiannually.	1,800,000	--
Hospital Authority No. 1 of Kearney County, Nebraska Revenue Bonds, Series 2010, due through May 2025, payable in semi-annual installments of \$178,877, interest rate of 5.95%, paid semiannually.	3,500,000	--
Nebraska Investment Finance Authority Revenue Bonds, Series 2010, due through May 2025, payable in semi-annual installments of \$359,050, interest rate of 6.04%, paid semiannually.	7,000,000	--
Various promissory notes to Charitable Remainder Annuity Trusts, secured by deeds of trusts on certain real property, monthly interest payments only through specified date or when trusts terminate, interest rates ranging from 6.44% to 8.88%.	884,054	884,054
Various mortgages, payable, in monthly installments, including interest at rates ranging from 6.00% to 7.88%, maturing between 2010 and 2038. These mortgages are secured by real estate in Connecticut, Colorado, Nebraska, Illinois, Wisconsin and Texas.	5,395,404	4,938,623
United States Department of Agriculture (USDA), payable in monthly installments, including interest at a rate of 4.75%, outstanding principal due November 2023. This mortgage payable is secured by all property, equipment and revenue of The Oaks.	1,727,327	1,817,874
U.S. Department of Housing and Urban Development, payable in monthly installments of \$3,438, including interest at a rate of 8.50%, outstanding principal due October 2032. This mortgage payable is secured by all property and equipment of Mosaic Housing Corp I.	412,186	418,131
Line of credit, Wells Fargo Bank, due through December 31, 2012, variable interest rate of 2.38% secured by revenue of Mosaic.	1,744,633	3,038,000
American National Bank note, payable in monthly installments of \$39,304, including interest at a rate of 4.65%, outstanding principal due May 2013. This note payable is secured by all assets of Spectrum Medical Equipment, Inc.	1,250,363	1,653,572
Wells Fargo Bank note, payable in monthly principal installments of \$50,000, interest payable at 2.35%, outstanding principal due June 2017.	4,200,000	--
Line of credit, American National Bank, due through December 31, 2049, interest rate of 4.00%.	244,155	279,155

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
Other long-term debt	37,000	42,481
Total long-term debt	34,939,688	21,071,018
Less - Current maturities of long-term debt	<u>(3,438,002)</u>	<u>(2,170,215)</u>
Long-term debt, excluding current maturities	\$ <u>31,501,686</u>	<u>18,900,803</u>

Hospital Authority No. 1 of Kearney County, Nebraska Series 2003 Revenue Bonds were issued in connection with improvements to the Axtell, Nebraska campus in Kearney County. Under a loan agreement dated January 28, 2003, the proceeds of the bonds were forwarded to Mosaic. The issue is secured by a mortgage/deed of trust in land, improvements and fixtures located in the Axtell program.

Hospital Authority No. 2 of Douglas County, Nebraska Series 2008 Revenue Refunding Bonds were issued to refund other long-term debt. Under a loan agreement dated June 24, 2008, the proceeds of the bonds were forwarded to Mosaic. The issue is secured by the respective programs' accounts receivable and a mortgage/deed of trust in facilities located in the geographic boundaries of Hospital Authority No. 2 of Douglas County, Nebraska.

Hospital Authority No. 1 of Kearney County, Nebraska Series 2008 Revenue Bonds were issued in connection with the construction of improvements to the streets and sanitary sewer system in Axtell, Nebraska. Under loan agreements dated May 7, 2008, the issue is secured by land in Axtell including real property located thereon.

Housing Revenue Bonds Series 2000 were issued to refinance certain prior taxable debt and to acquire, construct, and install facilities in Dwight, Peoria, and Pontiac, Illinois. Under loan agreements dated December 27, 2000, the proceeds of the bonds were forwarded to Mosaic. The issue is secured by a mortgage/deed of trust in land, improvements and fixtures located in Dwight, Peoria, and Pontiac, Illinois.

Housing Revenue Bonds Series 1999 were issued in connection with the construction of living and care facilities in Cowley County, Kansas. Under lease purchase agreement dated February 1, 1999, the proceeds of the bonds were forwarded to Mosaic. The issue is secured by a mortgage/deed of trust in land, improvements and fixtures located in Cowley County, Kansas.

Housing Revenue Bonds Series 1996 were issued in connection with the construction of living and care facilities in Osage, Iowa. Under loan agreements dated September 29, 1995, the proceeds of the bonds were forwarded to Mosaic. The issue is secured by a mortgage/deed of trust in land, improvements and fixtures located in Osage, Iowa.

Hospital Authority No. 1 of Gage County, Hospital Authority No. 1 of Kearney County, Nebraska, and the Nebraska Investment Finance Authority Revenue Bonds, Series 2010, were issued in connection with a project to build 11 homes in the state of Nebraska. Under loan agreements dated March 12, 2010, March 31, 2010, and April 14, 2010, respectively, the proceeds of the bonds were forwarded to Mosaic. The issues are secured by the assets of the related homes.

At June 30, 2010 and 2009, Spectrum Medical Equipment, Inc. had available a \$500,000 line of credit with American National Bank. The line of credit had a balance of \$244,155 and \$279,155 at June 30, 2010 and 2009, respectively, with an interest rate of 4.00%.

At June 30, 2010 and 2009, Mosaic also had available a line of credit of \$9,500,000 with Wells Fargo Bank. Mosaic holds two accounts within this line of credit. The line of credit at June 30, 2010 had a balance of \$1,744,633 with an interest rate of 2.38% and is secured by the revenue of Mosaic. The real estate term loans at June 30, 2010 have a balance of \$203,643 and an interest rate of 3.00%.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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Future maturities of long-term debt as of June 30, 2010 are as follows:

2011	\$	3,438,002
2012		4,010,571
2013		4,933,337
2014		2,087,323
2015		2,617,922
Thereafter		17,852,533

#### Capital Lease Obligations

Mosaic conducts a portion of its operations in leased facilities. For financial reporting purposes, minimum lease rentals relating to client housing have been capitalized. At June 30, 2010, sixteen (16) homes are leased from the Corporation for Independent Living under capital leases.

The related assets and obligations have been recorded using the incremental borrowing rate at the inception of the leases. The leases expire at various dates through 2022, at which time ownership of the leased property will transfer to Mosaic. The value of properties leased under capital leases are as follows:

		<u>2010</u>	<u>2009</u>
Leased facilities and equipment	\$	4,914,576	4,887,224
Less - Accumulated depreciation		<u>(3,640,548)</u>	<u>(3,376,378)</u>
Net leased facilities	\$	<u>1,274,028</u>	<u>1,510,846</u>

The following is a schedule of future minimum lease payments under capital leases, together with the present value of the net minimum lease payments for each of the next five years and in the aggregate:

2011	\$	340,556
2012		276,291
2013		261,034
2014		258,534
2015		254,095
Thereafter		<u>448,148</u>
Total minimum lease payments		1,838,658
Less - Amount representing interest		<u>(505,242)</u>
Present value of net minimum lease payments		1,333,416
Less - Current portion		<u>(216,860)</u>
Long-term obligation under capital leases	\$	<u>1,116,556</u>

Should Mosaic decide to terminate the lease agreements, Mosaic could owe the lessor an additional six months of lease payments following the date of termination.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### (10) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets relate to the following at June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Support of general operations of Mosaic	\$ 2,734,509	2,800,047
Mosaic Housing Corp II capital advance and grant	1,274,900	1,274,900
Mosaic Housing Corp III capital advance	948,600	948,600
Mosaic Housing Corp IV capital advance and grant	479,300	479,300
Mosaic Housing Corp VII capital advance	865,300	865,300
Mosaic Housing Corp XIII capital advance	949,848	949,848
Mosaic Housing Corp IX capital advance	144,077	144,077
Mosaic Housing Corp X capital advance	153,082	153,082
Mosaic Housing Corp XI capital advance	189,179	189,179
Mosaic Housing Corp XIII capital advance	954,400	954,400
Mosaic Housing Corp XII capital advance	991,400	991,400
Mosaic Housing Corp XIV capital advance	1,025,494	1,025,494
Mosaic Housing Corp XV capital advance and grants	1,498,413	1,349,898
Mosaic Housing Corp XVI capital advance	1,444,917	1,444,917
Mosaic Housing Corp XVII capital advance and grants	1,449,200	494,353
Mosaic Housing Corp XVIII capital advance and grants	1,614,500	--
Mosaic Housing Corp XIX capital advance	910,134	--
City of Omaha HOME grants	523,768	523,768
Affordable Housing loans	98,000	98,000
Illinois Housing Development Authority loan	564,500	564,500
Affordable Housing Program loan	50,000	--
City of Fort Collins grant	67,140	72,736
Donor restricted for program purposes	116,170	116,170
	<u>\$ 19,046,831</u>	<u>15,439,969</u>

Capital advances, grants and loans relate to the construction and/or operation of housing projects for low income persons with disabilities and are not required to be repaid so long as the projects comply with appropriate regulations and operate for terms as specified within the advance, grant or loan.

Permanently restricted net assets listed below include endowment funds which are to be held in perpetuity, the income which is expendable for the following:

	<u>2010</u>	<u>2009</u>
Support of general operations of Mosaic	\$ <u>3,321,721</u>	<u>3,075,464</u>

#### (11) Endowment

The Nebraska Uniform Prudent Management of Institutional Funds Act (NUPMIFA) was enacted April 4, 2007. NUPMIFA sets out guidelines to be considered when managing and investing donor restricted endowment funds. On July 1, 2008, Mosaic adopted FASB ASC Topic 958 Subtopic 205 Subtopic 45, *Reporting of Endowment Funds*.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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Mosaic endowments consist of funds established to invest permanently restricted donations. As required by GAAP, net assets associated with endowment funds, including funds designated by Board of Trustees to function as endowments and beneficial interest in trust assets, are classified and reported based on the existence or absence of donor-imposed restrictions.

Mosaic has interpreted NUPMIFA as requiring the preservation of the whole dollar value of the original gift as of the gift date of donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Mosaic 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. Absent any donor-imposed restrictions, interest, dividends and net appreciation of donor-restricted endowment funds is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Mosaic in a manner consistent with the standard of prudence prescribed by NUPMIFA.

In accordance with NUPMIFA, Mosaic considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of Mosaic and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of Mosaic
7. The investment policies of Mosaic

The net asset composition and changes in endowment net assets for the year ended June 30, 2010 and 2009 are as follows:

#### Endowment Net Asset Composition by Type of Fund

		June 30, 2010			
		Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Board-designated endowment funds	\$	27,277,021	--	--	27,277,021
Donor-restricted endowment funds		--	748,156	3,321,721	4,069,877
	\$	<u>27,277,021</u>	<u>748,156</u>	<u>3,321,721</u>	<u>31,346,898</u>
		June 30, 2009			
		Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Board-designated endowment funds	\$	22,639,791	--	--	22,639,791
Donor-restricted endowment funds		--	748,156	3,075,464	3,823,620
	\$	<u>22,639,791</u>	<u>748,156</u>	<u>3,075,464</u>	<u>26,463,411</u>

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

#### Changes in Endowment Net Assets

		Year Ended June 30, 2010			Total
		Unrestricted	Temporarily Restricted	Permanently Restricted	
Net assets, beginning of year	\$	22,639,791	748,156	3,075,464	26,463,411
Investment income (loss)		3,045,891	--	(2,010)	3,043,881
Contributions		2,898,456	--	248,267	3,146,723
Amounts appropriated for expenditure		(1,319,589)	--	--	(1,319,589)
Other changes, Transfer to increase board designated endowment funds		12,472	--	--	12,472
Endowment net assets, end of year	\$	<u>27,277,021</u>	<u>748,156</u>	<u>3,321,721</u>	<u>31,346,898</u>

		Year Ended June 30, 2009			Total
		Unrestricted	Temporarily Restricted	Permanently Restricted	
Net assets, beginning of year	\$	26,603,315	748,156	2,986,300	30,337,771
Investment loss		(4,007,915)	--	(2,215)	(4,010,130)
Contributions		1,440,182	--	91,379	1,531,561
Amounts appropriated for expenditure		(1,588,913)	--	--	(1,588,913)
Other changes, Transfer to increase board designated endowment funds		193,122	--	--	193,122
Endowment net assets, end of year	\$	<u>22,639,791</u>	<u>748,156</u>	<u>3,075,464</u>	<u>26,463,411</u>

#### Return Objectives and Risk Parameters

The primary objective of Mosaic's endowment funds is to generate sufficient funds to support a long-term distribution policy of five percent (5%) of the total balance of endowments to Mosaic. Unrestricted matured deferred gifts including all bequests and other estate gifts will be added to the principal of the Board-designated endowment annually unless otherwise directed by the Board of Directors. Mosaic has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to agencies supported by its endowment, while seeking to maintain the purchasing power of endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity or for a donor-specified period(s) as well as board designated funds. Under this policy, as approved by the Board of Directors, the endowment assets are invested in a manner that is intended to generate sufficient funds to support a long-term distribution policy of five percent (5%) or as otherwise designated by the donor or Board, while minimizing investment risk.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### Strategies Employed for Achieving Objectives

Mosaic relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest & dividends). The organization targets a diversified asset allocation strategy.

The endowment funds will be invested in publicly-traded common stocks and other equity-type securities, fixed income securities, money-market instruments and hedging instruments. The total funds will invest in major asset categories as follows:

	<u>Actual Allocation</u>	<u>Target Allocation Range</u>
Equities	70%	50% to 70%
Fixed income	28%	30% to 50%
Cash equivalents	2%	0% to 10%
Alternatives	0%	0% to 10%

#### Appropriation Policy and How the Investment Objectives Relate to Appropriation Policy

The endowment funds are held in the Mosaic Foundation, which has a policy of distributing to Mosaic each year 5% of all endowment funds. The Foundation considers the long-term expected return on its funds in establishing this policy.

#### **(12) Professional Liability Insurance**

Mosaic's professional liability policy provides coverage on a claims-made basis covering only those claims which have occurred and are reported to the insurance company while the coverage is in force. In the event Mosaic should elect not to purchase insurance from the present carrier or the carrier should elect not to renew the policy, any unreported claims which occurred during the policy year may not be recoverable from the carrier. Mosaic could have exposure on possible incidents that have occurred for which claims will be made in the future, should professional liability insurance not be obtained, should coverage be limited and/or not available. Mosaic also carries an umbrella policy which provides additional coverage on an occurrence basis.

#### **(13) Workers' Compensation**

BICO is a wholly-owned subsidiary of Mosaic (see Note 7). BICO insures Mosaic for the deductible portion of U.S. workers' compensation risks. The deductible reimbursement policy risk was \$500,000 at June 30, 2010 and 2009. BICO has established a letter of credit of \$3,000,000 at June 30, 2010 and 2009, held in favor of Sentry Insurance as the third party administrator on the workers' compensation program as security for all outstanding claims. Premiums paid by Mosaic to BICO are based upon an actuarial analysis.

#### **(14) Employee Benefit Plans**

##### Deferred Compensation Plan

Mosaic offers its employees a deferred compensation plan created in accordance with Internal Revenue Code 403(b). The plan permits all eligible Mosaic employees to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, disability, retirement, death or unforeseeable emergency.

The employee is the beneficial owner of all assets the employee places in the plan.

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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Mosaic may elect to make matching contributions of which the amount is dependent upon employee funded levels and years of service. Vesting requirements are dependent on employee level and years of service. For the year ended June 30, 2010 and 2009, total pension expense of \$1,278,939 and \$1,509,395, respectively, was incurred by Mosaic.

#### Executive Supplemental Benefit Plan

Mosaic adopted an executive supplemental benefit plan (Plan) in 2004 to provide supplemental retirement benefits for a certain number of its employees. When a participant reaches a total age plus years of service equal to seventy-five or more, the participant becomes eligible for post retirement payments (salary continuation) and health care benefits. As of June 30, 2010, only a limited number of employees were eligible to participate in the Plan and only one employee had reached the threshold to be vested in the Plan.

Effective June 30, 2007, Mosaic adopted the recognition and disclosure provisions of FASB ASC Topic 715, *Compensation – Retirement Benefits* (ASC Topic 715). ASC Topic 715 requires companies to recognize the funded status of defined benefit pension and other postretirement plans as a net asset or liability and to recognize changes in that funded status in the year in which the changes occur through other changes in net assets, to the extent those changes are not included in the net periodic cost. The funded status reported on the consolidated balance sheet as of June 30, 2010 and 2009 under ASC Topic 715 was measured as the difference between the fair value of plan assets and the benefit obligation.

The following summarizes the recognition of the executive supplemental benefit plan in the financial statements at June 30 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Balance Sheets:		
Liability for post-retirement benefits -		
Salary continuation	\$ 1,366,713	1,215,077
Health benefits	390,996	352,254
	<u>\$ 1,757,709</u>	<u>1,567,331</u>
Statements of operations and changes in net assets:		
Included with employee benefits -		
Salary continuation	\$ 196,219	178,651
Health benefits	41,773	11,593
	<u>\$ 237,992</u>	<u>190,244</u>
Postretirement benefit related changes other than net periodic cost -		
Salary continuation	\$ (28,546)	(154,529)
Health benefits	9,450	74,912
	<u>\$ (19,096)</u>	<u>(79,617)</u>

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### *Projected Benefit Obligation – Salary Continuation*

The following table summarizes the projected benefit obligation, the fair value of plan assets, and the funded status at the measurement dates of June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Changes to benefit obligation:		
Benefit obligation at beginning of period	\$ 1,215,077	1,074,362
Service cost	46,405	41,332
Interest cost	84,205	64,355
Assumption change	135,956	(19,076)
Plan change	--	116,593
Experience gain	<u>(114,930)</u>	<u>(62,489)</u>
Benefit obligation at end of period	<u>1,366,713</u>	<u>1,215,077</u>
Fair value of plan assets at end of period	<u>--</u>	<u>--</u>
Funded status at end of period	\$ <u>(1,366,713)</u>	\$ <u>(1,215,077)</u>
Amounts recognized in the consolidated balance sheets, Noncurrent liabilities	\$ <u>1,366,713</u>	\$ <u>1,215,077</u>

The following is a summary of the components of net periodic postretirement benefit cost for the years ended June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Service cost during the period	\$ 46,405	41,332
Interest cost on projected benefit obligation	84,205	64,355
Amortization	<u>65,609</u>	<u>72,964</u>
Net periodic pension cost	\$ <u>196,219</u>	\$ <u>178,651</u>

Items not yet recognized as a component of periodic pension cost at June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Net loss	\$ <u>453,351</u>	\$ <u>481,897</u>

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### *Accumulated Postretirement Benefit Obligation – Health Benefits*

The following table summarizes the accumulated post retirement benefit obligation, the fair value of plan assets, and the funded status at the measurement dates of June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Changes to benefit obligation:		
Benefit obligation at beginning of period	\$ 352,254	278,230
Service cost	4,952	3,509
Interest cost	24,340	17,389
Assumption change	51,228	67,806
Experience gain	<u>(41,778)</u>	<u>(14,680)</u>
Benefit obligation at end of period	<u>390,996</u>	<u>352,254</u>
Fair value of plan assets at end of period	<u>--</u>	<u>--</u>
Funded status at end of period	\$ <u>(390,996)</u>	\$ <u>(352,254)</u>
Amounts recognized in the consolidated balance sheets, Noncurrent liabilities	\$ <u>390,996</u>	<u>352,254</u>

The following is a summary of the components of net periodic pension cost for the years ended June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Service cost during the period	\$ 4,952	3,509
Interest cost on accumulated postretirement benefit obligation	24,340	17,389
Amortization	<u>12,481</u>	<u>(9,305)</u>
Net periodic pension cost	\$ <u>41,773</u>	<u>11,593</u>

Items not yet recognized as a component of periodic pension cost at June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Net experience (gain) loss	\$ <u>22,981</u>	<u>32,429</u>

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### Actuarial Assumptions

The following are the actuarial assumptions used by the Plans to develop the components of the pension projected benefit obligation and accumulated postretirement benefit obligation for the year ended June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Discount rate – Pension	4.62%	6.93%
Discount rate – Health	3.49	6.91
Rate of increase in compensation levels	5.00	5.00

#### **(15) Health Care Plan**

Mosaic provides comprehensive medical and vision care benefits and an employee assistance program for eligible employees and their dependents through participation in a multi-employer Voluntary Employee's Beneficiary Association (VEBA). In addition, educational compensation benefits are provided for participating employees through the VEBA. Mosaic contributes 100% of the core medical plan cost (single person coverage) based on actuarial determined rates. For the years ended June 30, 2010 and 2009, total health insurance expense of \$15,915,676 and \$15,220,795 was incurred by Mosaic.

To the extent the VEBA has plan liabilities in excess of plan assets, future employer contributions may be increased to continue to provide benefits to eligible employees and their dependents of Mosaic and its affiliates.

#### **(16) Concentrations of Credit Risk**

The majority (more than 90%) of Mosaic's program service activity is with individuals who are beneficiaries of the various states' Medicaid programs. The Medicaid programs' ability to honor their contracts is dependent on State and Federal funding of the programs.

Mosaic has investments in marketable equity securities, corporate bonds and real estate. The value of these investments are determined by market value and are not insured or collateralized.

The investments are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investments, it is at least reasonably possible that changes in values of investment will occur in the near term and that such changes could materially affect net assets of Mosaic.

#### **(17) Commitments and Contingencies**

##### Operating Leases

Mosaic conducts a portion of its operations in facilities that are leased on a month-to-month basis and, therefore, are not included in the minimum rental commitments shown below.

The minimum rental commitments under operating leases, which includes facilities, vehicles and equipment, are as follows for years ended June 30:

2011	\$	3,169,651
2012		2,284,318
2013		1,314,507
2014		884,443
2015		542,036

## Mosaic and Affiliates

### Notes to Consolidated Financial Statements June 30, 2010 and 2009

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#### Litigation

The health and human services industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government health and human services program participation requirements, reimbursements for client services, and Medicaid fraud and abuse. Violations of these laws and regulations could result in expulsion from government health care programs together with the imposition of significant fines and penalties, as well as significant repayments for client services previously billed.

Management believes that Mosaic is in compliance with applicable government laws and regulations as they see apply to the areas of fraud and abuse. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time.

Mosaic is involved in litigation arising in the normal course of business. After consultation with legal counsel, management estimates these matters will be resolved without material adverse affect on Mosaic's future financial position or results from operations.

#### (18) **Functional Expenses**

Mosaic provides care, rehabilitative and vocational services to individuals with disabilities within its geographic location. Expenses related to providing these services are as follows:

	<u>2010</u>	<u>2009</u>
Program services	\$ 171,000,273	171,414,867
General and administrative	16,725,997	17,833,881
Fundraising	1,787,369	2,059,912
Investment management fees	<u>123,061</u>	<u>139,596</u>
	<u>\$ 189,636,700</u>	<u>191,448,256</u>

**Independent Auditor's 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  
Mosaic and Affiliates  
Omaha, Nebraska:

We have audited the consolidated financial statements of Mosaic and Affiliates as of and for the year ended June 30, 2010, and have issued our report thereon dated October 15, 2010. 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.

*Internal Control Over Financial Reporting*

In planning and performing our audit, we considered Mosaic's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of Mosaic's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Mosaic's internal control over financial reporting

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.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

*Compliance and Other Matters*

As part of obtaining reasonable assurance about whether Mosaic and Affiliates' consolidated financial statements are free of 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*.

This report is intended solely for the information and use of the audit committee, management and federal and state awarding agencies, and is not intended to be and should not be used by anyone other than those specified parties.

*Seim, Johnson, Sestak + Quist, LLP*

Omaha, Nebraska,  
October 15, 2010.

## **Mosaic and Affiliates**

### **Independent Auditor's Comments on Resolution of Prior Audit Findings June 30, 2010**

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There were no prior year audit findings.