

ABILITY360 AND SUBSIDIARY
CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED JUNE 30, 2017 AND 2016

**ABILITY360 AND SUBSIDIARY
TABLE OF CONTENTS
YEARS ENDED JUNE 30, 2017 AND 2016**

INDEPENDENT AUDITORS' REPORT	1
CONSOLIDATED FINANCIAL STATEMENTS	
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION	3
CONSOLIDATED STATEMENTS OF ACTIVITIES	4
CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES	6
CONSOLIDATED STATEMENTS OF CASH FLOWS	8
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS	9

INDEPENDENT AUDITORS' REPORT

Board of Directors
Ability360 and Subsidiary
Phoenix, Arizona

We have audited the accompanying consolidated financial statements of Ability360 and Subsidiary, which comprise the consolidated statements of financial position as of June 30, 2017 and 2016, and the related consolidated statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Board of Directors
Ability360 and Subsidiary

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Ability360 and Subsidiary as of June 30, 2017 and 2016, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Phoenix, Arizona
November 14, 2017

ABILITY360 AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
JUNE 30, 2017 AND 2016

ASSETS	<u>2017</u>	<u>2016</u>
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 10,374,806	\$ 8,600,792
Certificates of Deposit	-	6,465,486
Designated Cash	26,383	32,749
Accounts Receivable, Net	8,205,294	6,059,265
Prepaid Expenses and Other Assets	94,702	107,002
Total Current Assets	<u>18,701,185</u>	<u>21,265,294</u>
INVESTMENTS	1,750,603	668,922
PROPERTY AND EQUIPMENT, NET	<u>32,124,419</u>	<u>33,016,431</u>
Total Assets	<u><u>\$ 52,576,207</u></u>	<u><u>\$ 54,950,647</u></u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Current Maturity of Note Payable	\$ -	\$ 4,684,342
Accounts Payable	229,968	233,091
Accrued Payroll and Related Expenses	945,353	1,182,898
Compensated Absences Payable	286,430	293,706
Deferred Revenue	197,932	214,557
Other Liabilities	12,978	30,103
Interest Rate Swap Liability	-	174,195
Total Current Liabilities	<u>1,672,661</u>	<u>6,812,892</u>
NET ASSETS		
Unrestricted	50,856,148	47,938,894
Temporarily Restricted	<u>47,398</u>	<u>198,861</u>
Total Net Assets	<u>50,903,546</u>	<u>48,137,755</u>
Total Liabilities and Net Assets	<u><u>\$ 52,576,207</u></u>	<u><u>\$ 54,950,647</u></u>

See accompanying Notes to Consolidated Financial Statements.

**ABILITY360 AND SUBSIDIARY
CONSOLIDATED STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2017**

	Unrestricted	Temporarily Restricted	Total
SUPPORT AND REVENUE			
Grants and Contracts	\$ 43,512,340	\$ -	\$ 43,512,340
Contributions and Donations	748,056	-	748,056
Program Income	465,300	-	465,300
Interest and Dividends	70,356	-	70,356
Unrealized Losses on Investments	(14,586)	-	(14,586)
Realized Gains on Investments	90,264	-	90,264
Rental Income	489,771	-	489,771
Other	134,176	-	134,176
Total Support and Revenue Before Net Assets Released from Restrictions	45,495,677	-	45,495,677
Net Assets Released from Restrictions	151,463	(151,463)	-
Total Support and Revenue	45,647,140	(151,463)	45,495,677
EXPENSES, GAINS, AND LOSSES			
Program Services:			
Personal Assistant Services	35,551,948	-	35,551,948
Community Integration	4,536,153	-	4,536,153
Support Services:			
Administration	2,739,886	-	2,739,886
Total Expenses	42,827,987	-	42,827,987
Bad Debts Expense	76,094	-	76,094
Change in Value of Interest Rate Swap	(174,195)	-	(174,195)
Total Expenses, Gains, and Losses	42,729,886	-	42,729,886
CHANGES IN NET ASSETS	2,917,254	(151,463)	2,765,791
Net Assets - Beginning of Year	47,938,894	198,861	48,137,755
NET ASSETS - END OF YEAR	<u>\$ 50,856,148</u>	<u>\$ 47,398</u>	<u>\$ 50,903,546</u>

See accompanying Notes to Consolidated Financial Statements.

**ABILITY360 AND SUBSIDIARY
CONSOLIDATED STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2016**

	Unrestricted	Temporarily Restricted	Total
SUPPORT AND REVENUE			
Grants and Contracts	\$ 41,551,852	\$ -	\$ 41,551,852
Contributions and Donations	236,686	180,000	416,686
Program Income	571,853	-	571,853
Interest and Dividends	61,785	-	61,785
Unrealized Losses on Investments	(59,379)	-	(59,379)
Realized Gains on Investments	27,546	-	27,546
Rental Income	479,087	-	479,087
Other	110,729	-	110,729
Total Support and Revenue Before Net Assets Released from Restrictions	42,980,159	180,000	43,160,159
Net Assets Released from Restrictions	100,000	(100,000)	-
Total Support and Revenue	43,080,159	80,000	43,160,159
EXPENSES, GAINS, AND LOSSES			
Program Services:			
Personal Assistant Services	34,685,683	-	34,685,683
Community Integration	4,147,046	-	4,147,046
Support Services:			
Administration	2,913,570	-	2,913,570
Total Expenses	41,746,299	-	41,746,299
Recovery of Bad Debts	(10,997)	-	(10,997)
Change in Value of Interest Rate Swap	(224,764)	-	(224,764)
Total Expenses, Gains, and Losses	41,510,538	-	41,510,538
CHANGES IN NET ASSETS	1,569,621	80,000	1,649,621
Net Assets - Beginning of Year	46,369,273	118,861	46,488,134
NET ASSETS - END OF YEAR	<u>\$ 47,938,894</u>	<u>\$ 198,861</u>	<u>\$ 48,137,755</u>

See accompanying Notes to Consolidated Financial Statements.

ABILITY360 AND SUBSIDIARY
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
YEAR ENDED JUNE 30, 2017

	Program Services			Support Services	Total Expenses
	Personal Assistant Services	Community Integration	Total Program Services	Administration	
Salaries and Related Payroll Expense	\$ 34,454,963	\$ 2,358,352	\$ 36,813,315	\$ 990,689	\$ 37,804,004
Home Modification Costs	-	680,460	680,460	-	680,460
Office Expenses and Postage	82,689	66,644	149,333	28,441	177,774
Training and Tuition	477	12,184	12,661	53,141	65,802
Public Relations/Information	-	26,943	26,943	100,866	127,809
Professional Services	21,052	56,044	77,096	15,960	93,056
Occupancy and Communications	375,801	480,843	856,644	117,145	973,789
Insurance	77,421	10,053	87,474	26,858	114,332
Equipment Rental and Repairs	182,674	107,559	290,233	98,949	389,182
Travel and Mileage	75,179	52,572	127,751	21,277	149,028
Printing and Publications	20,738	33,851	54,589	15,511	70,100
Interest and Bank Charges	-	-	-	276,145	276,145
Meetings and Conferences	-	15,253	15,253	10,818	26,071
Other Expenses	90,412	464,853	555,265	25,713	580,978
Building Expenses	-	-	-	265,871	265,871
Depreciation	170,542	170,542	341,084	692,502	1,033,586
	<u>\$ 35,551,948</u>	<u>\$ 4,536,153</u>	<u>\$ 40,088,101</u>	<u>\$ 2,739,886</u>	<u>\$ 42,827,987</u>
Total Functional Expenses	<u>\$ 35,551,948</u>	<u>\$ 4,536,153</u>	<u>\$ 40,088,101</u>	<u>\$ 2,739,886</u>	<u>\$ 42,827,987</u>

See accompanying Notes to Consolidated Financial Statements.

ABILITY360 AND SUBSIDIARY
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
YEAR ENDED JUNE 30, 2016

	Program Services			Support Services	Total Expenses
	Personal Assistant Services	Community Integration	Total Program Services	Administration	
Salaries and Related Payroll Expense	\$ 33,607,502	\$ 2,185,272	\$ 35,792,774	\$ 972,462	\$ 36,765,236
Home Modification Costs	-	710,442	710,442	-	710,442
Office Expenses and Postage	88,981	60,612	149,593	30,212	179,805
Training and Tuition	4,259	15,114	19,373	52,192	71,565
Public Relations/Information	-	18,772	18,772	124,022	142,794
Professional Services	20,843	102,952	123,795	7,687	131,482
Occupancy and Communications	368,278	253,788	622,066	135,564	757,630
Insurance	78,144	11,402	89,546	23,405	112,951
Equipment Rental and Repairs	155,039	108,062	263,101	110,922	374,023
Travel and Mileage	87,707	48,936	136,643	31,086	167,729
Printing and Publications	33,902	64,825	98,727	22,802	121,529
Interest and Bank Charges	-	-	-	379,170	379,170
Meetings and Conferences	-	20,978	20,978	28,269	49,247
Other Expenses	68,115	372,978	441,093	30,273	471,366
Building Expenses	-	-	-	263,377	263,377
Depreciation	172,913	172,913	345,826	702,127	1,047,953
	<u>\$ 34,685,683</u>	<u>\$ 4,147,046</u>	<u>\$ 38,832,729</u>	<u>\$ 2,913,570</u>	<u>\$ 41,746,299</u>
Total Functional Expenses					

See accompanying Notes to Consolidated Financial Statements.

**ABILITY360 AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2017 AND 2016**

	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Changes in Net Assets	\$ 2,765,791	\$ 1,649,621
Adjustments to Reconcile Changes in Net Assets to Net Cash Provided by Operating Activities:		
Depreciation	1,033,586	1,047,953
Change in Provision for Doubtful Accounts	13,988	(64,845)
Loss on Disposal of Property and Equipment	8,530	-
Amortization of Debt Issuance Costs	-	5,696
Reinvested Investment Earnings	(1,517)	-
Net Realized and Unrealized (Gains) Losses on Investments	(75,678)	31,833
Change in Value of Interest Rate Swap Liability	(174,195)	(224,764)
Increase (Decrease) in Cash Resulting from Changes in:		
Accounts Receivable	(2,160,017)	(93,395)
Pledges Receivable	-	100,000
Prepaid Expenses and Other Assets	12,300	(9,826)
Accounts Payable	(3,123)	(122,163)
Accrued Payroll and Related Expenses	(237,545)	141,922
Compensated Absences Payable	(7,276)	30,874
Deferred Revenue	(16,625)	102,402
Other Liabilities	(17,125)	(61,526)
Net Cash Provided by Operating Activities	1,141,094	2,533,782
CASH FLOWS FROM INVESTING ACTIVITIES		
Maturities of Certificates of Deposit	6,465,486	18,935
Proceeds from Sale of Investments	1,391	-
Purchases of Investments	(1,005,877)	-
Decrease in Designated Cash for a Sports Complex	6,366	627,205
Purchases of Property and Equipment	(150,104)	(55,887)
Net Cash Provided by Investing Activities	5,317,262	590,253
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of Note Payable	(4,684,342)	(597,996)
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,774,014	2,526,039
Cash and Cash Equivalents - Beginning of Year	8,600,792	6,074,753
CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 10,374,806	\$ 8,600,792
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash Paid for Interest	\$ 229,147	\$ 313,666

See accompanying Notes to Consolidated Financial Statements.

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Ability360 was organized as a nonprofit corporation in May 1984 under the laws of the state of Arizona. Ability360 offers a full range of empowering programs for individuals with disabilities and family members with disability concerns. Ability360's programs include independent living skills instruction, peer support, information and referral, advocacy, home modifications, social and recreational programs, early intervention and outreach to rehabilitation hospitals, community reintegration from nursing homes, youth transition, personal assistance services, social security work incentives and benefits counseling, and employment services for SSDI and SSI beneficiaries.

ABIL Development, LLC was incorporated in the state of Arizona on February 1, 2007, as a limited liability company. Ability360 is the sole member of ABIL Development, LLC and Ability360 has an economic interest in and exercises control over ABIL Development, LLC. The purpose of ABIL Development, LLC is to carry out the programs that complement the activities of Ability360.

Consolidated Financial Statements

The consolidated financial statements include both the accounts of Ability360 and ABIL Development, LLC (collectively referred to as Ability360). All of the financial activities and balances of these organizations are included in these consolidated financial statements. All significant interorganization accounts and transactions have been eliminated in consolidation.

The consolidated financial statements of Ability360 and Subsidiary have been prepared on the accrual basis of accounting. The significant accounting policies followed are described below to enhance the usefulness of the consolidated financial statements to the reader.

Basis of Presentation

The Organization's financial statements are presented in accordance with the American Institute of Certified Public Accountants (AICPA) Not-for-Profit Industry Guidance within the Financial Accounting Standards Board (FASB) Codification (Guidance). Under the Guidance, the Organization is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets as follows:

Unrestricted Net Assets

Unrestricted net assets are not subject to donor-imposed stipulations and are those currently available at the discretion of the board of directors for use in Ability360's operations, in accordance with its bylaws. Temporarily restricted contributions received and expended in the same year are classified as unrestricted.

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Presentation (Continued)

Temporarily Restricted Net Assets

Temporarily restricted net assets are those which are subject to donor-imposed stipulations that will be met by Ability360 and/or the passage of time.

Permanently Restricted Net Assets

Permanently restricted net assets are those which represent permanent endowments where it is stipulated by donors that the principal remain in perpetuity and only the income is available as unrestricted or temporarily restricted, as per the endowment agreements. At June 30, 2017 and 2016, Ability360 had no permanently restricted net assets.

Use of Estimates in the Preparation of Consolidated Financial Statements

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make a number of 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 and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents consist of short-term, highly liquid investments that are both (a) readily convertible to known amounts of cash; and (b) so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. Generally, only investments with original maturities of three months or less, when purchased, meet this definition.

Accounts Receivable

Accounts receivable consist primarily of amounts due from various agencies and are unsecured. Accounts receivable are stated at the amount management expects to collect. The carrying amount of accounts receivable is reduced by a valuation allowance that reflects management's best estimate of amounts that will not be collected. Management provides for probable, uncollectible amounts through a charge to operations and an increase to a valuation allowance based on the assessment of the current status of individual balances. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a decrease to accounts receivable.

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Pledges Receivable

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. Conditional promises to give are not included as support until the conditions are substantially met. There are no pledges receivables as of June 30, 2017 and 2016.

Investments

Investments in marketable securities with readily determinable fair values and all investments in debt securities are valued at their fair values in the consolidated statements of financial position. Investment income (including interest and dividends) and realized and unrealized gains and losses are reported in the consolidated statements of activities under support and revenue.

Property and Equipment

Purchased property and equipment are initially recorded at cost, and donated property and equipment are recorded at fair value at the date of gift to Ability360. Such donations are reported as unrestricted support unless the donor has restricted the donated assets to a specific purpose. Maintenance and repairs are charged to operations when incurred. Betterments and renewals in excess of \$2,500 are capitalized. When property and equipment is sold or otherwise disposed of, the asset and related accumulated depreciation and amortization accounts are relieved, and any gain or loss is included in operations. Depreciation and amortization is provided using the straight-line method over the respective useful lives of the assets, which range from 3 to 50 years. Leasehold improvements are amortized over the shorter of the useful lives of the improvements or the lease terms.

Impairment of Long-Lived Assets

Ability360 reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. Management does not believe that there were any impairments as of June 30, 2017 and 2016.

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Debt Issuance Costs

During 2008, Ability360 incurred \$159,489 of costs in connection with the long-term debt disclosed in Note 9. These costs were deferred and were being amortized over the term of the loan using the straight-line method (which approximates the interest method). Accumulated amortization of these debt issuance costs were \$- and \$159,489 at June 30, 2017 and 2016, respectively, and was paid off during June 30, 2017.

Contributions

Ability360 accounts for contributions and grants in accordance with the Audit Guide and they are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. All donor-restricted support is reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions. However, if a restriction is fulfilled in the same time period in which the contribution is received, Ability360 reports the support as unrestricted.

Grants and Contracts

Grants and contracts consist of governmental reimbursements at contracted rates. These revenues are recognized when the related services are performed.

Derivative Financial Instruments

Ability360 was a party to an interest rate swap agreement to hedge the cash flow effects of fluctuations in interest rate related to its long-term debt instrument. The net amount receivable or payable associated with the interest rate swap agreement was recorded and reflected on the consolidated statements of financial position.

Income Taxes

Ability360 qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code and, therefore, there is no provision for federal or state corporate income taxes. In addition, Ability360 has been determined by the Internal Revenue Service not to be a private foundation within the meaning of Section 509(a) of the Code.

ABIL Development, LLC is a limited liability company incorporated in the state of Arizona which is a pass-through entity. All income or loss of this entity is reported at the Ability360 level.

Both Organizations remain subject to income taxes on any net income that is derived from a trade or business, regularly carried on and not in furtherance of the purpose for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the consolidated financial statements taken as a whole.

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Allocation of Functional Expenses

The costs of providing the various programs and other activities have been summarized on a functional basis in the consolidated statements of functional expense. Accordingly, certain costs have been allocated among the programs and support services benefited. The allocation methods used are subject to a degree of estimation by management. Ability360 directly allocates certain expenses to the various functions to which they apply.

NOTE 2 CASH AND CASH EQUIVALENTS

Cash and cash equivalents at June 30 consist of the following:

	2017	2016
Cash on Hand	\$ 647	\$ 647
Checking Account Balances	7,114,175	7,850,763
Money Market Funds	3,259,984	749,382
Total Cash and Cash Equivalents	<u>\$ 10,374,806</u>	<u>\$ 8,600,792</u>

NOTE 3 INVESTMENTS IN CERTIFICATES OF DEPOSIT

At June 30, 2017, Ability360 had \$-0- in certificates of deposit.

At June 30, 2016, Ability360 had \$6,465,486 in certificates of deposit which were recorded at cost includes accrued interest which approximates fair value. These certificates of deposit matured in fiscal year 2017, earning interest from 0.60% to 1.150%.

NOTE 4 ACCOUNTS RECEIVABLE

Ability360 receives a substantial amount of revenue from grants and contracts. Ability360's accounts receivable at June 30 consist of the following:

	2017	2016
Mercy Care	\$ 5,509,946	\$ 3,827,555
Bridgeway	1,263,839	924,752
Evercare Select/United Health Care	1,192,518	959,263
Other	444,027	538,743
Total	<u>8,410,330</u>	<u>6,250,313</u>
Less: Allowance for Doubtful Accounts	(205,036)	(191,048)
Accounts Receivable, Net	<u>\$ 8,205,294</u>	<u>\$ 6,059,265</u>

ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016

NOTE 5 FAIR VALUE OF FINANCIAL INSTRUMENTS

In determining fair value, Ability360 uses various valuation approaches within the fair value measurement framework. Fair value measurements are determined based on the assumptions that market participants would use in pricing an asset or liability.

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

Level 1 – Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that Ability360 has the ability to access.

Level 2 – Inputs to the valuation methodology include:

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

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 – Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable, such as pricing models, discounted cash flow models, and similar techniques not based on market, exchange, dealer, or broker-traded transactions.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 5 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

A description of the valuation methodologies used for financial instruments follows:

Investments

Equity securities, corporate bonds, government issued securities, money market funds, and other funds listed on a national market or exchange are valued at the last sales price, or if there is no sale and the market is still considered active, at the last transaction price before year-end. Such securities are classified within Level 1 of the valuation hierarchy.

Debt securities consisting of government agency debt obligations are generally valued at the most recent price of the equivalent quoted yield for such securities, or those of comparable maturity, quality, and type. There are no directly held debt securities in the investment portfolio. Debt securities are generally classified within Level 2 of the valuation hierarchy.

Hedge funds, private equity, venture capital, and other investments for which there is not an active market are valued at the quoted market price for underlying marketable securities or an estimate of underlying asset fair values as determined in good faith by the general partner. These alternative investments are classified within Level 3 of the valuation hierarchy.

Ability360 also invests in the Arizona Community Foundation, Inc. (ACF) pool. The fair value of these investments is based on its investment percentage in the investment pool. The ACF pool is invested in cash, equity securities, bonds, and other investments. This investment is classified within Level 3 of the valuation hierarchy.

Interest Rate Swap Agreement

The fair value of interest rate swaps was estimated by a third party using a model that builds a yield curve from market data for actively traded securities at various times and maturities and takes into account current interest rates and the current credit worthiness of the respective counterparties. Such securities are classified within Level 2 of the valuation hierarchy.

ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016

NOTE 5 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although Ability360 believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table presents assets and liabilities measured at fair value by classification within the fair value hierarchy as of June 30, 2017:

	Level 1	Level 2	Level 3	Total
Fixed Income	\$ -	\$ 148,501	\$ -	\$ 148,501
Equity	568,466	-	-	568,466
Mutual Funds	250,997	-	-	250,997
Exchange-Traded Products	7,555	-	-	7,555
Cash and Cash Equivalents	-	-	-	20,378
Pooled Investments:				
Arizona Community Foundation	-	-	754,706	754,706
Total Investments	<u>\$ 827,018</u>	<u>\$ 148,501</u>	<u>\$ 754,706</u>	<u>\$ 1,750,603</u>

The following table presents assets and liabilities measured at fair value by classification within the fair value hierarchy as of June 30, 2016:

	Level 1	Level 2	Level 3	Total
Pooled Investments:				
Arizona Community Foundation	\$ -	\$ -	\$ 668,922	\$ 668,922
Total Investments	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 668,922</u>	<u>\$ 668,922</u>
Interest Rate Swap Liability (Note 9)	<u>\$ -</u>	<u>\$ (174,195)</u>	<u>\$ -</u>	<u>\$ (174,195)</u>

The following is a reconciliation of the beginning and ending balances of assets measured at fair value on a recurring basis using significant unobservable (Level 3) inputs during the years ended June 30:

	2017	2016
Balance - Beginning of Year	\$ 668,922	\$ 697,795
Realized and Unrealized Gains (Losses)	85,784	(28,873)
Balance - End of Year	<u>\$ 754,706</u>	<u>\$ 668,922</u>

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 6 PROPERTY AND EQUIPMENT

Property and equipment at June 30 consist of the following:

	<u>2017</u>	<u>2016</u>
Land	\$ 366,662	\$ 367,671
Buildings	35,565,843	35,565,843
Swimming Pool	984,951	941,773
Furniture, Equipment, and Vehicles	1,862,086	2,292,399
Leasehold Improvements	<u>3,203,675</u>	<u>3,226,822</u>
Total	41,983,217	42,394,508
Less: Accumulated Depreciation and Amortization	<u>(9,858,798)</u>	<u>(9,378,077)</u>
Property and Equipment, Net of Accumulated Depreciation and Amortization	<u>\$ 32,124,419</u>	<u>\$ 33,016,431</u>

Depreciation and amortization expense charged to operations was \$1,033,586 and \$1,047,953 for the years ended June 30, 2017 and 2016, respectively.

NOTE 7 RENTALS UNDER OPERATING LEASES

Ability360 leases office space to unrelated parties. Certain of these leases contain options to renew. Rental revenue recognized by Ability360 was \$480,371 and \$479,087 for the years ended June 30, 2017 and 2016, respectively.

The future minimum rental income under these operating leases is as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2018	\$ 392,030
2019	196,408
2020	45,249
2021	<u>3,605</u>
Total	<u>\$ 637,292</u>

Management believes that leases that expire will be renewed; thus, it is anticipated that future rental revenue will approximate the amount recognized in fiscal 2017.

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 8 NOTE PAYABLE

Note payable at June 30 consisted of the following:

	2017	2016
<p>Note payable to US Bank, NA; amount not to exceed \$12,375,000, including interest at 1.15% in excess of one-month LIBOR (.47% and .19% at June 30, 2016 and 2015, respectively) through March 28, 2014, 1.00% in excess of one-month LIBOR through March 28, 2017; payable on March 28, 2014, a payment in an amount equal to the greater of \$1,548,600 or the amount necessary to reduce the outstanding principal balance such that the outstanding principal balance after the payment of such amount is equal to 65% of the then current appraised value of the Project. Ability360 paid down \$6,395,000 of principal on April 1, 2014. Due in monthly payments of \$49,833 with the entire outstanding principal balance of \$4,186,012 due and payable at the maturity date of April 1, 2017; secured by deed of trust.</p>	\$ -	\$ 4,684,342
Total	-	4,684,342
Less: Current Maturities	-	4,684,342
Long-Term Maturities of Notes Payable	\$ -	\$ -

NOTE 9 INTEREST RATE SWAP AGREEMENT

In March 2007, ABIL Development, LLC entered into an interest rate swap agreement, a fair value hedge, with a financial institution. ABIL Development, LLC pays a fixed rate of interest of 5.16% on a notional amount of \$12,375,000 for a period of 18 years. The financial institution pays ABIL Development, LLC interest based on LIBOR. The purpose of this derivative financial instrument was to hedge the risk of higher interest rates in the future. The swap agreement was restructured effective April 1, 2014 with a \$837,250 prepayment, the due date shortened to March 28, 2017, and the notional amount reduced to \$5,980,000. The fair value of the interest rate swap agreement was a liability of \$-0- and \$174,195 as of June 30, 2017 and 2016, respectively. The interest rate swap was paid off during the fiscal year ended June 30, 2017.

**ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016**

NOTE 10 OPERATING LEASES

Ability360 leases office space and office equipment under the provisions of noncancelable operating leases. Rental expense under the terms of the operating leases was \$180,817 and \$139,909 for the years ended June 30, 2017 and 2016, respectively. Certain operating leases provide for renewal options.

The future minimum rental payments under these operating leases are as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2018	\$ 57,722
2019	43,811
2020	41,880
2021	7,669
2022	1,256
Total	<u>\$ 152,338</u>

NOTE 11 TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following:

	<u>2017</u>	<u>2016</u>
Cash for Sports Complex	\$ 28,537	\$ 180,000
Cash for Mast House Replacements	18,861	18,861
Total Temporarily Restricted Net Assets	<u>\$ 47,398</u>	<u>\$ 198,861</u>

A summary of net assets released from restrictions is as follows:

	<u>2017</u>	<u>2016</u>
Sports Complex	\$ 100,000	\$ 100,000
Arizona Diamondbacks Foundation	51,463	-
Total	<u>\$ 151,463</u>	<u>\$ 100,000</u>

NOTE 12 DONATED GOODS AND SERVICES

Ability360 receives donated services from a variety of unpaid volunteers assisting in various programs. No amounts have been recognized in the accompanying consolidated statements of activities because the accounting criteria for recognition of such volunteer efforts have not been satisfied.

ABILITY360 AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016

NOTE 13 RETIREMENT PLAN

Ability360 maintains a 403(b) thrift plan which is available to all full-time employees. Under the plan, employees can elect to have their salary reduced on a pre-tax basis, based on a percentage of compensation. Ability360 has a matching contribution requirement up to 4% for the years ended June 30, 2017 and 2016. Ability360's retirement plan expense was \$148,351 and \$143,743 for the years ended June 30, 2017 and 2016, respectively.

NOTE 14 CONCENTRATION RISK

Ability360 received approximately 79% and 81% of their revenue from three government contracts during the years ended June 30, 2017 and 2016, respectively. Approximately 94% and 91% of the accounts receivable balance is due from three government contracts as of June 30, 2017 and 2016, respectively.

Ability360 maintains all of its cash with banks located in Arizona. Balances on deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to specified limits. Balances in excess of FDIC limits are uninsured. As of June 30, 2017 and 2016, a portion of cash balances at financial institutions exceeded the balance insured by the FDIC.

NOTE 15 COMMITMENTS AND CONTINGENCIES

Ability360 participates in a number of federal and state assisted grant and contract programs which are subject to financial and compliance audits. Accordingly, Ability360's compliance with applicable grant or contract requirements may be determined at some future date. The amount, if any, of expenditures or fees for units of service which may be disallowed by the granting or contracting agencies cannot be determined at this time, although Ability360's management expects such amounts, if any, to be immaterial.

Ability360 is contingently liable in respect to claims incidental to the ordinary course of its operations. In the opinion of management, such matters will not have a material adverse effect on Ability360's financial position, operations, or liquidity. Therefore, no provision has been made in the accompanying consolidated financial statements for losses, if any, that might result from the ultimate outcome of these matters.

NOTE 16 SUBSEQUENT EVENTS

Management evaluated subsequent events through November 14, 2017, the date the consolidated financial statements were available to be issued. Events or transactions occurring after June 30, 2017, but prior to November 14, 2017, that provided additional evidence about conditions that existed at June 30, 2017, have been recognized in the consolidated financial statements for the year ended June 30, 2017. Events or transactions that provided evidence about conditions that did not exist at June 30, 2017, but arose before the consolidated financial statements were available to be issued have not been recognized in the consolidated financial statements for the year ended June 30, 2017.