

SOUTH COUNTY OUTREACH
Financial Statements
(with Independent Auditors' Report Thereon)
December 31, 2013

SOUTH COUNTY OUTREACH
Financial Statements

December 31, 2013

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An Independent CPA Firm

Board of Directors
South County Outreach
Irvine, California

INDEPENDENT AUDITORS' REPORT

Report on Financial Statements

We have audited the accompanying financial statements of South County Outreach (a nonprofit organization), which comprise the statement of financial position as of December 31, 2013, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of South County Outreach as of December 31, 2013, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Board of Directors
South County Outreach
Irvine, California
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Other Reporting Required By Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 13, 2014 on our consideration of South County Outreach's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering South County Outreach's internal control over financial reporting and compliance.

David L. Gruber and Associates, Inc.

David L. Gruber and Associates, Inc.
Huntington Beach, CA
March 13, 2014

SOUTH COUNTY OUTREACH
Statement of Financial Position
December 31, 2013

Assets

| | |
|---|---------------------|
| Cash and cash equivalents | \$ 555,579 |
| Certificate of deposit | 166,637 |
| Grants receivable (Note 2) | 51,275 |
| Inventory | 31,495 |
| Deposits | 21,772 |
| Other assets | 2,500 |
| Property, furniture and equipment, net (Note 3) | <u>1,100,420</u> |
| Total assets | <u>\$ 1,929,678</u> |

Liabilities and Net Assets

| | |
|--------------------------------------|----------------|
| Accounts payable | \$ 9,696 |
| Accrued liabilities | 11,449 |
| Accrued vacation | 12,649 |
| Notes payable - current (Note 4) | 17,116 |
| Security deposits and other deposits | 21,964 |
| Notes payable - long-term (Note 4) | <u>441,400</u> |
| Total liabilities | <u>514,274</u> |

Net assets:

| | |
|---------------------------------|------------------|
| Temporarily restricted (Note 6) | 76,436 |
| Unrestricted | <u>1,338,968</u> |
| Total net assets | <u>1,415,404</u> |

| | |
|----------------------------------|---------------------|
| Total liabilities and net assets | <u>\$ 1,929,678</u> |
|----------------------------------|---------------------|

See accompanying notes to financial statements.

SOUTH COUNTY OUTREACH
Statement of Activities
Year Ended December 31, 2013

| | |
|--|---------------------|
| Unrestricted revenue and support: | |
| Government grants (Note 2) | \$ 323,857 |
| Thrift store sales | 157,606 |
| Contributions-foundations | 213,933 |
| Contributions-corporate | 81,068 |
| Contributions-individuals and others | 321,712 |
| Special events: | |
| Empty Bowls (net of \$8,801 direct expenses) | 29,128 |
| Stars & Stripes (net of \$60,454 direct expenses) | 19,302 |
| Transitional housing rent | 68,881 |
| Donated supplies-food | 1,369,924 |
| Donated supplies-other | 6,160 |
| Miscellaneous | 12,785 |
| Interest income | <u>4,138</u> |
| Subtotal | <u>2,608,494</u> |
| Net assets released from restrictions (Note 6) | <u>116,215</u> |
| Total unrestricted support and revenue | <u>2,724,709</u> |
| Expenses: | |
| Program services | <u>2,508,895</u> |
| Supporting services: | |
| General and administrative | 152,267 |
| Fundraising | <u>28,304</u> |
| Subtotal supporting services | <u>180,571</u> |
| Total expenses | <u>2,689,466</u> |
| Increase (decrease) in unrestricted net assets | 35,243 |
| <u>TEMPORARILY RESTRICTED NET ASSETS</u> | |
| Support and revenue: | |
| Contributions - foundations (Note 6) | <u>190,012</u> |
| Total temporarily restricted support and revenues | 190,012 |
| Net assets released from restriction (Note 6) | <u>(116,215)</u> |
| Increase (decrease) in temporarily restricted net assets | <u>73,797</u> |
| Increase (decrease) in net assets | 109,040 |
| Net assets beginning of year | <u>1,306,364</u> |
| Net assets at end of year | <u>\$ 1,415,404</u> |

See accompanying notes to financial statements.

SOUTH COUNTY OUTREACH
Statement of Functional Expenses
Year Ended December 31, 2013

| | Program | Supporting Services | | | Total |
|--|---------------------|----------------------------|---------------|----------------|------------------|
| | | General and Administrative | Fundraising | Subtotal | |
| Salaries and related expenses: | | | | | |
| Salaries and related expenses | \$ 397,130 | 66,188 | 9,455 | 75,644 | 472,774 |
| Employee benefits | 21,118 | 3,520 | 503 | 4,022 | 25,140 |
| Payroll taxes | <u>34,009</u> | <u>5,668</u> | <u>810</u> | <u>6,478</u> | <u>40,487</u> |
| | | | | | |
| Total salaries and related expenses | <u>452,257</u> | <u>75,376</u> | <u>10,768</u> | <u>86,144</u> | <u>538,401</u> |
| | | | | | |
| Other expenses: | | | | | |
| Professional services | 42,920 | 4,663 | - | 4,663 | 47,583 |
| Rental and utility assistance | 74,620 | - | - | - | 74,620 |
| Training and counseling | 91,653 | - | - | - | 91,653 |
| Transitional housing program expenses | 97,043 | - | - | - | 97,043 |
| Donated supplies- food | 1,369,924 | - | - | - | 1,369,924 |
| Donated supplies- other | 6,160 | - | - | - | 6,160 |
| Food purchase | 29,730 | - | - | - | 29,730 |
| Rent -facilities | 123,836 | 13,760 | - | 13,760 | 137,595 |
| Interest | 23,078 | - | - | - | 23,078 |
| Utilities and telephone | 25,448 | 2,828 | - | 2,828 | 28,275 |
| Office supplies | 39,378 | 21,204 | - | 21,204 | 60,582 |
| Accounting and audit | 7,162 | 3,856 | - | 3,856 | 11,018 |
| Repairs and maintenance | 1,374 | 343 | - | 343 | 1,717 |
| License fees, bank fees and other fees | | 9,576 | - | 9,576 | 9,576 |
| Transportation and travel | 25,894 | 6,474 | - | 6,474 | 32,368 |
| Miscellaneous | - | 2,402 | - | 2,402 | 2,402 |
| Insurance | 9,428 | 2,357 | - | 2,357 | 11,785 |
| Staff development and meetings | 8,090 | 1,428 | - | 1,428 | 9,518 |
| Public relations and marketing | <u>-</u> | <u>-</u> | <u>17,536</u> | <u>17,536</u> | <u>17,536</u> |
| | | | | | |
| Total other expenses | <u>1,975,737</u> | <u>68,890</u> | <u>17,536</u> | <u>86,426</u> | <u>2,062,163</u> |
| | | | | | |
| Total expenses before depreciation | <u>2,427,994</u> | <u>144,266</u> | <u>28,304</u> | <u>172,570</u> | <u>2,600,564</u> |
| | | | | | |
| Depreciation (Note 3) | <u>80,901</u> | <u>8,001</u> | <u>-</u> | <u>8,001</u> | <u>88,902</u> |
| | | | | | |
| Total expenses | <u>\$ 2,508,895</u> | <u>152,267</u> | <u>28,304</u> | <u>180,571</u> | <u>2,689,466</u> |

See accompanying notes to financial statements.

SOUTH COUNTY OUTREACH
Statement of Cash Flows
Year Ended December 31, 2013

| | |
|---|-------------------|
| Cash flows from operating activities: | |
| Change in net assets | \$ 109,040 |
| Adjustments to reconcile change in net assets to net cash provided by (used for) operating activities: | |
| Depreciation | 88,902 |
| Donated inventory | (2,343) |
| Decrease (increase) in grants receivable | (15,689) |
| Decrease (increase) in deposits receivable | (10,336) |
| (Decrease) increase in account payable | (184) |
| (Decrease) increase in accrued liabilities | 2,117 |
| (Decrease) increase in accrued vacation | (990) |
| (Decrease) increase in deposits payable | <u>8,879</u> |
| Net cash provided by (used for) operating activities | <u>179,396</u> |
| Cash flows from investing activities: | |
| Interest earned and paid to certificate of deposit | <u>(3,659)</u> |
| Net cash provided by (used for) investing activities | <u>(3,659)</u> |
| Cash flows from financing activities: | |
| Principal payments on notes payable | (18,047) |
| Net cash provided by (used for) financing activities | <u>(18,047)</u> |
| Increase (decrease) in cash and cash equivalents | 157,690 |
| Cash and cash equivalents at beginning of year | <u>397,889</u> |
| Cash and cash equivalents at end of year | <u>\$ 555,579</u> |
| | |
| <u>Supplemental disclosure of cash flow information:</u> | |
| Cash paid for interest expense | <u>\$ 23,078</u> |

See accompanying notes to financial statements.

SOUTH COUNTY OUTREACH

Notes to the Financial Statements

December 31, 2012

(1) Summary of Significant Accounting Policies

The significant accounting policies of the South County Outreach (SCO) are presented to assist in the understanding of SCO's financial statements. The financial statements and notes are representations of SCO's management, who is responsible for the integrity and objectivity of the financial statements. These accounting policies conform to accounting principles generally accepted in the United States of America and have been consistently applied in the preparation of the financial statements.

(a) Organization and Sources of Revenues

South County Outreach (formerly Saddleback Community Outreach) was incorporated in 1988 as a California nonprofit public benefit corporation. SCO provides comprehensive homeless prevention and transitional housing services to south Orange County families and individuals. SCO offers the following services: food pantry; rent and utility assistance; computer training; and a transitional housing program operated by a 17 unit condominium complex owned by SCO. In addition, SCO operates a thrift store which sells a variety of new and second hand goods which are donated. The operation is "volunteer driven" and is primarily dependent upon public and private contributions, "in-kind" contributions of goods and services, and fundraising events.

SCO operates certain programs under contracts with various federal and non-federal government agencies which provide reimbursement up to a fixed maximum for the cost of contract services performed. SCO is also awarded specific purpose grants.

(b) Basis of Accounting and Revenue Recognition

SCO uses the accrual basis of accounting. Under this method of accounting, revenues are recognized when earned and expenses are recognized when incurred.

(c) Financial Statement Presentation

In accordance with Financial Accounting Standards Board (FASB) *Accounting Standards Codification (ASC) 958- Not for Profit Entities*, SCO 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.

SOUTH COUNTY OUTREACH
Notes to the Financial Statements

(Continued)

(1) Summary of Significant Accounting Policies. (Continued)

Cash and Cash Equivalents

- (d) For purposes of the statement of cash flows, SCO considers all unrestricted highly liquid investments with a maturity of three months or less to be cash equivalents. SCO maintains cash deposits with its financial institutions that at times exceed amounts covered by the insurance provided by the Federal Deposit Insurance Corporation (FDIC). SCO also actively evaluates the credit worthiness of the institutions with which it invests.

(e) Certificate of Deposit

As of December 31, 2013, the Company owned a certificate of deposit in the amount of \$166,637. This time certificate matures in August 2016, at a rate of interest of 2.19 percent per annum. Because the term of the certificate is greater than three months, it is not included by the Company as a cash equivalent for purposes of the statement of cash flows.

(f) Property, Furniture and Equipment

It is SCO's policy to capitalize long-lived assets over \$500 and a useful life of three years or longer. Lesser amounts are expensed. Property, furniture and equipment are capitalized at cost. Donations of long-lived assets are recorded as contributions at their estimated fair values. Such donations are reported as unrestricted contributions unless the donor has restricted the donated asset to a specific purpose in which case they are recorded as restricted contributions until such restriction expires. Property, furniture and equipment are depreciated on the straight-line method, using estimated useful lives of 27.5 years for the buildings, 5 to 10 years for the furniture and equipment, and 5 years on vehicles.

(g) Impairment of Long-Lived Assets

SCO evaluates long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. If the estimated future cash-flows (undiscounted and without interest charges) from the use of an asset are less than the carrying value, a write-down would be recorded to reduce the related asset to its estimated fair value.

(h) Thrift Store Inventory

Inventory consists of donated goods such as apparel, clothing and similar merchandise. Inventory is valued at fair value on the date of donation.

SOUTH COUNTY OUTREACH
Notes to the Financial Statements

(Continued)

(1) Summary of Significant Accounting Policies. (Continued)

(i) Fair Value of Financial Instruments

SCO follows guidance issued by the ASC 820 *Fair Value Measurements*, which establishes a framework for measuring fair value, clarifies the definition of fair value within that framework, and expands disclosures about the use of fair value measurements. This guidance applies whenever fair value is the applicable measurement. This guidance establishes a fair value hierarchy which prioritizes the inputs to valuation techniques used to measure fair values into Levels 1, 2, and 3.

Level 1 inputs consist of unadjusted quoted prices in active markets for identical instruments and have the highest priority. Level 2 inputs include quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, or inputs other than quoted prices that are directly or indirectly observable. Level 3 inputs are unobservable and are given the lowest priority.

SCO's financial instruments, including cash and cash equivalents, grants receivable, and accounts payable and other accrued expenses are carried at cost, which approximates fair value because of the short-term nature of these instruments. SCO records its inventory at fair value on the date of donation based on values provided by the donors. These inputs are based on observable inputs of similar assets and are considered level 3 for the year ended December 31, 2013.

(j) Restricted and Unrestricted Revenue and Support

In accordance with ASC 958-605, contributions received are categorized as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Unconditional promises to give are recognized as revenues or gains in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

All support that is restricted by the donor 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 statement of activities as net assets released from restrictions.

Grant contract funds received from U.S Department of Housing and Urban Development, the State of California, and various other grantor agencies are reported as exchange transactions and are recognized as the related expenses are incurred.

SOUTH COUNTY OUTREACH
Notes to the Financial Statements

(Continued)

(1) Summary of Significant Accounting Policies. (Continued)

(k) Functional Expense Allocations

Costs of providing SCO's programs and other activities have been presented in the statement of functional expenses. Accordingly, certain costs have been allocated between the program and supporting services benefited.

(l) Accrued Vacation

SCO's policy is to record accumulated vacation when earned. As of December 31, 2013, the accrued vacation liability was \$12,649.

(m) Income Taxes

SCO is a tax-exempt organization under Internal Revenue Code Section 501(c)(3) and California Revenue and Taxation Code Section 23701(d) and files all federal and state information returns required by law. The SCO's Forms 990, *Return of Organization Exempt from Income Tax*, for the years ending in years 2013, 2012, and 2011 are subject to examination by the IRS, generally for three years after they were filed.

(n) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America require management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

(o) Pledges receivable

Contributions are recognized when the donor makes a promise to give to the Chapter that is, in substance, unconditional. Contributions that are restricted by the donor are reported as increases in unrestricted net assets if the restriction expires in the fiscal year in which the contributions are recognized. All other donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified as unrestricted net assets. SCO uses the allowance method to determine uncollectible promises receivable. The allowance was estimated to be 0% and is based on prior years' experience and management's analysis of specified promises made.

SOUTH COUNTY OUTREACH
Notes to the Financial Statements

(Continued)

(1) Summary of Significant Accounting Policies. (Continued)

(p) Donated services and supplies

Significant services and supplies are donated to SCO by various individuals, corporations and other organizations, and are reflected in the accompanying financial statements at their fair values at the date of donation.

Donations of services are only recognized if the services received: (1) create or enhance nonfinancial assets or require specialized skills; (2) are provided by individuals possessing those skills; and (3) would typically need to be purchased if not provided by donation. Other volunteer services that do not meet these criteria are not recognized in the financial statements as there is no objective basis for deriving their value.

In addition, a significant portion of the SCO's functions and programs are conducted by unpaid volunteers. The value of this contributed time is not reflected in the accompanying financial statements since the services do not require specialized skills. During the year ended December 31, 2013, computer lab volunteers donated approximately 3,512 of hours with an estimated value of \$105,360. This value was computed using an estimated hourly rate of \$30, based upon the average hourly earnings of similar employees plus estimated fringe benefits. During the year ended December 31, 2013, labor volunteers donated approximately 47,628 of hours with an estimated value of \$476,280. This value was computed using an estimated hourly rate of \$10, based upon the average hourly earnings of similar employees plus estimated fringe benefits.

Donated supplies consists primarily of food with a fair value of \$1.60 per pound based on management's estimate with the use of a study performed by Feeding America.

(2) Summary of Government Grant Funding

SCO's contract revenues for the year ended December 31, 2013 are summarized as follows:

| | |
|---|-------------------|
| U.S. Dept of Housing & Urban Development-Care | \$ 194,172 |
| Community Development Block Grants* | 75,693 |
| Rescare Workforce Services | 53,992 |
| Total | <u>\$ 323,857</u> |

*- Passed through the cities of Laguna Woods, Rancho Santa Margarita, Laguna Niguel, Mission Viejo, Irvine, Lake Forest, and Irvine.

At December 31, 2013, grant receivable in the amount of \$51,275 consisted of both federal and non-federal receivables and were reported in the statement of financial position.

SOUTH COUNTY OUTREACH
Notes to the Financial Statements

(Continued)

(3) Property, Furniture and Equipment

Property, furniture and equipment consist of the following at December 31, 2013:

| | |
|--------------------------|--------------------|
| Residential buildings * | \$1,946,936 |
| Leasehold improvements | 151,216 |
| Office equipment | 106,719 |
| Vehicles | 28,767 |
| Accumulated depreciation | <u>(1,133,218)</u> |
| | <u>\$1,100,420</u> |

*Residential buildings consist of condominium units of which the land is not owned. As required under the terms of grants, certain of the Organization's residential rental properties with an aggregate cost of \$1,805,579 are to be used for transitional housing for families and individuals meeting specified eligibility requirements. In addition, certain of the rental properties with an aggregate cost of \$1,070,209 serve as collateral for the Organization's notes payable.

Total depreciation expenses for the year ended December 31, 2013 was \$88,902.

(4) Notes payable

Notes payable at December 31, 2013 are comprised of the following:

A note payable to County of Orange, California, collateralized by a deed of trust on real property and an assignment of rents, bearing interest at 2.0% per annum, payable in monthly principal and interest installments of \$1,023, with final payment due May 25, 2029. The total amount outstanding on the note as of December 31, 2013 was \$162,920.

A note payable to a bank, collateralized by a deed of trust on real property, bearing interest at 7.0% per annum, payable in monthly principal and interest installments of \$599, with final payment due June 1, 2017. The total amount outstanding on the note as of December 31, 2013 was \$74,471.

A note payable to a bank collateralized by a deed of trust on real property, bearing interest at 7.0% per annum, payable in monthly installments of \$799, with final payment due June 1, 2017. The total amount outstanding on the note as of December 31, 2013 was \$99,333.

A note payable to a bank collateralized by a deed of trust on real property, bearing interest at 7.05% per annum, payable in monthly installments of \$669, with final payment due May 1, 2017. The total amount outstanding on the note as of December 31, 2013 was \$82,563.

SOUTH COUNTY OUTREACH

Notes to the Financial Statements

(Continued)

(4) Notes Payable (Continued)

A note payable to a bank collateralized by a deed of trust on real property, bearing interest at 6.625% per annum, payable in monthly installments of \$360, with final payment due June 26, 2013. The total amount outstanding on the note as of December 31, 2023 was \$39,229.

Total outstanding notes payable as of December 31, 2013 was \$458,516. Scheduled principal payments on notes payable are as follows:

| <u>Year ending June 30:</u> | | <u>Totals</u> |
|-----------------------------|----|-----------------|
| 2014 | \$ | 17,116 |
| 2015 | | 17,832 |
| 2016 | | 18,541 |
| 2017 | | 244,304 |
| 2018 | | 11,103 |
| Thereafter | | <u>149,620</u> |
| Totals | | <u>458,516</u> |
| Less current portion | | <u>(17,116)</u> |
| Long-term portion | \$ | <u>441,400</u> |

(5) Lease Obligations

Operating leases

SCO rents its administrative office and pantry, and its thrift store under terms classified as operating leases. Monthly payments are approximately \$7,000 and \$3,500 for the facilities, respectively. Terms on the leases expire in January 2014 and June 2014 for the office and pantry, respectively. SCO entered into a new lease for its administrative office and pantry. The new lease payments are approximately \$8,000 per month through January 2019. Rent expense for the two facilities was \$137,595 for the year ended December 31, 2013. SCO also leases various equipment. Monthly payments on the equipment range from approximately \$51 to \$565 per month and expire ranging from May 2016 to July 2016. Rent expense for the equipment was \$12,191 for the year ended December 31, 2013. Minimum rental commitments are as follows:

Year ending June 30:

| | |
|-------------------------------------|------------------|
| 2014 | \$107,784 |
| 2015 | 107,784 |
| 2016 | 101,110 |
| 2017 | 96,696 |
| 2018 | <u>96,696</u> |
| Total future minimum lease payments | <u>\$510,070</u> |

SOUTH COUNTY OUTREACH
Notes to the Financial Statements

(Continued)

(6) Release of Temporarily Restricted Net Assets

During the year ended December 31, 2013, \$116,215 of temporarily restricted net assets, were released to unrestricted net assets as a result of the satisfaction of donor imposed restrictions.

| <u>Restricted for:</u> | Temporarily Restricted Net Assets- Beginning of Year, restated | Temporarily Restricted Revenues | Released From Restriction | Temporarily Restricted Net Assets- End of Year |
|--|---|--|--|---|
| Rent/ utility assistance, food program, and other | <u>\$2,639</u> | <u>190,012</u> | <u>(116,215)</u> | <u>76,436</u> |

(7) Other Commitments and Contingencies

Financial assistance from federal, state, and local governmental entities in the form of grants are subject to special audit. Such audits could result in claims against SCO for disallowed costs or noncompliance with grantor restrictions. No provision has been made for any liabilities that may arise from such audits since the amounts, if any, cannot be determined at this date.

SCO is also subject to legal proceedings, claims, and assessments which arise in the ordinary course of its business. In the opinion of management, the amount of ultimate liability with respect to these actions, should they occur, will not materially affect the SCO's financial statements.

(8) Concentrations and Grant Funding

In recent years, SCO has received significant funding from the Department of Housing and Urban Development, Rescare Workforce Services, and various Cities in Orange County. Due to potential reductions in federal funding to these agencies, future grants to SCO are uncertain. Although management is reviewing alternatives for continuing operations, if grants are reduced, any reduction may impact the future operations of SCO. SCO received numerous grant contracts from these agencies for funding through December 31, 2014. Additionally, it is the intent of SCO to bid for funding from these agencies through December 31, 2015. Actual funding amounts from the various cities are dependent upon amounts allocated by various federal and state awarding agencies. SCO also receives multi-year grant funding from various sources which are recorded in the period received or pledged. However, expenditures related to those grants can occur over several years. As a result, timing differences are created which can have an effect on changes in net assets.

SOUTH COUNTY OUTREACH
Notes to the Financial Statements

(Continued)

(9) Compliance with Laws and Regulations

By accepting subrecipient funds from the various federal grantor agencies, SCO is required to comply with certain laws and regulations provided for under the respective grant agreements. Management believes that it has complied with such laws and regulations.

(10) Subsequent Events

Management has evaluated subsequent events through March 13, 2014, the date the financial statements were available to be issued.



An Independent CPA Firm

Board of Directors
South County Outreach
Irvine, California

**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**

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of South County Outreach (SCO), as of and for the year ended December 31, 2013, and the related notes to the financial statements, which collectively comprise SCO's basic financial statements, and have issued our report thereon dated March 13, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered SCO's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of SCO's internal control. Accordingly, we do not express an opinion on the effectiveness of SCO's internal control.

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

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

Compliance and Other Matters

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

Purpose of this Report

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

David L. Gruber and Associates, Inc.

David L. Gruber and Associates, Inc.
Huntington Beach, California
March 13, 2014