

**AID TO ADOPTION OF SPECIAL KIDS/ARIZONA
AND SUBSIDIARIES**

CONSOLIDATED FINANCIAL STATEMENTS

Year Ended June 30, 2017

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AND SUBSIDIARIES**

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3101 N. Central Ave., Suite 300 ■ Phoenix, AZ 85012
Main: 602.264.6835 ■ Fax: 602.265.7631 ■ www.mhmcpa.com

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of

AID TO ADOPTION OF SPECIAL KIDS/ARIZONA AND SUBSIDIARIES

We have audited the accompanying consolidated financial statements of *Aid to Adoption of Special Kids/Arizona and Subsidiaries*, which comprise the consolidated statement of financial position as of June 30, 2017, and the related consolidated statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of ***Aid to Adoption of Special Kids/Arizona and Subsidiaries*** as of June 30, 2017, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited ***Aid to Adoption of Special Kids/Arizona and Subsidiaries'*** 2016 consolidated financial statements, and our report dated December 9, 2016, expressed an unmodified opinion on those audited consolidated financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2016, is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

A handwritten signature in black ink that reads "Mayer Hoffman McCann P.C." in a cursive, professional style.

November 8, 2017

**AID TO ADOPTION OF SPECIAL KIDS/ARIZONA
AND SUBSIDIARIES**

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

June 30, 2017
(with comparative totals at June 30, 2016)

	<u>ASSETS</u>	
	<u>2017</u>	<u>2016</u>
CASH AND CASH EQUIVALENTS	\$ 3,654,506	\$ 2,898,873
INVESTMENTS	12,958,332	11,793,137
RECEIVABLES, net	1,446,905	1,503,341
PLEDGES RECEIVABLE, net	229,851	371,365
PREPAID EXPENSES AND OTHER ASSETS	60,116	34,244
PROPERTY AND EQUIPMENT, net	2,972,294	3,124,945
ENDOWMENT CASH	<u>15,047</u>	<u>15,042</u>
TOTAL ASSETS	<u>\$ 21,337,051</u>	<u>\$ 19,740,947</u>

<u>LIABILITIES AND NET ASSETS</u>		
NOTE PAYABLE	\$ 84,000	\$ 96,000
ACCOUNTS PAYABLE AND ACCRUED EXPENSES	632,462	562,643
DEFERRED REVENUE	<u>-</u>	<u>8,308</u>
TOTAL LIABILITIES	716,462	666,951
NET ASSETS		
Unrestricted	20,380,738	18,617,631
Temporarily restricted	229,851	446,365
Permanently restricted	<u>10,000</u>	<u>10,000</u>
TOTAL NET ASSETS	<u>20,620,589</u>	<u>19,073,996</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 21,337,051</u>	<u>\$ 19,740,947</u>

**AID TO ADOPTION OF SPECIAL KIDS/ARIZONA
AND SUBSIDIARIES**

CONSOLIDATED STATEMENT OF ACTIVITIES

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>	
				<u>2017</u>	<u>2016</u>
SUPPORT AND REVENUES					
Government contracts	\$ 9,096,978	\$ -	\$ -	\$ 9,096,978	\$ 9,333,881
Contributions	1,345,477	114,500	-	1,459,977	1,037,887
Fundraising event (net of direct donor benefits)	120,358	-	-	120,358	79,759
United Way	116,461	-	-	116,461	120,719
Interest and dividend income	109,597	-	-	109,597	62,415
Realized and unrealized (losses) gains on investments	(19,832)	-	-	(19,832)	12,005
Other	9,600	-	-	9,600	9,600
Total support before net assets released from restrictions	10,778,639	114,500	-	10,893,139	10,656,266
Net assets released from restrictions	331,014	(331,014)	-	-	-
TOTAL SUPPORT AND REVENUES	11,109,653	(216,514)	-	10,893,139	10,656,266
EXPENSES					
Program services:					
Family Support Services	1,791,284	-	-	1,791,284	1,894,007
Specialized Foster Care	1,765,067	-	-	1,765,067	1,963,437
Regular Adoption & Foster Care	4,411,790	-	-	4,411,790	3,544,087
Community Funded Initiatives	314,701	-	-	314,701	502,570
Birth Parent Counseling	33,754	-	-	33,754	25,639
Total program services	8,316,596	-	-	8,316,596	7,929,740
Supporting services:					
Management and General	751,692	-	-	751,692	858,608
Fundraising	278,258	-	-	278,258	221,342
Total supporting services	1,029,950	-	-	1,029,950	1,079,950
TOTAL EXPENSES	9,346,546	-	-	9,346,546	9,009,690
CHANGE IN NET ASSETS	1,763,107	(216,514)	-	1,546,593	1,646,576
NET ASSETS, BEGINNING OF YEAR	18,617,631	446,365	10,000	19,073,996	17,427,420
NET ASSETS, END OF YEAR	\$ 20,380,738	\$ 229,851	\$ 10,000	\$ 20,620,589	\$ 19,073,996

See Notes to Consolidated Financial Statements

**AID TO ADOPTION OF SPECIAL KIDS/ARIZONA
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CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

	Program Services					Supporting Services		Totals		
	Family Support Services	Specialized Foster Care	Regular Adoption & Foster Care	Community Funded Initiatives	Birth Parent Counseling	Total Program Services	Management and General	Fundraising	2017	2016
Payroll:										
Salaries - Full Time	\$ 273,431	\$ 294,576	\$ 2,952,693	\$ 177,155	\$ 27,031	\$ 3,724,886	\$ 404,566	\$ 168,974	\$ 4,298,426	\$ 3,891,193
Salaries - Part Time	1,267,965	-	53,083	-	-	1,321,048	-	-	1,321,048	1,267,509
Payroll taxes	132,445	23,251	246,359	14,130	2,236	418,421	29,043	14,630	462,094	417,989
Benefits	22,444	9,536	135,690	7,501	-	175,171	17,516	4,605	197,292	149,596
Retirement	10,922	8,464	46,869	4,962	1,081	72,298	8,587	5,477	86,362	176,227
Total payroll	1,707,207	335,827	3,434,694	203,748	30,348	5,711,824	459,712	193,686	6,365,222	5,902,514
Family related services	-	1,349,596	351,152	64,599	-	1,765,347	-	6,360	1,771,707	1,901,040
Professional services	-	15,771	16,740	102	-	32,613	111,059	-	143,672	168,933
Occupancy	10,436	10,326	129,902	12,100	979	163,743	13,243	6,045	183,031	172,743
Advertising	-	-	11,807	-	-	11,807	-	5,108	16,915	38,518
Bad debts	29,458	18,307	42,172	-	-	89,937	-	4,500	94,437	154,970
Travel	5,113	8,359	121,998	8,825	374	144,669	2,263	3,018	149,950	158,282
Communications	4,165	5,751	59,324	4,807	358	74,405	3,515	1,765	79,685	63,669
Printing and copying	5,693	3,588	8,711	348	22	18,362	356	4,994	23,712	7,988
Office and general supplies	3,675	2,523	40,958	3,605	213	50,974	31,919	8,917	91,810	93,706
Postage and shipping	1,030	198	3,187	29	18	4,462	2,135	1,703	8,300	13,938
Insurance	-	-	-	-	-	-	97,562	-	97,562	85,544
Employee Recruitment, Training and Retention	12,509	3,151	38,906	3,541	328	58,435	1,198	5,909	65,542	37,279
Depreciation	11,998	11,670	152,168	12,997	1,114	189,947	15,106	6,988	212,041	186,448
Other	-	-	71	-	-	71	13,624	29,265	42,960	24,118
TOTAL FUNCTIONAL EXPENSES	\$ 1,791,284	\$ 1,765,067	\$ 4,411,790	\$ 314,701	\$ 33,754	\$ 8,316,596	\$ 751,692	\$ 278,258	\$ 9,346,546	\$ 9,009,690

See Notes to Consolidated Financial Statements

**AID TO ADOPTION OF SPECIAL KIDS/ARIZONA
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CONSOLIDATED STATEMENT OF CASH FLOWS

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

	2017	2016
RECONCILIATION OF CHANGE IN NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Change in net assets	\$ 1,546,593	\$ 1,646,576
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Provision for bad debts	94,437	154,970
Gain on forgiveness of note payable	(12,000)	(12,000)
Realized and unrealized losses (gains) on investments	19,832	(12,005)
Depreciation	212,041	186,448
Changes in discounts on pledges receivable	(11,000)	310
Changes in operating assets and liabilities:		
Decrease (increase) in:		
Receivables	(38,001)	(554,980)
Pledges receivable	152,514	(25,879)
Prepaid expenses and other assets	(25,872)	(23,637)
Increase (decrease) in:		
Accounts payable and accrued expenses	69,819	21,450
Deferred revenue	(8,308)	8,308
Net cash provided by operating activities	2,000,055	1,389,561
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(59,390)	(31,968)
Purchases of investments	(7,226,708)	(7,048,898)
Proceeds from maturities of investments	6,041,681	5,987,000
Change in endowment cash	(5)	(4)
Net cash used in investing activities	(1,244,422)	(1,093,870)
NET CHANGE IN CASH AND CASH EQUIVALENTS	755,633	295,691
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	2,898,873	2,603,182
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 3,654,506	\$ 2,898,873

SUPPLEMENTAL DISCLOSURE OF NONCASH FINANCING ACTIVITIES

The Organization received \$12,000 of forgiveness of debt for the years ended June 30, 2017 and 2016.

The Organization received \$153,171 of repairs and maintenance service paid for by insurance proceeds for the year ended June 30, 2016.

AID TO ADOPTION OF SPECIAL KIDS/ARIZONA AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

(1) Organization operations and summary of significant accounting policies

Organization operations – *Aid to Adoption of Special Kids/Arizona and Subsidiaries* (the "Organization") is a private, non-profit adoption and child placement agency licensed by the Arizona Department of Child Safety, dedicated to the placement of special needs children into permanent, loving homes in the state of Arizona. The Organization's goal of building and preserving families is served through parent training, adoption placement, specialized medical foster care, post-placement support, and community education services.

The significant accounting policies followed by the Organization are summarized below:

Principles of consolidation – The accompanying consolidated financial statements include the accounts of *Aid to Adoption of Special Kids/Arizona* ("AASK"), *AASK Phoenix Property, LLC* ("AASK-Phoenix"), *AASK Peoria Property, LLC* ("AASK-Peoria") and *AASK Chandler Property, LLC* ("AASK-Chandler"). Collectively, the entities are referred to hereinafter as the Organization. In December, 1988, AASK was incorporated in the state of Arizona. During the year ended June 30, 2014, AASK-Phoenix, AASK-Peoria, and AASK-Chandler were established for the purposes of owning and operating real property solely for the Organization's use. Each subsidiary was organized as a single-member limited liability company with AASK as the sole member. All significant intercompany transactions and accounts have been eliminated in consolidation.

Basis of presentation – The accompanying consolidated financial statements are presented in accordance with FASB ASC 958-205, *Not-for-Profit Organizations - Presentation of Financial Statements*. Under FASB ASC 958-205, 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.

Prior year summarized information – The consolidated financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). Accordingly, such information should be read in conjunction with the Organization's consolidated financial statements for the year ended June 30, 2016 from which the summarized information was derived.

Management's use of estimates – The preparation of consolidated financial statements in conformity with U.S. GAAP 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 revenues and expenses during the reporting period. Actual results could differ from these estimates.

Cash and cash equivalents – Cash includes cash and, at times, cash equivalents that consist of highly liquid financial instruments purchased with original maturities of three months or less. Cash deposits in each institution are insured in limited amounts by the Federal Deposit Insurance Corporation ("FDIC").

AID TO ADOPTION OF SPECIAL KIDS/ARIZONA AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

(1) Organization operations and summary of significant accounting policies (continued)

Investments – The Organization accounts for its investments in accordance with FASB ASC 958-320, *Not-for-Profit Entities – Investments - Debt and Equity Securities* and FASB ASC 958-325, *Not-for-Profit Entities – Investments - Other*. Under FASB ASC 958-320, the Organization is required to report investments in equity securities that have readily determinable fair values and all investments in debt securities, including negotiable certificates of deposit, at fair value. The fair value of securities with readily determinable fair values is based upon quoted market prices or publicly available net asset values. Negotiable certificates of deposit are valued using proprietary valuation models incorporating live data from active market makers and inter-dealer brokers as reported on electronic communication networks. The valuation models incorporate benchmark yields, reported trades, broker/dealer quotes, bids, offers, and other data. Under FASB ASC 958-325, certificates of deposit investments that are not debt securities are stated at amortized cost, which approximates fair value. Investments in money market funds are measured at fair value based on quoted market prices.

Fair value measurements – FASB ASC 820, *Fair Value Measurements*, establishes a common definition for fair value to be applied to accounting principles generally accepted in the United States of America requiring use of fair value, establishes a framework for measuring fair value, and expands disclosures about such fair value measurements. The Organization adopted FASB ASC 820 for assets and liabilities subject to fair value measurement on a recurring and non-recurring basis. FASB ASC 820 also establishes a hierarchy for ranking the quality and reliability of the information used to determine fair values by requiring that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

Level 1: Unadjusted quoted market prices in active markets for identical assets or liabilities.

Level 2: Unadjusted quoted prices in active markets for similar assets or liabilities, unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable for the asset or liability.

Level 3: Unobservable inputs for the asset or liability.

Receivables – Receivables consist of program service fees and contracts receivable. The Organization is exposed to certain credit risks, and manages its risk by regularly reviewing its accounts and following collection procedures. The Organization provides an appropriate allowance for doubtful accounts. Receivables are stated at the amount management expects to collect. Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to receivables.

AID TO ADOPTION OF SPECIAL KIDS/ARIZONA AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

(1) Organization operations and summary of significant accounting policies (continued)

Property and equipment – Purchased property and equipment is recorded at cost and donated property and equipment is recorded at its fair value at the date of contribution to the Organization. Maintenance and repairs are charged to operations when incurred. Betterments and renewals in excess of \$1,000 are capitalized. When property and equipment are sold or otherwise disposed of, the asset account and related accumulated depreciation account are relieved and any gain or loss is included in operations. Depreciation is computed on a straight-line basis over the following estimated range of useful lives:

	<u>Estimated Useful Lives</u>
Building	30 years
Improvements	5 - 15 years
Furniture and equipment	3 - 15 years

Impairment of long-lived assets – The Organization accounts for long-lived assets in accordance with the provisions of FASB ASC 360, *Property, Plant and Equipment*. FASB ASC 360 requires that long-lived assets be reviewed 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 to be 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. The Organization has reviewed its long-lived assets and has found no impairment has occurred during the years ended June 30, 2017 and 2016.

Revenue recognition – The major source of support and revenue for the Organization is received under government contracts from the Arizona Department of Child Safety (“DCS”). Revenues are recognized as actual expenditures are incurred and services are provided in accordance with the contracts and grants and their approved budgets. The contracts expire annually (June 30 or September 30 generally), and management expects the contracts to be renewed through the respective renewal process. Revenue recognized under DCS contracts represented approximately 58% and 56% of total government contracts revenue for the years ended June 30, 2017 and 2016, respectively. Additionally, one other contract represented 28% and 25% of total government contracts for the years ended June 30, 2017 and 2016, respectively. If these contracts are not renewed or are otherwise lost, the Organization’s operations would be significantly impacted.

Program revenues from respite and adoption fees are recognized when the related services are performed. Revenue received in advance is recorded in deferred revenue in the accompanying consolidated statement of financial position.

Contributions – The Organization accounts for contributions in accordance with FASB ASC 958-605, *Not-for-Profit Organizations - Revenue Recognition*. Contributions received 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 restrictions. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily or permanently restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions. Restricted support, where restrictions are met in the same period as the contribution is made, is shown as unrestricted support.

AID TO ADOPTION OF SPECIAL KIDS/ARIZONA AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

(1) Organization operations and summary of significant accounting policies (continued)

Promises to give – Unconditional promises to give (pledges) that are 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 initially recorded at the fair value of their estimated future cash flows as of the date of the promise to give through the use of a present value discount technique. In periods subsequent to initial recognition, unconditional promises to give are reported at the amount management expects to collect and are discounted over the collection period using the same discount rate as determined at the time of initial recognition. The discount rate determined at the initial recognition of the unconditional promise to give is based upon management's assessment of many factors, including when the receivable is expected to be collected, the creditworthiness of the other parties, the Organization's past collection experience and its policies concerning the enforcement of promises to give, expectations about possible variations in the amount or timing, or both, of the cash flows, and other factors concerning the receivable's collectability. Amortization of the discounts is included in support from contributions. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

Special events revenue – The Organization introduced a special event in fiscal year 2014. A portion of the gross proceeds paid by the participant represents payment for the direct cost of the benefits received by the participant at the event. Unless a verifiable, objective means exists to demonstrate otherwise, the fair value of meals and entertainment provided at special events is measured at the actual cost to the Organization. The revenue is presented net of the direct costs of the special event which ultimately benefit the donor rather than the Organization in the accompanying consolidated statement of activities. Direct donor benefits for special events totaled \$1,106 and \$3,575 for 2017 and 2016, respectively.

Donated materials and services – Donated materials and services are reflected in the accompanying consolidated financial statements at their estimated fair value at the date of the donation. Donated services are recognized as contributions in accordance with FASB ASC 958-605 if the services (a) create or enhance nonfinancial assets or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased.

Functional expenses – The costs of providing various programs and other activities have been summarized on a functional basis in the accompanying consolidated statement of functional expenses. Certain costs have been allocated among the programs and support services benefited based on management's estimate of employee hours devoted to each function.

Advertising – Advertising costs are charged to operations when incurred. Advertising expense charged to operations was \$16,915 and \$38,518 for the years ended June 30, 2017 and 2016, respectively.

Income tax status – AASK qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code (the "Code") and, accordingly, there is no provision for income taxes. In addition, AASK qualifies for the charitable contribution deduction under Section 170 of the Code and has been classified as an organization that is not a private foundation. AASK-Phoenix, AASK-Chandler, and AASK-Peoria are disregarded entities for tax purposes. Income determined to be unrelated business taxable income ("UBTI") would be taxable.

The Organization evaluates its uncertain tax positions, if any, on a continual basis through review of their policies and procedures, review of their regular tax filings, and discussions with outside experts.

AASK's Federal Return of Organizations Exempt from Income Tax (Form 990) for fiscal year 2014, 2015 and 2016 are subject to examination by the IRS, generally for the three years after they were filed. As of the date of this report, the fiscal year 2017 Form 990 has not been filed.

AID TO ADOPTION OF SPECIAL KIDS/ARIZONA AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

(1) Organization operations and summary of significant accounting policies (continued)

Recent accounting pronouncements – In May 2014, the FASB issued Accounting Standards Update (“ASU”) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* that will supersede most current revenue recognition guidance, including industry-specific guidance. The core principle of the new guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include the capitalization and amortization of certain contract costs, ensuring the time value of money is considered in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. Additionally, the guidance requires disclosures related to the nature, amount, timing, and uncertainty of revenue that is recognized.

In August 2015, the FASB issued FASB Accounting Standards Update (“ASU”) No. 2015-14, *Revenue from Contracts with Customers (Topic 606)*, which changed the effective date of the provisions of FASB ASU No. 2014-09. As a result, the new effective dates for public business entities, certain not-for-profit entities, and certain employee benefit plans to apply the guidance in FASB ASU No. 2014-09 is for annual reporting periods beginning after December 15, 2017. All other entities should apply the guidance in FASB ASU No. 2014-09 to annual reporting periods beginning after December 15, 2018. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2016. Transition to the new guidance may be done using either a full or modified retrospective method. The Organization is currently evaluating the full effect that the adoption of this standard will have on the consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02 – *Leases (Topic 842)*. ASU 2016-02 requires that a lease liability and related right-of-use-asset representing the lessee’s right to use or control the asset be recorded on the balance sheet upon the commencement of all leases except for short-term leases. Leases will be classified as either finance leases or operating leases, which are substantially similar to the classification criteria for distinguishing between capital leases and operating in existing lease accounting guidance. The ASU is effective for fiscal years beginning after December 15, 2019. Early adoption is permitted. The Organization is currently evaluating the effect that the adoption of this standard will have on the consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958), Presentation of Financial Statements of Not-for-Profit Entities*. ASU 2016-14 improves the current net asset classification requirements and the information presented in financial statements and notes about a not-for-profit entity’s liquidity, financial performance, and cash flows. ASU 2016-14 is effective for annual financial statements issued for fiscal years beginning after December 15, 2017. Early application is permitted. The amendments of this ASU are to be applied on a retrospective basis in the year that the ASU is first applied. The Organization is currently evaluating the full effect that the adoption of this standard will have on the consolidated financial statements.

In August 2014, the FASB issued ASU 2014-15, *Presentation of Financial Statements—Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern*. The amendments in ASU 2014-15 are intended to define management’s responsibility to evaluate whether there is substantial doubt about an organization’s ability to continue as a going concern and to provide related footnote disclosures. FASB ASU 2014-15 is effective for annual periods ending after December 15, 2016, and interim periods within annual periods beginning after December 15, 2016. The Organization adopted ASU 2014-15 in 2017 with no significant impact to the consolidated financial statements.

AID TO ADOPTION OF SPECIAL KIDS/ARIZONA AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended June 30, 2017
(with comparative totals for the year ended June 30, 2016)

(1) Organization operations and summary of significant accounting policies (continued)

Subsequent events – The Organization has evaluated subsequent events through November 8, 2017 which is the date the consolidated financial statements were available to be issued.

(2) Investments

At June 30, 2017 and 2016, investments consisted of the following:

	2017	2016
Cash and cash equivalents	\$ 250,437	\$ 283,991
Negotiable certificates of deposit (fair value)	12,414,351	11,146,686
Money market funds	293,544	362,460
Total investments	\$ 12,958,332	\$ 11,793,137

Investments are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in risks in the near term would materially affect account balances and the amounts reported in the accompanying consolidated financial statements. At June 30, 2017 and 2016, the negotiable certificates of deposit are in individual amounts such that they are covered by FDIC insurance.

(3) Receivables

	2017	2016
State contracts	\$ 1,692,532	\$ 1,702,947
Adoption fees	21,897	31,277
Total receivables	1,714,429	1,734,224
Allowance for doubtful accounts	(267,524)	(230,883)
Net receivables	\$ 1,446,905	\$ 1,503,341

Three state contracts comprise approximately 78% of gross state contract receivable as of June 30, 2017, and three state contracts comprise approximately 83% of the gross state contracts receivable balance as of June 30, 2016.

Claims submitted under state contracts are recorded in support and revenues from government contracts in the accompanying statement of activities at the date services are performed although they are subject to a claims adjudication process by the Regional Behavioral Health Authority (RBHA). Claims related to state contracts which had not been fully adjudicated by the RHBA were \$76,715 and \$157,208 as of June 30, 2017 and 2016, respectively. Management believes these claims will be favorably adjudicated

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(4) Pledges receivable

Pledges receivable consist of the following promises to give:

	2017	2016
Receivable in less than one year	\$ 235,511	\$ 288,025
Receivable in two to five years	-	100,000
Total pledges receivable	235,511	388,025
Discounts to present value	(5,660)	(16,660)
Net pledges receivable	\$ 229,851	\$ 371,365

The estimated cash flow for pledges receivable are discounted over the collection period using a discount rate of 6.00%.

Management provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its 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 credit to pledges receivable. All receivables are considered by management to be collectible in full and, accordingly, an allowance for uncollectible pledges receivable had not been provided as of June 30, 2017 or 2016. Three donors comprised 91% and four donors comprised 94% of the gross pledges receivable balance at June 30, 2017 and 2016, respectively.

(5) Property and equipment

Property and equipment consists of:

	2017	2016
Cost and donated value:		
Building	\$ 3,531,000	\$ 3,531,000
Building improvements	701,272	664,313
Furniture and equipment	515,099	492,668
Total cost and donated value	4,747,371	4,687,981
Accumulated depreciation	(1,775,077)	(1,563,036)
Net property and equipment	\$ 2,972,294	\$ 3,124,945

Depreciation expense charged to operations was \$212,041 and \$186,448 for the years ended June 30, 2017 and 2016, respectively.

During the year ended June 30, 2003, the City of Phoenix provided approximately \$180,000 to assist in the acquisition of certain property (a building). This property is available for the Organization's use in its continuing programs. Under the terms of the agreement with the City of Phoenix, the property is to be used for the contracted services for 20 years from the date of issuance of the Certificate of Completion, which occurred on October 1, 2003. Since inception of the forgivable loan, the \$180,000 obligation (see Note 6) has been reduced by approximately \$96,000 and \$84,000 as of June 30, 2017 and 2016, respectively. The property is recorded at cost of approximately \$581,000 with accumulated depreciation of approximately \$266,000 and \$247,000 at June 30, 2017 and 2016, respectively.

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(6) Note payable

The Organization entered into a Construction Loan Contract (“Loan”), funded by the Community Development Block Grant (“CDBG”) Program on March 3, 2003, with the City of Phoenix. The Certificate of Completion was received from the City of Phoenix on October 1, 2003. The assistance was not to exceed \$180,000, and was used by the Organization for the acquisition of property. The CDBG Loan is secured by a 20-year lien on the real property. So long as the Organization complies with the grant restrictions, the Loan is forgivable in annual installments of \$12,000 beginning in year 6 through year 20 based on the effective date of the Loan, at a rate of 6.67% per year. If the Organization fails to comply with the grant restrictions, the Organization will be required to repay the current balance of the note on demand.

The outstanding balance will be forgiven in future periods as follows:

Years Ending June 30:

2018	\$	12,000
2019		12,000
2020		12,000
2021		12,000
2022		12,000
Subsequent to 2022		24,000
Total	<u>\$</u>	<u>84,000</u>

(7) Temporarily restricted net assets

Temporarily restricted net assets were restricted for the following purposes:

	<u>2017</u>	<u>2016</u>
Time Restricted	\$ 229,851	\$ 371,365
Purpose Restricted	-	75,000
Total temporarily restricted net assets	<u>\$ 229,851</u>	<u>\$ 446,365</u>

During the years ended June 30, 2017 and 2016, the Organization released \$331,014 and \$273,831, respectively, of temporarily restricted net assets based on the cash received in satisfaction of pledges receivable and by incurring expenses satisfying the restricted purposes.

(8) Permanently restricted net assets

During 2000, the Organization received \$10,000 to establish an endowed charitable fund. The interest and dividend earnings are to be used to support services for families of adopted children with special needs. Permanently restricted net assets were \$10,000 at June 30, 2017 and 2016.

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(9) Pension plan

The Organization sponsors a 401(k) plan covering eligible employees. The Organization currently matches 100% of the participants' contributions for the first 4% of the participants' compensation. Contributions made by the Organization were approximately \$86,400, and \$176,200 for the years ended June 30, 2017 and 2016, respectively. The contributions for the year ended June 30, 2016 include the \$105,000 corrective contribution discussed below.

During the year ended June 30, 2016, management of the Organization became aware of an operational issue relating to the plan's eligible participants and has taken appropriate steps to correct this matter in accordance with the guidance available under the IRS' Employee Plans Compliance Resolution System "EPCRS". On August 25, 2016, the Organization submitted a Voluntary Correction Plan application (the "Application") for the Plan under EPCRS, seeking from the IRS a compliance statement with respect to the operational failures identified by the Organization in the Application. The Organization funded the anticipated correction amount of approximately \$105,000 in August 2016 to resolve the specific operational failures detailed in the compliance statement and to satisfy the requirements of the IRC. The Organization received a signed compliance statement from the IRS dated February 3, 2017 stating that the correction methods detailed in the application are acceptable.

(10) Leases

The Organization leases office equipment under operating lease agreements expiring in September 2019.

In July 2012, the Organization entered into a noncancelable operating lease expiring in July 2017 for office equipment. In September 2014, the Organization entered into a noncancelable operating lease expiring in September 2019 for office equipment. Minimum future rental payments under noncancelable operating leases, including the leases entered into in July 2012 and September, 2014, with remaining terms in excess of one year are as follows:

Years Ending June 30:

2018	\$	2,830
2019		2,139
2020		535
Total	\$	<u>5,504</u>

Total rental expense under operating leases with a term in excess of one month was \$14,552 in 2017 and \$9,706 in 2016. No renewal options are provided for in the leases; however, in the normal course of business, operating leases are generally renewed or replaced by other leases.

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(11) Contributions

Contributions consisted of the following:

	2017	2016
Grants and foundations	\$ 326,643	\$ 573,722
Individual and civic donors	1,128,334	454,328
Corporate donors	5,000	9,837
Total contributions	\$ 1,459,977	\$ 1,037,887

One donor comprised 10% and another donor comprised 14% of contributions for the years ended June 30, 2017 and 2016, respectively.

(12) Fair value measurements

The following table summarizes the valuation of the Organization's assets and liabilities by the above FASB ASC 820 categories as of June 30, 2017:

	Level 1	Level 2	Level 3
Negotiable certificates of deposit	\$ -	\$ 12,414,351	\$ -
Money market funds	293,544	-	-

The following table summarizes the valuation of the Organization's assets and liabilities by the above FASB ASC 820 categories as of June 30, 2016:

	Level 1	Level 2	Level 3
Negotiable certificates of deposit	\$ -	\$ 11,146,686	\$ -
Money market funds	362,460	-	-

The Organization holds no other assets or liabilities required to be measured at fair value on a recurring or nonrecurring basis.

(13) Contingencies

In the ordinary course of conducting its business, the Organization may periodically be a defendant in various legal proceedings. Any estimated loss contingencies in excess of amounts covered by business liability insurance are included in accrued expenses. It is the best judgment of management that neither the financial position nor results of operations of the Organization will be materially affected by the final outcome of any known legal proceedings.