

Neighborhood House Association

**Financial Statements and
Supplementary Information in
Accordance with Office of Management and
Budget Circular A-133 and
Independent Auditor's Reports**

June 30, 2015 and 2014

Neighborhood House Association

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Independent Auditor's Report

To the Audit Committee
Neighborhood House Association

Report on the Financial Statements

We have audited the accompanying financial statements of Neighborhood House Association ("NHA"), which comprise the statements of financial position as of June 30, 2015 and 2014, and the related statements of activities and cash flows for the years then ended, and the related statement of functional expenses for the year ended June 30, 2015 (with summarized financial information for 2014), 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of NHA as of June 30, 2015 and 2014, and the changes in its net assets and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Our audits were conducted for the purpose of forming an opinion on the financial statements of NHA as a whole. The accompanying schedules of expenditures of Federal and state awards, as required by Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the 2015 financial statements. The information has been subjected to the auditing procedures applied in the audit of the 2015 financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the 2015 financial statements or to the 2015 financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the 2015 financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 12, 2015 on our consideration of NHA'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 NHA's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "CohnReznick LLP". The signature is written in a cursive, flowing style.

San Diego, California
November 12, 2015

Neighborhood House Association

Statements of Financial Position June 30, 2015 and 2014

	<u>Assets</u>	
	2015	2014
Current assets		
Cash and cash equivalents (Note 14)	\$ 4,089,173	\$ 5,606,890
Investments (Notes 2 and 17)	224,326	132,882
Grants and contracts receivable (Note 4)	3,099,323	1,618,563
Other accounts receivable	410,560	352,799
Operating advances	-	4,894
Prepaid expenses	98,268	125,080
Total current assets	7,921,650	7,841,108
Property and equipment (Note 5)		
Property and equipment	20,548,987	24,186,198
Less accumulated depreciation and amortization	(16,184,010)	(19,051,775)
Total property and equipment, net	4,364,977	5,134,423
Deposits	86,961	73,600
Total assets	\$ 12,373,588	\$ 13,049,131
	<u>Liabilities and Net Assets</u>	
Current liabilities		
Accrued payroll and related liabilities	\$ 664,136	\$ 1,177,860
Accounts payable and accrued expenses	3,198,314	2,046,915
Accrued annual leave (Note 6)	2,536,763	2,519,303
Current portion of long-term debt (Note 8)	70,757	83,323
Total current liabilities	6,469,970	5,827,401
Deferred rent	158,807	121,435
Long-term debt, net of current portion (Note 8)	2,104,199	2,171,102
Total liabilities	8,732,976	8,119,938
Commitments and contingencies (Notes 9 and 10)		
Net assets		
Unrestricted	3,640,612	4,929,193
Total net assets	3,640,612	4,929,193
Total liabilities and net assets	\$ 12,373,588	\$ 13,049,131

See Notes to Financial Statements.

Neighborhood House Association
Statements of Activities
Years Ended June 30, 2015 and 2014

	2015	2014
Changes in unrestricted net assets		
Revenues and support		
Grants and contracts (Note 11)	\$ 79,322,094	\$ 74,640,563
Food reimbursements	1,376,517	1,281,114
Reimbursements from partners	407,453	473,961
Contributions and donations	901,381	970,629
Service fees	880,047	962,747
Investment return and interest income	2,438	4,924
Other revenues	1,060,092	963,239
Total unrestricted revenues and support	83,950,022	79,297,177
Expenses		
Program services	78,483,525	74,130,641
Supporting services		
Fundraising	140,469	90,365
Management and general	6,614,609	5,778,037
Total expenses	85,238,603	79,999,043
Change in unrestricted net assets from continuing operations before loss on mark-to-market of interest rate swap agreement	(1,288,581)	(701,866)
Loss on mark-to-market of interest rate swap agreement	-	(9,791)
Change in unrestricted net assets	(1,288,581)	(711,657)
Unrestricted net assets		
Beginning of year	4,929,193	5,640,850
End of year	\$ 3,640,612	\$ 4,929,193

See Notes to Financial Statements.

Neighborhood House Association
Statements of Cash Flows
Years Ended June 30, 2015 and 2014

	2015	2014
Operating activities		
Change in net assets	\$ (1,288,581)	\$ (711,657)
Adjustments to reconcile change in net assets to net cash used in operating activities		
Depreciation and amortization	803,869	802,517
Bad debt expense	1,993	1,036
Loss on mark-to-market of interest rate swap agreeme	-	9,791
Deferred rent	37,372	(9,760)
Nonoperating grant and contract revenue	(38,811)	(303,405)
Loss on disposal of equipment	791	-
Unrealized gain on investments	(91,444)	(39,543)
Changes in operating assets and liabilities		
Grants and contracts receivable	(1,480,760)	2,164,000
Other accounts receivable	(59,754)	23,679
Prepaid expenses and deposits	13,451	(58,281)
Operating advances	4,894	32,166
Accounts payable and accrued expenses	1,151,399	(2,259,133)
Accrued payroll and related liabilities	(513,724)	(19,249)
Accrued annual leave	17,460	354,089
Net cash used in operating activities	(1,441,845)	(13,750)
Investing activities		
Proceeds from sale of property and equipment	9,009	-
Purchases of property and equipment	(44,223)	(303,405)
Net cash used in investing activities	(35,214)	(303,405)
Financing activities		
Repayments on debt	(79,469)	(2,330,347)
Repayments on interest rate swap	-	(279,975)
Proceeds from borrowings	-	2,550,000
Receipt of grant and contract revenue for capital projects	38,811	303,405
Net cash (used in) provided by financing activities	(40,658)	243,083
Net decrease in cash and cash equivalents	(1,517,717)	(74,072)
Cash and cash equivalents at beginning of year	5,606,890	5,680,962
Cash and cash equivalents at end of year	\$ 4,089,173	\$ 5,606,890
Supplemental disclosures of cash flow data		
Cash paid for interest	\$ 120,122	\$ 124,486

See Notes to Financial Statements.

Neighborhood House Association
Statement of Functional Expenses
Year Ended June 30, 2015
(With Summarized Financial Information for 2014)

	Program Services			Supporting Services		Total Expenses	
	Childcare Programs	Health and Nutrition Programs	Youth and Other Services	Fundraising	Management and General	2015	2014
Salaries	\$ 21,532,000	\$ 1,824,282	\$ 601,077	\$ -	\$ 3,365,562	\$ 27,322,921	\$ 24,976,029
Fringe benefits	7,206,852	525,887	115,766	-	844,810	8,693,315	8,902,085
Contracted services	1,166,121	334,050	33,612	65,829	1,051,547	2,651,159	2,048,058
Supplies	1,298,739	110,068	11,542	16,002	52,099	1,488,450	1,384,584
Telephone and pagers	308,051	52,821	1,707	-	52,217	414,796	337,464
Postage	11,555	1,674	355	-	14,860	28,444	29,769
Occupancy and storage	2,493,403	327,237	67,164	4,311	39,816	2,931,931	2,774,868
Utilities	468,636	31,681	-	-	53,805	554,122	461,339
Printing, publications and advertising	92,582	1,740	8,323	19,454	14,655	136,754	70,110
Travel and meetings	631,240	77,723	35,873	725	142,689	888,250	947,412
Subcontracts (Note 16)	35,087,959	-	-	-	-	35,087,959	33,487,079
Food expense	1,284,566	101,310	6,080	19,358	10,635	1,421,949	1,536,509
Client assistance	72,641	109,716	38,043	-	4,100	224,500	198,909
Equipment expense	823,058	154,732	17,921	5,742	305,163	1,306,616	830,722
Depreciation and amortization	632,080	-	-	-	171,819	803,899	802,517
Insurance	374,967	26,593	3,064	-	109,404	514,028	545,089
Interest and fees	107,679	5,587	18,544	6,299	53,529	191,638	267,555
Other expenses	185,766	8,256	53,202	2,749	327,899	577,872	398,945
Indirect cost	5,206,304	372,336	8,721	-	(5,587,361)	-	-
Subtotal	78,984,199	4,065,693	1,020,994	140,469	1,027,248	85,238,603	79,999,043
Less: indirect allocation	(5,206,304)	(372,336)	(8,721)	-	5,587,361	-	-
Total expenses by function	\$ 73,777,895	\$ 3,693,357	\$ 1,012,273	\$ 140,469	\$ 6,614,609	\$ 85,238,603	\$ 79,999,043

See Notes to Financial Statements.

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

Note 1 - Organization and significant accounting policies

General

Neighborhood House Association ("NHA") is a California nonprofit corporation organized to provide an extensive network of services to residents of San Diego County.

NHA provides comprehensive health and human services through programs that include child development, family day care, senior nutrition, adult day health care, mental health services, housing and rental assistance and other related services that assist low-income and less fortunate families.

Basis of accounting

The accompanying financial statements are prepared on the accrual basis of accounting in accordance with guidance for financial statements of not-for-profit organizations. Under this guidance, NHA 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. NHA does not have any temporarily or permanently restricted assets.

NHA classifies its net assets and revenues, gains and other support based on the existence or absence of donor-imposed restrictions. Permanently restricted net assets result from contributions whose use is limited by donor stipulations that do not expire. Temporarily restricted net assets result from contributions whose use is limited by donor stipulations that either expire with the passage of time or can be fulfilled and removed by actions of NHA pursuant to those stipulations. Unrestricted net assets represent resources over which the board of directors has discretionary control.

Revenue and support

Revenue from government grants and contracts designated for use in specific activities is recognized in the period when expenditures have been incurred in compliance with the grantor's restrictions. Grants and contracts awarded for the acquisition of long-lived assets are reported as unrestricted operating revenue, in the absence of donor stipulations to the contrary, during the fiscal year in which the assets are acquired. Cash received in excess of revenue recognized is recorded as refundable advances.

Contributions and support are recognized in the period in which NHA receives a promise to give that is, in substance, unconditional. Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the support is recognized. All other donor-restricted support is reported as an increase in temporarily restricted or permanently restricted net assets depending on the nature of the restriction. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets.

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

Accounts receivable

Accounts receivable are stated at unpaid balances, less an allowance for doubtful accounts. NHA provides for losses on accounts receivable by calculating an allowance for uncollectible receivables. The allowance is based on experience, third-party contracts and other circumstances. Receivables are considered impaired if full principal payments are not received in accordance with the contractual terms. It is NHA's policy to charge off uncollectible accounts receivable when management determines the receivable will not be collected. There were no allowances for doubtful accounts recorded as of June 30, 2015 and 2014.

Donated goods and services

Contributions of services are recognized when they are received if the services (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills and would typically need to be purchased if not donated. During 2015 and 2014, the value of contributed services recognized as revenues in the accompanying financial statements was approximately \$561,000 and \$500,000, respectively, which included ophthalmology services and related use of supplies and equipment.

In addition, a substantial number of volunteers donated their time to NHA's program services during each year; however, the value of these donated services is not reflected in the financial statements, as the requirements for recognition have not been met.

Cash and cash equivalents

NHA considers all highly-liquid investments with an original maturity of three months or less when acquired to be cash equivalents.

Investments

NHA invests in marketable securities which are carried at fair value, with realized and unrealized gains and losses included in the statements of activities.

Operating advances

Operating advances represent advances to delegate agencies that relate to the next program year. Advances are made to ensure that operations continue over the summer. They are repaid through a reduction of funding at the end of the contract.

Derivatives

NHA makes limited use of derivative instruments for the purpose of managing interest rate risks. Interest rate swap agreements are used to convert NHA's floating rate long-term debt to a fixed rate. NHA recognizes all derivatives as either assets or liabilities in the statements of financial position and measures those instruments at fair value. Changes in fair value of those instruments are reported in the statements of activities.

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

Property and equipment

Property and equipment with an acquisition cost of \$5,000 or greater is capitalized at cost and depreciated using the straight-line method over its estimated useful life. Leasehold improvements are amortized over the shorter of the useful life or the lease term. Useful lives are as follows:

<u>Description</u>	<u>Useful Life</u>
Buildings	15-30 years
Building improvements	3-10 years
Leasehold improvements	3-15 years
Vehicles	5 years
Furniture and equipment	3-5 years
Computer equipment	3-5 years

Impairment of long-lived assets

NHA reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. In performing a review for impairment, NHA compares the carrying value of the assets with their estimated future undiscounted cash flows. If it is determined that impairment has occurred, the loss would be recognized during that period. The impairment loss is calculated as the difference between the asset carrying values and the present value of estimated net cash flows or comparable market values, giving consideration to recent operating performance and pricing trends. NHA does not believe that any material impairment currently exists related to its long-lived assets.

Deferred rent

Rent expense on operating leases with scheduled or minimum rent increases is expensed on the straight-line basis over the lease terms. Deferred rent represents the excess of rent charged to expense over rent payable under the lease agreements. Deferred rent was approximately \$159,000 and \$121,000 as of June 30, 2015 and 2014, respectively.

Income taxes

NHA is a private, nonprofit agency organized under the laws of the State of California and is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code.

For the years ended June 30, 2015 and 2014, management of NHA believes it has adequate support for all material tax positions and that it is more likely than not, based on the technical merits, that the positions will be sustained upon examination. NHA recognizes interest and penalties, if any, related to tax in interest expense. NHA has analyzed the tax positions taken in its filings with the Internal Revenue Service and the California Franchise Tax Board. Accordingly, NHA has not recorded any reserves, or related accruals for interest and penalties for uncertain income tax positions at June 30, 2015 and 2014.

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

NHA's Federal and state income tax returns prior to fiscal years 2012 and 2011, respectively, are closed. Management continually evaluates expiring statutes of limitations, audits, proposed settlements, changes in tax laws and new authoritative rulings. Management is not aware of any pending reviews or examinations.

Advertising

NHA expenses advertising costs as incurred. Advertising costs for the years ended June 30, 2015 and 2014 were approximately \$61,000 and \$19,000, respectively.

Functional expenses

The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of functional expenses. Accordingly, certain costs have been allocated among the program and supporting services benefited.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and those differences could be significant.

Subsequent events

Subsequent events have been evaluated through November 12, 2015, which is the date the financial statements were available to be issued.

Note 2 - Investments

Investments consist of equity and other securities with an approximate fair value of \$224,000 and \$133,000 at June 30, 2015 and 2014, respectively. Fair values have been determined by reference to the most recent market quotations for the respective investments.

Note 3 - Fair value of financial instruments

NHA's material financial instruments at December 31, 2015 and 2014 for which disclosure of estimated fair value is required by certain accounting standards consisted of cash and cash equivalents, accounts receivable, marketable securities, accounts payable and notes payable to unrelated parties. The fair values of cash and cash equivalents, accounts receivable and accounts payable are equal to their carrying value because of their liquidity and short-term maturity. Marketable securities are stated at fair value based on quoted market values, observable inputs such as quoted prices for similar assets, or unobservable inputs. Management believes that the fair values of notes payable to unrelated parties do not differ materially from their aggregate carrying values in that substantially all the obligations bear variable interest rates that are based on market rates or interest rates that are periodically adjustable to rates that are based on market rates.

Neighborhood House Association

**Notes to Financial Statements
June 30, 2015 and 2014**

Note 4 - Grants and contracts receivable

At June 30, 2015 and 2014, grants and contracts receivable consist of the following:

	2015	2014
Head Start	\$ 2,032,953	\$ 792,664
State programs	14,633	15,155
County programs	651,264	590,707
Food reimbursements	384,313	209,678
Other programs	16,160	10,359
Totals	\$ 3,099,323	\$ 1,618,563

Note 5 - Property and equipment

Property and equipment as of June 30, 2015 consists of the following:

	Cost	Accumulated Depreciation and Amortization	Net Book Value
Land	\$ 1,191,750	\$ -	\$ 1,191,750
Building	4,768,000	2,488,754	2,279,246
Building improvements	634,885	616,974	17,911
Leasehold improvements	8,066,687	7,448,234	618,453
Vehicles	2,005,376	1,949,523	55,853
Furniture and equipment	3,583,057	3,389,914	193,143
Computer equipment	299,232	290,611	8,621
	\$ 20,548,987	\$ 16,184,010	\$ 4,364,977

Property and equipment as of June 30, 2014 consists of the following:

	Cost	Accumulated Depreciation and Amortization	Net Book Value
Land	\$ 1,191,750	\$ -	\$ 1,191,750
Building	4,768,000	2,330,487	2,437,513
Building improvements	694,991	647,683	47,308
Leasehold improvements	8,529,190	7,656,875	872,315
Vehicles	2,837,946	2,744,452	93,494
Furniture and equipment	5,845,298	5,376,392	468,906
Computer equipment	319,023	295,886	23,137
	\$ 24,186,198	\$ 19,051,775	\$ 5,134,423

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

A significant portion of NHA's property and equipment is identified as collateral for certain long-term debt as described in Note 8. There were disposals with a net carrying value of \$9,800 and \$0 during the fiscal years ended June 30, 2015 and 2014, respectively.

Property and equipment acquired by NHA with funds from award programs is considered to be owned by NHA while used in the program for which it was purchased and in other authorized programs. However, funding sources have reversionary interest in the property and in its disposition (i.e., the asset is returned to the Federal government upon disposal or if no longer in-use), as well as the ownership of any proceeds which are subject to pertinent regulations. The net book value of reversionary assets as of June 30, 2015 and 2014 is approximately \$4,365,000 and \$5,108,000, respectively, and is included in property and equipment.

Note 6 - Accrued annual leave

Accrued annual leave is presented as a liability in the statements of financial position. NHA records the accrued leave as it is earned by the employees. Accrued annual leave for the years ended June 30, 2015 and 2014 was approximately \$2,537,000 and \$2,519,000, respectively. These amounts have been funded with deposits with Torrey Pines Bank. These amounts are included in cash and cash equivalents.

Note 7 - Line of credit

NHA has a \$500,000 secured line of credit with Torrey Pines Bank, which matures on January 25, 2016. There was no outstanding balance for the years ended June 30, 2015 and 2014. Borrowings on the line of credit bear interest at a variable rate not to exceed 5.25% (5.0% as of June 30, 2015). The line of credit requires NHA to maintain certain non-financial covenants. NHA was in compliance with all associated covenants as of June 30, 2015.

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

Note 8 - Long-term debt

Long-term debt consists of the following:

	2015	2014
Note payable to Torrey Pines Bank in monthly installments of principal and interest, with a fixed interest rate of 5.25%. The loan commenced on July 25, 2013 and matures on July 28, 2023. The note is secured by a Deed of Trust covering real property located at 5660 Copley Drive, San Diego, California.	\$ 2,174,956	\$ 2,239,968
Note payable to Neighborhood National Bank in monthly installments of principal and interest, with a variable interest rate at the Wall Street Journal Prime Rate plus 1.5%. The interest rate as of June 30, 2014 was 4.75%. The loan commenced on November 2, 2004 and matured on November 2, 2014. The note was secured by a Deed of Trust covering real property located at 802-804 San Pasqual Street, San Diego, California.	-	14,457
	2,174,956	2,254,425
Less current portion	(70,757)	(83,323)
Long-term portion	\$ 2,104,199	\$ 2,171,102

On July 16, 2013, NHA refinanced debt with Torrey Pines Bank for \$2,550,000 and the outstanding loan and interest rate swap agreement with Union Bank were paid in full. The change in the fair value of the interest rate swap agreement for the years ended June 30, 2015 and 2014 totaled \$0 and (\$9,791), respectively, and is included as a non-operating loss in the statements of activities. The new loan commenced on July 25, 2013 and matures on July 28, 2023. The loan is payable in equal monthly installments of principal and interest in the amount of \$15,402. The interest rate is fixed at 5.25%. The note is secured by real property located at 5660 Copley Drive, San Diego, California. The loan requires NHA to maintain certain financial and non-financial covenants. NHA was in compliance with all associated financial and non-financial covenants as of June 30, 2015.

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

Maturities of long-term debt in each of the five years subsequent to June 30, 2015 and thereafter are calculated as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2016	\$ 70,757
2017	76,473
2018	80,585
2019	84,920
2020	89,487
Thereafter	<u>1,772,734</u>
Total	<u>\$ 2,174,956</u>

Interest expense for the years ended June 30, 2015 and 2014 was approximately \$120,000 and \$124,000, respectively.

Note 9 - Operating lease commitments

NHA occupies numerous facilities under operating lease agreements that expire at various dates through June 2029. The future minimum payments under these operating leases for each of the five years subsequent to June 30, 2015 and thereafter are as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2016	\$ 1,833,982
2017	1,371,882
2018	1,122,342
2019	647,308
2020	472,462
Thereafter	<u>1,866,350</u>
Total	<u>\$ 7,314,326</u>

Total operating lease expense for the years ended June 30, 2015 and 2014 was approximately \$1,787,000 and \$1,761,000, respectively.

Note 10 - Contingencies

NHA is involved in various claims arising from the normal course of operating its programs and activities, none of which in the opinion of management or NHA's legal counsel will have a material adverse effect on the financial position or results of operations of NHA.

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

Note 11 - Grants and contracts revenues

In the fiscal years ended June 30, 2015 and 2014, NHA recognized grants and contract revenues from the following sources:

	2015	2014
Head Start program	\$ 71,683,461	\$ 67,598,607
State programs	4,056,968	3,597,452
County programs	3,510,075	3,362,497
Other programs	71,590	82,007
Total grants and contracts	\$ 79,322,094	\$ 74,640,563

Note 12 - 401(k) plan

NHA maintains a defined contribution 401(k) plan covering regular full-time employees. NHA's contribution to the 401(k) plan is based upon a maximum of 6% of the salaries of those employees participating in the plan. Employees covered by the plan have a mandatory contribution of 3% of their respective gross salaries, and can make additional voluntary contributions not to exceed \$18,000 for the tax year ending December 31, 2015. Also, employees age 50 or over by the end of the plan year are allowed to make up to \$6,000 of additional contributions to the 401(k) plan, in excess of the standard limits. The 401(k) plan is administered by a private pension company. Employer contributions charged to operations for the years ended June 30, 2015 and 2014 were approximately \$1,288,000 and \$1,247,000, respectively.

Note 13 - Indirect costs

NHA has negotiated and obtained the following indirect cost rates from the U.S. Department of Health and Human Services, the Federal cognizant agency:

	Provisional 2015	Provisional 2014
All programs	10.4%	10.4%
Delegate agencies	2.0%	2.0%

Indirect costs are charged to the programs in accordance with negotiated rates or specific budgetary limits. The amounts charged for the years ended June 30, 2015 and 2014 were approximately \$5,587,000 and \$5,194,000, respectively.

Note 14 - Concentrations of credit risk

Financial instruments, which potentially subject NHA to concentrations of credit risk, consist primarily of cash and cash equivalents and accounts receivable. NHA maintains its cash and cash equivalents with high-credit quality institutions. At times, such amounts may

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

exceed Federally insured limits. However, to minimize risk, the funds are diversified among various financial institutions.

At June 30, 2015, NHA had cash and cash equivalents in excess of FDIC insured limits at certain financial institutions totaling approximately \$5,081,000.

NHA has approximately eleven government contracts in fiscal year 2014 from Federal, state and local sources. The largest contract was for the Federal Head Start program totaling \$71,683,461. Included in grants and contracts receivable at June 30, 2015 is \$2,032,953 related to this contract.

Note 15 - Union contract

Most non-management personnel (representing 58% of total employees) of NHA are members of the Service Employees International Union, Local #2028. NHA's contract with the union is in effect through June 30, 2017, and continues to be in effect from year to year thereafter, unless either party terminates the contract. NHA's other employees are not represented by a union.

Note 16 - Subcontracts expense

Subcontracts expense for the fiscal years ended June 30, 2015 and 2014 included the following:

	<u>2015</u>	<u>2014</u>
NHA delegate agencies	\$ 28,534,024	\$ 26,846,707
Other	<u>6,553,935</u>	<u>6,640,372</u>
Totals	<u>\$ 35,087,959</u>	<u>\$ 33,487,079</u>

Note 17 - Fair value measurements

NHA values its financial assets and liabilities based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, a fair value hierarchy that prioritizes observable and unobservable inputs is used to measure fair value into three broad levels, which are described below:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for identical assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in inactive markets or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated with observable market data.

Neighborhood House Association

Notes to Financial Statements June 30, 2015 and 2014

Level 3: Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

In determining fair value, NHA utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible as well as considers counterparty credit risk in its assessment of fair value.

Financial assets and liabilities carried at fair value at June 30, 2015 are classified in the table below in one of the three categories described above:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Equity securities	\$ 214,326	\$ -	\$ -	\$ 214,326
Investment stock of a local bank	<u>-</u>	<u>-</u>	<u>10,000</u>	<u>10,000</u>
Total assets at fair value	<u>\$ 214,326</u>	<u>\$ -</u>	<u>\$ 10,000</u>	<u>\$ 224,326</u>

Financial assets and liabilities carried at fair value at June 30, 2014 are classified in the table below in one of the three categories described above:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Equity securities	\$ 122,882	\$ -	\$ -	\$ 122,882
Investment stock of a local bank	<u>-</u>	<u>-</u>	<u>10,000</u>	<u>10,000</u>
Total assets at fair value	<u>\$ 122,882</u>	<u>\$ -</u>	<u>\$ 10,000</u>	<u>\$ 132,882</u>

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at June 30, 2015 and 2014.

Investments in equity securities are valued using market prices on active markets (Level 1). Level 1 instrument valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets.

The investment in common stock of a local bank is designated as a Level 3 instrument due to inherent limitations on the availability of market data. Management believes that the investment's cost fairly approximates its fair value as of June 30, 2015 and 2014.

The preceding methods may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although management 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.

Supplementary Information

Neighborhood House Association

Schedule of Expenditures of Federal Awards Year Ended June 30, 2015

Federal Grantor / Pass-Through Grantor / Program Title	Federal CFDA Number	Award Number	Net Federal Program Expenditures
<u>U.S. Department of Health and Human Services</u>			
Head Start Program	93.600	09CH9118/01	\$ 71,596,707
Passed through from the County of San Diego:			
Aging Cluster:			
Special Programs for the Aging - Title III, Part B - Grants for Supportive Services and Senior Centers	93.044	533569	19,315
Special Programs for the Aging - Title III, Part C - Nutrition Services	93.045	533569	62,318
Nutrition Services Incentive Program	93.053	533569	9,977
Total Aging Cluster			91,610
HIV Emergency Relief Project Grants (Case Management)	93.914	537490	234,445
HIV Emergency Relief Project Grants (Case Management)	93.914	537490	140,385
HIV Emergency Relief Project Grants (Transportation Services)	93.914	536702	68,629
HIV Emergency Relief Project Grants (Transportation Services)	93.914	536702	7,088
Total for HIV Emergency Relief Project Grants			450,547
Total U.S. Department of Health and Human Services			72,138,864
<u>U.S. Department of Agriculture</u>			
Passed through from the State Department of Education:			
Child and Adult Care Food Program:			
Child Care Centers	10.558	04500-CACFP-37-NP-CS	1,328,453
Adult Day Care Centers	10.558	04500-CACFP-37-NP-CS	48,064
Total U.S. Department of Agriculture			1,376,517
<u>U.S. Department of Education</u>			
CCDF Cluster:			
Child Care Mandatory and Matching Funds of the Child Care and Development Fund	93.596	CCTR-4220	178,489
Child Care Mandatory and Matching Funds of the Child Care and Development Fund	93.596	CSPP-4443	95,247
Total for Child Care Mandatory and Matching Funds of the Child Care and Development Fund			273,736
Child Care and Development Block Grant	93.575	CCTR-4220	98,200
Child Care and Development Block Grant	93.575	CSPP-4443	52,402
Total for Child Care and Development Block Grant			150,602
Total CCDF Cluster			424,338
Total U.S. Department of Education			424,338
<u>U.S. Department of Housing and Urban Development</u>			
Passed through from the Rural Community Assistance Corporation:			
Housing Finance Agency Innovation Fund for the Hardest Hit Housing Markets	14.000		71,591
Total Department of Housing and Urban Development			71,591
Total Expenditures of Federal Awards			\$ 74,011,310

Notes:

(1) Program year - July 2014 - February 2015

(2) Program year - March 2015 - June 2015

Value of non-cash assistance (in-kind)

\$ 22,355,854

Amount of insurance expense during the year

294,948

See Notes to Schedules of Expenditures of Federal and State Awards.

Neighborhood House Association

**Schedule of Expenditures of State Awards
Year Ended June 30, 2015**

<u>State Department / Program Title</u>	<u>Award Number</u>	<u>Award Amount</u>	<u>Net Program Expenditures</u>
<u>California State Department of Education</u>			
Child Development Program	CCTR-4220	\$ 657,501	\$ 369,873
Child Development Program	CSPP-4443	<u>3,629,040</u>	<u>3,262,758</u>
Total Expenditures of State Awards		<u>\$ 4,286,541</u>	<u>\$ 3,632,631</u>

See Notes to Schedules of Expenditures of Federal and State Awards.

Neighborhood House Association

Notes to Schedules of Expenditures of Federal and State Awards Year Ended June 30, 2015

Note 1 - Organization and significant accounting policies

General

Neighborhood House Association ("NHA") is a California nonprofit corporation organized to provide an extensive network of services to residents of San Diego County.

NHA provides comprehensive health and human services through programs that include child development, family day care, senior nutrition, adult day health care, mental health services, housing and rental assistance and other related services that assist low-income and less fortunate families.

Basis of presentation

The accompanying schedules of expenditures of Federal and state awards include the Federal and state grant activity of NHA and are presented on the accrual basis of accounting. The information in these schedules is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, Non-Profit Organizations, and with the CDE Audit Guide issued by the California Department of Education.

Program revenues

Revenues from award programs are recognized in the period in which terms of the grant or contractual agreements have been met and the revenue earned.

Noncash awards

Noncash awards are recorded and reflected in the accompanying schedules of expenditures of Federal and state awards at their fair values at the time of receipt or the assessed value provided by NHA.

Net program expenditures

It is the policy of NHA to record expenditures in the period incurred in accordance with the accrual basis of accounting. Where applicable, Federal and state expenditures are reflected net of other income sources.

Subrecipients

During the year ended June 30, 2015, NHA provided \$35,087,959 to sub-grantees under its fund for improvement of Head Start Program (CFDA # 93.600).

Neighborhood House Association

**Notes to Schedules of Expenditures of Federal and State Awards
Year Ended June 30, 2015**

Note 2 - Federal contracts

Reconciliation of reported and audited expenses

Program	Program Expenses
Amount shown on the Schedule of Expenditures of Federal Awards	\$ 71,596,707
Add: obligations liquidated after June 30, 2015	<u>611,130</u>
Total Head Start Expenses Reported on the SF-425	<u><u>\$ 72,207,837</u></u>

Note 3 - Disclosure of audit fees

In accordance with the audit disclosure requirements of the State of California, Department of Education, the audit contract for NHA for the fiscal year ended June 30, 2015 included an audit fee of approximately \$118,000.

Independent Auditor's Report on Internal Control over
Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in
Accordance with *Government Auditing Standards*

To the Audit Committee
Neighborhood House Association

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 Neighborhood House Association ("NHA"), which comprise the statement of financial position as of June 30, 2015, and the related statements of activities, functional expenses and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated November 12, 2015.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered NHA'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of NHA's internal control. Accordingly, we do not express an opinion on the effectiveness of NHA'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 NHA'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.

A handwritten signature in black ink that reads "Cohn Reznick LLP". The signature is written in a cursive, flowing style.

San Diego, California
November 12, 2015

Independent Auditor's Report on Compliance for Each Major
Federal Program and Report on Internal Control over
Compliance Required by OMB Circular A-133

To the Audit Committee
Neighborhood House Association

Report on Compliance for Each Major Federal Program

We have audited Neighborhood House Association's ("NHA") compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that could have a direct and material effect on each of NHA's major Federal programs for the year ended June 30, 2015. NHA's major Federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts and grants applicable to its Federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of NHA's major Federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major Federal program occurred. An audit includes examining, on a test basis, evidence about NHA's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major Federal program. However, our audit does not provide a legal determination of NHA's compliance.

Opinion on Each Major Federal Program

In our opinion, NHA complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major Federal programs for the year ended June 30, 2015.

Report on Internal Control over Compliance

Management of NHA is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered NHA's internal control over compliance with the types of requirements that could have a direct and material effect on each major Federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major Federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of NHA's internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

A handwritten signature in black ink that reads "Cohn Reznick LLP". The signature is written in a cursive, flowing style.

San Diego, California
November 12, 2015

Neighborhood House Association

**Schedule of Findings and Questioned Costs
Year Ended June 30, 2015**

Part I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: Unmodified
Internal control over financial reporting:
Material weaknesses identified? _____yes X no

Significant deficiencies identified? _____yes X none reported

Noncompliance material to financial statements noted? _____yes X no

Federal Awards

Internal control over major programs:
Material weaknesses identified? _____yes X no

Significant deficiencies identified? _____yes X none reported

Type of auditor's report issued on compliance
for major programs: Unmodified

Any audit findings disclosed that are required to be
reported in accordance with Section .510(a) of
Circular A-133? _____yes X no

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program</u>	<u>Amount</u>
93.600	Head Start Program	\$71,596,707

Dollar threshold used to distinguish between
Type A and Type B programs: \$ 2,220,339

Auditee qualified as low-risk auditee? X yes _____no

Neighborhood House Association
Schedule of Findings and Questioned Costs
Year Ended June 30, 2015

Part II - Financial Statement Findings Section

This section identifies the significant deficiencies, material weaknesses and instances of noncompliance related to the financial statements for which *Government Auditing Standards* require reporting in a Circular A-133 audit.

Findings for fiscal year ended 2015: None.

Part III - Federal Award Findings and Questioned Costs Section

This section identifies the audit findings required to be reported by Circular A-133 Section .510(a) (for example, significant deficiencies, material weaknesses and material instances of noncompliance, including questioned costs), as well as any abuse findings involving Federal awards that are material to a major program.

Findings for fiscal year ended 2015: None.

Neighborhood House Association

**Schedule of Prior Audit Findings
Year Ended June 30, 2014**

None.