



*REPORT OF INDEPENDENT AUDITORS
AND FINANCIAL STATEMENTS WITH
FEDERAL AWARDS SUPPLEMENTARY INFORMATION*

FOR

EPISCOPAL COMMUNITY SERVICES

June 30, 2017 and 2016

MOSSADAMS.COM

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Report of Independent Auditors

The Board of Directors
Episcopal Community Services

Report on the Financial Statements

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

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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 audits 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 Episcopal Community Services as of June 30, 2017 and 2016, 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

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2 *U.S. Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* is presented for purposes of additional analysis and is 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 financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the 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 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 October 19, 2017 on our consideration of Episcopal Community Services' 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 solely 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 the effectiveness of Episcopal Community Services' 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 Episcopal Community Services' internal control over financial reporting and compliance.

Moss Adams LLP

Dan Diego, California
October 19, 2017

Episcopal Community Services
Statements of Financial Position
June 30, 2017 and 2016

	2017	2016
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 870,130	\$ 1,046,615
Investments	1,332,439	1,196,191
Receivables, net	1,626,616	825,945
Unconditional promise to give	-	38,000
Prepaid expenses and other current assets	183,286	102,034
Total current assets	4,012,471	3,208,785
Deposits and Other Assets	259,496	201,395
Unconditional Promises to Give, net	451,910	600,950
Property and Equipment, net	1,322,636	1,177,175
Total assets	\$ 6,046,513	\$ 5,188,305
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts payable and accrued expenses	\$ 1,114,304	\$ 506,598
Accrued payroll	797,108	1,118,903
Deferred revenue	32,498	-
Current portion of long-term debt	140,214	31,088
Total current liabilities	2,084,124	1,656,589
Long-Term Debt	500,522	380,382
Conditional Contribution	-	222,000
Total liabilities	2,584,646	2,258,971
Commitments and Contingencies (Notes 9, 12, and 14)		
Net Assets		
Unrestricted	2,998,763	2,288,613
Temporarily restricted	463,104	640,721
Total net assets	3,461,867	2,929,334
Total liabilities and net assets	\$ 6,046,513	\$ 5,188,305

Episcopal Community Services
Statements of Activities
Years Ended June 30, 2017 and 2016

	2017			2016		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
REVENUES, GAINS, AND OTHER SUPPORT						
Grants and contracts	\$ 22,673,612	\$ -	\$ 22,673,612	\$ 22,100,447	\$ -	\$ 22,100,447
Service fees	2,238,750	-	2,238,750	2,327,820	-	2,327,820
Contributions	449,037	11,194	460,231	366,797	39,771	406,568
Other (Note 16)	455,929	-	455,929	49,347	-	49,347
Investment income (loss)	136,249	-	136,249	(1,910)	-	(1,910)
Change in value of beneficial interests in charitable remainder trusts	-	(149,040)	(149,040)	-	125,929	125,929
Net assets released from restrictions	39,771	(39,771)	-	-	-	-
Total revenues, gains, and other support	<u>25,993,348</u>	<u>(177,617)</u>	<u>25,815,731</u>	<u>24,842,501</u>	<u>165,700</u>	<u>25,008,201</u>
EXPENSES						
Programs:						
Child development	17,106,492	-	17,106,492	17,193,758	-	17,193,758
Clinical services	3,286,240	-	3,286,240	2,874,563	-	2,874,563
Housing and supportive services	1,707,099	-	1,707,099	1,919,018	-	1,919,018
Nutrition services	827,944	-	827,944	670,444	-	670,444
Total program expenses	<u>22,927,775</u>	<u>-</u>	<u>22,927,775</u>	<u>22,657,783</u>	<u>-</u>	<u>22,657,783</u>
Management and general	2,379,485	-	2,379,485	2,502,389	-	2,502,389
Fundraising and communications	215,524	-	215,524	149,000	-	149,000
Total expenses	<u>25,522,784</u>	<u>-</u>	<u>25,522,784</u>	<u>25,309,172</u>	<u>-</u>	<u>25,309,172</u>
	470,564	(177,617)	292,947	(466,671)	165,700	(300,971)
Gain on transfer of property (Note 16)	<u>239,586</u>	<u>-</u>	<u>239,586</u>	<u>-</u>	<u>-</u>	<u>-</u>
	710,150	(177,617)	532,533	(466,671)	165,700	(300,971)
Beginning of year	<u>2,288,613</u>	<u>640,721</u>	<u>2,929,334</u>	<u>2,755,284</u>	<u>475,021</u>	<u>3,230,305</u>
End of year	<u>\$ 2,998,763</u>	<u>\$ 463,104</u>	<u>\$ 3,461,867</u>	<u>\$ 2,288,613</u>	<u>\$ 640,721</u>	<u>\$ 2,929,334</u>

**Episcopal Community Services
Statements of Functional Expenses
Years Ended June 30, 2017 and 2016**

2017				
	Programs	Management and General	Fundraising and Communications	Total
Personnel	\$ 15,884,527	\$ 1,650,244	\$ 91,750	\$ 17,626,521
Other direct costs	4,236,565	437,561	113,165	4,787,291
Occupancy	2,576,620	271,182	10,609	2,858,411
Depreciation	230,063	20,136	-	250,199
Interest	-	362	-	362
Total expenses	\$ 22,927,775	\$ 2,379,485	\$ 215,524	\$ 25,522,784

2016				
	Programs	Management and General	Fundraising and Communications	Total
Personnel	\$ 15,680,637	\$ 1,656,708	\$ 85,142	\$ 17,422,487
Other direct costs	4,321,357	552,920	52,990	4,927,267
Occupancy	2,317,168	271,978	10,868	2,600,014
Depreciation	331,836	20,136	-	351,972
Interest	6,785	647	-	7,432
Total expenses	\$ 22,657,783	\$ 2,502,389	\$ 149,000	\$ 25,309,172

Episcopal Community Services
Statements of Cash Flows
Years Ended June 30, 2017 and 2016

	2017	2016
OPERATING ACTIVITIES		
Change in net assets	\$ 532,533	\$ (300,971)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	250,199	351,972
Loss on disposal of property and equipment	4,729	31,099
Gain on transfer of property (Note 16)	(239,586)	-
Change in value of charitable remainder trusts	149,040	(125,929)
Net realized and unrealized (gains) losses net of fees on investments	(100,813)	39,189
Deferred revenue	32,498	-
Allowance for uncollectible receivables	-	10,881
Accrued interest added to note payable	-	6,785
Conditional contribution forgiveness	-	(24,600)
(Increase) decrease in operating assets:		
Receivables	(800,671)	470,323
Prepaid expenses and other current assets	(81,252)	114,812
Deposits and other assets	(58,101)	(34,733)
Unconditional promises to give	38,000	(38,000)
Increase (decrease) in operating liabilities:		
Accounts payable and accrued expenses	607,706	(219,882)
Accrued payroll	(321,795)	59,266
Net cash provided by operating activities	12,487	340,212
INVESTING ACTIVITIES		
Purchases of property and equipment	(122,448)	(116,808)
Purchases of investments	(35,435)	(37,279)
Net cash used in investing activities	(157,883)	(154,087)
FINANCING ACTIVITIES		
Repayment of long-term debt	(31,089)	(30,803)
Net cash used in financing activities	(31,089)	(30,803)
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(176,485)	155,322
CASH AND CASH EQUIVALENTS		
Beginning of year	1,046,615	891,293
End of year	\$ 870,130	\$ 1,046,615
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash payments for interest	\$ 362	\$ 647
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Additions to property and equipment with long-term debt	\$ 611,512	\$ -

Episcopal Community Services

Notes to Financial Statements

Note 1 – Nature of Organization

Episcopal Community Services (“ECS”), a California not-for-profit public benefit corporation, and in California a not-for-profit religious organization, which provides services to the community through programs that address specific social needs, is affiliated with the Episcopal Diocese of San Diego.

Programs offered by ECS are:

Child development programs – Head Start and Early Head Start are federally-funded comprehensive child development programs serving pregnant women, children from birth to age five, and their families. The programs are designed to help break the cycle of poverty by providing preschool children of low-income families with a comprehensive program to meet their emotional, social, health, nutritional, and psychological needs.

Other programs – ECS also offers programs that assist individuals and families through the often difficult transition from an existence which is dependent on social services, unhealthy relationships, or substance abuse to one of self-sufficiency. ECS offers a full spectrum of services to Southern Californians in transition, including emergency assistance and crisis intervention, drug and alcohol education and support services, employment assistance, food, counseling services for the chronically mentally ill, and short-term housing for the special-needs homeless population. ECS provides mental health services to low-income children and their families with behavioral problems as a result of having experienced trauma, divorce, illness, neglect, violence in the home, or drug abuse.

Income taxes – ECS 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. ECS may be subject to federal or state income taxes on unrelated business income. For each of the years ended June 30, 2017 and 2016, no provision for such taxes is required. ECS had no unrecognized tax benefits or liabilities as of June 30, 2017 and 2016. ECS files an exempt organization return in the United States federal jurisdiction and with the Franchise Tax Board in the state of California.

Note 2 – Summary of Significant Accounting Policies

Method of accounting – The financial statements have been prepared on the accrual basis of accounting.

Financial statement presentation – Net assets are classified as unrestricted, temporarily restricted, and permanently restricted based upon the following criteria:

- Unrestricted net assets represent expendable funds available for operations that are not otherwise limited by donor restrictions.
- Temporarily restricted net assets consist of contributed funds subject to specific donor-imposed restrictions which are contingent upon a specific performance of a future event or a specific passage of time before ECS may spend the funds.

Episcopal Community Services

Notes to Financial Statements

Note 2 – Summary of Significant Accounting Policies (continued)

- Permanently restricted net assets are subject to irrevocable donor restrictions requiring that the assets be maintained in perpetuity, primarily for generating investment income to fund current operations. ECS has no permanently restricted net assets at June 30, 2017 and 2016.

Revenue Recognition:

Grants and contracts – Revenue is recognized from grants and contracts to the extent that eligible costs are incurred and as services are provided.

Service fees – Revenue from service fees are recognized when services are provided.

Contributions – Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. Contributions subject to donor-imposed restrictions for use in a future period or for a specific purpose are either reported as temporarily or permanently restricted, depending on the nature of the donor's restriction. When a donor restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Contributions with donor restrictions which are met in the same reporting period are reported as unrestricted revenue.

Other – Revenue from services provided to a third-party developer was recognized when the services were provided. See Note 16.

Cash and cash equivalents – ECS considers all highly-liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

Restricted cash – In accordance with the terms of a contract with a funding agency, funds received for the Head Start program are required to be maintained in a separate bank account. As of June 30, 2017 and 2016, approximately \$545,000 and \$174,000, respectively, of the Head Start program funds were held in a separate bank account. These funds are included in cash in the accompanying statements of financial position.

Investments – Investments are reported at fair value based on quoted prices in active markets. The Controller, as monitored by the Chief Financial Officer, reviews and evaluates the values provided by investment managers annually and agrees with the valuation methods used.

Investment income or loss (including interest and realized gains and losses) is included in unrestricted revenues unless restricted by donor or law.

Receivables – Receivables consist of amounts due to ECS for services provided through June 30 that have not yet been collected. Amounts are generally considered past due if not collected within 30 days of billings. Interest is not charged on outstanding balances.

Note 2 – Summary of Significant Accounting Policies (continued)

Unconditional promises to give – Unconditional promises to give expected to be collected in future years are recorded at fair value when the promise is made based on a discounted cash flow model. In future years, the discounts to present value are computed using discount rates established in the years in which those promises are received. Amortization of the discounts is included in contributions.

Included in unconditional promises to give are beneficial interests ECS has received in irrevocable charitable remainder trusts (“CRTs”). The trust agreements require the trusts to make periodic payments, as defined, to the grantors or other designated beneficiaries of the trust over the beneficiary’s lifetime and, in some cases, after the beneficiary’s death. The trusts terminate upon the death of the grantors or completion of the specified benefit periods after their death. Upon termination of the trusts, ECS will receive its share of the remaining trust assets as designated in the trust agreements. The portion of a trust attributable to the fair value of the future benefits to be received by ECS is recorded in the statement of activities as temporarily restricted contributions in the year the trust is established. The fair value of the beneficial interests in CRTs at June 30, 2017 and 2016 is calculated based on a discounted cash flow model using the fair value of the assets in the trusts as provided by the trustees, interest rates of approximately 2 percent and life expectancies (based on applicable mortality tables) and other terms, as applicable, for payments to beneficiaries beyond the life expectancies ranging from 4 to 25 years. The unobservable inputs used in the calculations are evaluated and adjusted, as necessary, annually by the Controller, as monitored by the Chief Financial Officer.

Allowance for estimated uncollectible accounts – The allowance for estimated uncollectible accounts is based on past experience and on an analysis of current receivables. ECS does not obtain collateral. Accounts deemed uncollectible are written-off against the allowance in the year deemed uncollectible. Management established an allowance of approximately \$27,000 on receivables from client service fees as of June 30, 2017 and 2016.

Property and equipment – Property and equipment are recorded at cost for purchased assets and fair value at the date of donation for donated assets. Certain property and equipment acquired with grant funds are capitalized and are considered to be owned by the granting agency. Depreciation is computed using the straight-line method over the estimated useful lives of the assets ranging from 5 to 25 years. It is ECS’s policy to capitalize purchases with a cost greater than \$5,000.

Impairment of long-lived assets – ECS evaluates long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. If the estimated future cash flows (undiscounted and without interest charges) from the use of an asset are less than the carrying value, a write-down would be recorded to reduce the related asset to its estimated fair value. To date, no such write-downs have occurred.

Functional allocation of expenses – The costs of providing the various programs and other activities have been summarized on a functional basis in the statements of activities. Accordingly, certain costs have been allocated among the programs 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 related to the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may materially differ from those estimates.

Episcopal Community Services

Notes to Financial Statements

Note 2 – Summary of Significant Accounting Policies (continued)

Reclassifications - Certain amounts in the June 30, 2016 statement of activities have been reclassified to conform to the June 30, 2017 presentation, with no effect on net assets.

New accounting pronouncement – The June 30, 2017 financial statements reflect adoption of Financial Accounting Standards Board Accounting Standards Update (“ASU”) No. 2014.15, *Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern*. The adoption of this update does not have a material effect on the financial statements. ASU 2014-15 defines management’s responsibility to evaluate whether there is a substantial doubt about an organization’s ability to continue as a going concern and to provide related footnote disclosures. Management has concluded that there is not substantial doubt about ECS’s ability to continue as a going concern through October 19, 2018.

Subsequent events – Subsequent events are events or transactions that occur after the statement of financial position date, but before the financial statements are issued. ECS recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the statement of financial position, including the estimates inherent in the process of preparing the financial statements. ECS’s financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of financial position, but arose after the statement of financial position date and before the financial statements are available to be issued. ECS has evaluated subsequent events through October 19, 2017, which is the date the financial statements were available to be issued.

Note 3 – Concentrations

Cash and cash equivalents – ECS maintains cash and cash equivalents in bank deposit accounts which at times exceed the federally-insured deposit limits. ECS has not experienced any losses in such accounts.

Investments – ECS maintains investments in accounts which at times exceed the Securities Investors Protection Corporation (“SIPC”) limits. ECS has not experienced any losses in such accounts.

Unconditional promises to give – Unconditional promises to give include beneficial interests in CRTs which are exposed to various risks such as interest rates, change in value of underlying assets in the trusts, and donor life expectancies. Changes in the near-term are not expected to materially affect the amounts reported in the financial statements. As of June 30, 2017 and 2016, approximately 96 percent of beneficial interests in CRTs is due from two trusts.

Grants and contracts – Included in revenue from grants and contracts during the years ended June 30, 2017 and 2016 is approximately \$18,488,000 and \$18,106,000, respectively, earned from one funding source. These amounts represent approximately 72 percent of total revenues, gains, and other support for each of the years ended June 30, 2017 and 2016. Included in receivables from grants and contracts is approximately \$659,000 and \$447,000 due from one and two funding source(s) for the years ended June 30, 2017 and 2016, respectively.

Episcopal Community Services
Notes to Financial Statements

Note 4 – Investments

Investments at fair value consist of the following at June 30:

	<u>2017</u>	<u>2016</u>
Stock funds	\$ 762,266	\$ 686,625
Bond funds	439,703	382,687
Real estate funds	73,834	75,541
Reinsurance-related securities fund	38,339	35,282
Cash and cash equivalents	<u>18,297</u>	<u>16,056</u>
 Total investments	 <u>\$ 1,332,439</u>	 <u>\$ 1,196,191</u>

Investment income consists of the following for the year ended June 30:

Net realized and unrealized gains (losses)	\$ 109,304	\$ (31,266)
Interest and dividends	35,436	37,279
Investment fees	<u>(8,491)</u>	<u>(7,923)</u>
 Total investment income (loss)	 <u>\$ 136,249</u>	 <u>\$ (1,910)</u>

See Note 2 for the valuation methodologies used for investments that are measured at fair value on a recurring basis and recognized in the accompanying statements of financial position and Note 7 for classification in the fair value hierarchy.

Note 5 – Receivables

As of June 30, receivables consist of:

	<u>2017</u>	<u>2016</u>
Grants and contracts	\$ 1,259,167	\$ 685,705
Service fees	94,739	128,273
Other (Note 16)	<u>300,000</u>	<u>39,257</u>
	1,653,906	853,235
Less allowance for doubtful accounts	<u>(27,290)</u>	<u>(27,290)</u>
 Total receivables	 <u>\$ 1,626,616</u>	 <u>\$ 825,945</u>

Episcopal Community Services

Notes to Financial Statements

Note 6 – Unconditional Promises to Give

As of June 30, unconditional promises to give consist of:

	<u>2017</u>	<u>2016</u>
Due in less than one year:		
Pledge receivable	\$ -	\$ 38,000
Due in more than five years:		
Beneficial interest in CRTs	728,258	876,362
Less discount to fair value	<u>(276,348)</u>	<u>(275,412)</u>
Total beneficial interest in CRTs	<u>451,910</u>	<u>600,950</u>
 Net unconditional promises to give	 <u>\$ 451,910</u>	 <u>\$ 638,950</u>

See Note 2 for the valuation methodologies used for beneficial interests in CRTs that are measured at fair value on a recurring basis and recognized in the accompanying statements of financial position. The beneficial interests in CRTs are classified as Level 3 in the fair value hierarchy (see Note 7).

Note 7 – Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. There are three levels of inputs that may be used to measure fair value:

Level 1 – Quoted prices in active markets for identical assets or liabilities;

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Investments are exposed to various risks such as interest rates, market, and credit risk. Risk is managed through rigorous evaluation before an investment is made, quarterly monitoring of valuations and regular communication with investment managers. It is at least reasonably possible, given the level of risk associated with investments, that changes in the near term could materially affect the amounts reported in the financial statements.

Episcopal Community Services Notes to Financial Statements

Note 7 – Fair Value Measurements (continued)

The following table presents the assets carried at fair value on the statement of financial position as of June 30, 2017 and 2016:

	June 30, 2017			Total
	Level 1	Level 2	Level 3	
Stock funds:				
U.S. Large	\$ 367,304	\$ -	\$ -	\$ 367,304
U.S. Small-Medium	147,095	-	-	147,095
Foreign	247,867	-	-	247,867
Bond funds:				
Domestic	326,183	-	-	326,183
Foreign	113,520	-	-	113,520
Real estate funds:				
Domestic	42,929	-	-	42,929
Foreign	30,905	-	-	30,905
Reinsurance-related securities fund	38,339	-	-	38,339
Cash and cash equivalents	18,297	-	-	18,297
Subtotal investments	1,332,439	-	-	1,332,439
Beneficial interests in CRTs	-	-	451,910	451,910
Total assets measured at fair value	<u>\$ 1,332,439</u>	<u>\$ -</u>	<u>\$ 451,910</u>	<u>\$ 1,784,349</u>
	June 30, 2016			Total
	Level 1	Level 2	Level 3	
Stock funds:				
U.S. Large	\$ 337,887	\$ -	\$ -	\$ 337,887
U.S. Small-Medium	139,267	-	-	139,267
Foreign	209,471	-	-	209,471
Bond funds:				
Domestic	286,582	-	-	286,582
Foreign	96,105	-	-	96,105
Real estate funds:				
Domestic	46,241	-	-	46,241
Foreign	29,300	-	-	29,300
Reinsurance-related securities fund	35,282	-	-	35,282
Cash and cash equivalents	16,056	-	-	16,056
Subtotal investments	1,196,191	-	-	1,196,191
Beneficial interests in CRTs	-	-	600,950	600,950
Total assets measured at fair value	<u>\$ 1,196,191</u>	<u>\$ -</u>	<u>\$ 600,950</u>	<u>\$ 1,797,141</u>

Episcopal Community Services

Notes to Financial Statements

Note 7 – Fair Value Measurements (continued)

The following table discloses the summary of changes in the fair value of ECS' Level 3 assets (beneficial interests in CRTs) for the years ended June 30:

Balance, July 1, 2015	\$ 475,021
Change in value of beneficial interests in CRTs	<u>125,929</u>
Balance, June 30, 2016	600,950
Change in value of beneficial interest in CRTs	<u>(149,040)</u>
Balance, June 30, 2017	<u><u>\$ 451,910</u></u>

The change in value of the beneficial interests in CRTs is a separate line in the statements of activities.

Note 8 – Property and Equipment

As of June 30, property and equipment consists of:

	<u>2017</u>	<u>2016</u>
Leasehold improvements	\$ 2,203,133	\$ 1,855,177
Equipment	915,960	979,986
Buildings and improvements (Note 16)	-	666,226
Vehicles	<u>335,248</u>	<u>299,424</u>
	3,454,341	3,800,813
Less accumulated depreciation and amortization	<u>(2,131,705)</u>	<u>(2,747,338)</u>
	1,322,636	1,053,475
Land (Note 16)	<u>-</u>	<u>123,700</u>
Total	<u><u>\$ 1,322,636</u></u>	<u><u>\$ 1,177,175</u></u>

Episcopal Community Services Notes to Financial Statements

Note 9 – Debt

As of June 30, long-term debt consists of:

	2017	2016
Note payable, Paul H. Liljestrand Partners LP, unsecured. Bears simple interest of 4.75 percent per annum. Monthly principal and interest payments of \$11,470; due June 2022.	\$ 611,512	\$ -
Note payable, San Diego Housing Commission. Balance outstanding assigned to third-party in August 2016; Note 16.	-	351,157
Note payable, Episcopal Diocese of Los Angeles, unsecured. Annual payments of \$25,000; non-interest bearing; due December 2018.	25,000	50,000
Note payable, Episcopal Diocese of San Diego, unsecured. Monthly principal and interest payments of \$538; interest of 4.8 percent; due March 2018.	4,224	10,313
	640,736	411,470
Less current portion	140,214	31,088
Total	\$ 500,522	\$ 380,382

Future minimum debt service payments are as follows:

Years ending June 30,		
2018		\$ 140,214
2019		116,378
2020		122,028
2021		127,952
2022		134,164
Total		\$ 640,736

Line of credit – ECS has a revolving bank line of credit in the amount of \$500,000 secured by assets of ECS. No balance was outstanding on the line of credit as of June 30, 2017 and 2016. The interest rate on the line is the bank’s prime rate plus 0.250 percent (3.25 percent at June 30, 2017).

Total interest expense on debt was approximately \$360 and \$7,400 for the years ended June 30, 2017 and 2016, respectively.

Episcopal Community Services

Notes to Financial Statements

Note 10 – Conditional Contribution

During 1999, ECS was awarded a conditional contribution of \$394,200 from the San Diego Housing Commission ("SDHC"). The contribution was used to purchase or rehabilitate facilities that were placed into service during November 1999, and was utilized by ECS to provide supportive housing to the homeless. The SDHC funds were used for the San Diego Downtown Safe Haven facility.

In August 2016, ECS assigned the San Diego Downtown Safe Haven buildings and improvements and land and the associated debt (Note 9) to a third party developer for the purpose of constructing permanent supportive housing. This transaction resulted in the recognition of the remaining conditional contribution from the San Diego Housing Commission of \$222,000, which is included in the gain on transfer of property in the accompanying statement of activities for the year ended June 30, 2017 (Note 16).

Note 11 – Temporarily Restricted Net Assets

As of June 30, temporarily restricted net assets consist of:

	<u>2017</u>	<u>2016</u>
Time restrictions:		
Charitable remainder trusts	\$ 451,910	\$ 600,950
Purpose restrictions - programs	<u>11,194</u>	<u>39,771</u>
Total	<u>\$ 463,104</u>	<u>\$ 640,721</u>

For the year ended June 30, 2017, a total of approximately \$40,000 was released from temporarily restricted net assets and was comprised of approximately \$38,000 released for program administration and approximately \$2,000 released for Head Start.

Note 12 – Employee Benefit Plan

ECS has a 401(k) retirement plan (the "Plan") that provides salary deferral and matching employer contributions. Beginning on July 1, 2016 the Plan was amended to include a safe harbor nonelective contribution in which the organization makes a contribution equal to three percent of compensation. All employees who have completed one month of service and are 21 years of age are eligible. ECS has expensed and accrued contributions to the Plan totaling approximately \$379,000 and \$299,000 for the years ended June 30, 2017 and 2016, respectively.

Note 13 – Union Contract

A substantial portion of ECS's labor force is subject to a collective bargaining agreement. The agreement expires June 30, 2020.

Episcopal Community Services Notes to Financial Statements

Note 14 – Commitments and Contingencies

ECS occupies facilities in various locations under month-to-month and long-term operating leases with terms extending through July 2027. Rental expense under operating leases was approximately \$1,786,000 and \$1,698,000 for the years ended June 30, 2017 and 2016, respectively.

Future minimum annual rentals under long-term operating leases at June 30, 2017 are as follows:

Years ending June 30,	
2018	\$ 1,905,000
2019	1,495,642
2020	1,342,916
2021	1,382,401
2022	1,112,060
Thereafter	<u>2,493,890</u>
 Total	 <u><u>\$ 9,731,909</u></u>

Grants and contracts – ECS has contracts with government agencies which are subject to audit. No provision has been made for any additional liabilities that may arise from such audits, since the amounts, if any, cannot be determined. Management believes that any additional liability that may result from any such audits would not be material. Certain of these contracts may be terminated or reduced with 30-days written notice to ECS in the event that federal, state, or county funding for the agreement ceases or is reduced prior to the expiration dates of the contracts.

Risks and uncertainties – The operations of ECS are subject to the administrative directives, rules, and regulations of federal, state, and local regulatory agencies. Such administrative directives, rules, and regulations are subject to change by an act of Congress or other government agency or an administrative change. Such changes may occur with little notice or inadequate funding to pay for the related cost, including the additional administrative burden, if any, to comply with a change.

Legal – ECS is a party to certain legal actions and investigations arising in the ordinary course of business. Management and ECS's legal counsel are unable to determine the likelihood of unfavorable outcomes, if any.

Episcopal Community Services

Notes to Financial Statements

Note 15 – Related-party Transactions

Related-party transactions as of and for the years ended June 30 are as follows:

	2017	2016
Note payable to Episcopal Diocese of Los Angeles	\$ 25,000	\$ 50,000
Note payable to Episcopal Diocese of San Diego	4,224	10,313
Contribution from Episcopal Diocese of San Diego	25,798	23,570

ECS also has a beneficial interest in a CRT for which a member of the Board of Directors is a trustee. ECS's beneficial interest is valued at approximately \$200,000 and \$347,000 as of June 30, 2017 and 2016, respectively.

Note 16 – Transfer of Property

In August 2016, buildings and improvements and land with a net book value of \$333,571 used in the San Diego Downtown Safe Haven housing program and the associated debt to the San Diego Housing Commission on the property of \$351,157 was assigned to a third-party developer for the purpose of construction of permanent supportive housing. Also related to the transaction was the recognition of the remaining conditional contribution of \$222,000 associated with this property. A net gain on the transfer of property of \$239,586 is recognized in the accompanying statement of activities for the year ended June 30, 2017. The agreement for the transfer of the property required ECS to provide various pre-development services for a fee of \$300,000 to be paid by the third-party developer. These services were provided and the \$300,000 fee is included in other income in the accompanying statement of activities for the year ended June 30, 2017.

Supplementary Information

**Episcopal Community Services
Supplementary Information
Schedule of Expenditures of Federal Awards
Year Ended June 30, 2017**

Federal Agency/ Pass-through Entity/Program Title	CFDA Number	Pass-through Identifying Number	Passed-through to Subrecipients	Total Expenditures
Department of Health and Human Services:				
Administration for Children and Families:				
Passed-through Neighborhood House Association:				
Head Start	93.600	14-004812-DA	\$ -	\$ 12,754,785
Early Head Start	93.600	14-004812-DA	-	5,600,165
Training and Technical Assistance	93.600	14-004812-DA	-	132,610
<i>Total Head Start Cluster</i>			-	18,487,560
Substance Abuse Prevention Treatment Program:				
Passed-through the County of San Diego				
Projects for Assistance in Transition from Homelessness	93.150	541693	-	314,488
Block Grants for Prevention and Treatment of Substance Abuse	93.959	554898	-	78,452
<i>Total Department of Health and Human Services</i>			-	18,880,500
Department of Housing and Urban Development:				
Community Planning and Development:				
Supportive Housing Program - Downtown Safe Haven	14.235		-	260,087
Passed-through San Diego Housing Commission:				
Section-8 Moderate Rehabilitation Single Room Occupancy	14.249	52530B	-	91,780
<i>Total Department of Housing and Urban Development</i>			-	351,867
Department of Veterans Affairs ("VA"):				
VA Homeless Providers Grant and Per Diem Program	64.024		-	118,629
<i>Total Department of Veterans Affairs</i>			-	118,629
Department of Agriculture:				
Food and Nutrition Service:				
Passed-through the State of California, Department of Education, Food, and Consumer Service:				
Child and Adult Care Food Program	10.558	37-1550-OJ	-	626,748
<i>Total Department of Agriculture</i>			-	626,748
<i>Total expenditures of federal awards</i>			\$ -	\$ 19,977,744

Episcopal Community Services

Supplementary Information

Notes to Schedule of Expenditures of Federal Awards

Note 1 – Basis of Presentation

The accompanying schedule of expenditures of federal awards (the “Schedule”) includes the federal grant activity of Episcopal Community Services (“ECS”), under programs of the federal government for the year ended June 30, 2017. The information in this schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the “Uniform Guidance”).

Because this schedule presents only a selected portion of the activities of ECS, it is not intended to, and does not, present either the financial position or changes in net assets of ECS.

Note 2 – Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowed or are limited as to reimbursement. Pass-through entity identifying numbers are presented where available.

ECS has elected to use the 10 percent de minimis indirect cost rate as allowed under the Uniform Guidance.

Report of Independent Auditors 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*

Board of Directors
Episcopal Community Services

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 Episcopal Community Services, which comprise the statement of financial position as of June 30, 2017, 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 October 19, 2017.

Internal Control Over Financial Reporting

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

Moss Adams LLP

San Diego, California
October 19, 2017

Report of Independent Auditors on Compliance for The Major Federal Program and Report on Internal Control over Compliance Required by the Uniform Guidance

The Board of Directors
Episcopal Community Services

Report on Compliance for the Major Federal Program

We have audited Episcopal Community Services' compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on Episcopal Community Services' major federal program for the year ended June 30, 2017. Episcopal Community Services' major federal program is 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 federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for Episcopal Community Services' major federal program 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 the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* ("Uniform Guidance"). Those standards and the Uniform Guidance 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 Episcopal Community Services' 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 the major federal program. However, our audit does not provide a legal determination of Episcopal Community Services' compliance.

Opinion on the Major Federal Program

In our opinion, Episcopal Community Services complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on the major federal program for the year ended June 30, 2017.

Report on Internal Control Over Compliance

Management of Episcopal Community Services 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 Episcopal Community Services' internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, 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 Episcopal Community Services' 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 a 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 the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Moss Adams LLP

San Diego, California
October 19, 2017

Episcopal Community Services
Schedule of Findings and Questioned Costs
Year Ended June 30, 2017

Section I – Summary of Auditor’s Results

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP: Unmodified

Internal control over financial reporting:

- Material weakness(es) identified? Yes No
- Significant deficiency(ies) identified? Yes None reported

Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over the major federal program:

- Material weakness(es) identified? Yes No
- Significant deficiency(ies) identified? Yes None reported

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? Yes No

Identification of the Major Federal Program

CFDA Number	Name of Federal Program or Cluster	Type of auditor’s report issued on compliance for the major federal program:
93.600	Head Start Cluster	Unmodified

Dollar threshold used to distinguish between Type A and Type B programs: \$750,000

Auditee qualified as low-risk auditee? Yes No

Section II – Financial Statement Findings

None reported.

Section III – Federal Award Findings and Questioned Costs

None reported.



Summary Schedule of Prior Audit Findings

Name of Auditee: Episcopal Community Services

Period Covered by the Audit: July 1, 2016 to June 30, 2017

Name of Audit Firm: Moss Adams LLP

There were no open findings from the prior audit report.

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