
**CHILD & FAMILY RESOURCES, INC.
AND SUBSIDIARY**

**INDEPENDENT AUDITOR'S REPORT
AND CONSOLIDATED FINANCIAL STATEMENTS
WITH SUPPLEMENTARY INFORMATION**

YEARS ENDED JUNE 30, 2016 AND 2015



**CHILD & FAMILY RESOURCES, INC.
AND SUBSIDIARY**

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Child & Family Resources, Inc.
and Subsidiary
Tucson, Arizona

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Child & Family Resources, Inc. and Subsidiary (nonprofit organizations), which comprise the consolidated statements of financial position as of June 30, 2016, and the related consolidated statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 consolidated financial statements are free from material misstatement.

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

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

(continued)

Opinion

In our opinion, the 2016 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Child & Family Resources, Inc. and Subsidiary as of June 30, 2016, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Prior Period Financial Statements

The consolidated financial statements of Child & Family Resources, Inc. and subsidiary as of June 30, 2015, were audited by other auditors whose report dated December 30, 2015, expressed an unmodified opinion on those statements.

Other Matters

Report on Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information starting on page 24 is presented for purposes of additional analysis and is not a required part of the consolidated 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 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated 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 consolidated 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 December 16, 2016, on our consideration of Child & Family Resources, Inc.'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 Child & Family Resources, Inc.'s internal control over financial reporting and compliance.

Regina Ann + Monroe, L.L.P.

December 16, 2016
Tucson, Arizona

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

June 30, 2016 and 2015

ASSETS

	2016	2015
CURRENT ASSETS		
Cash and cash equivalents	\$ 878,458	\$ 705,272
Grants and accounts receivable, net	3,160,469	3,156,565
Investments	596,919	607,374
Prepaid expenses	81,140	54,756
Total current assets	4,716,986	4,523,967
PROPERTY AND EQUIPMENT, NET	2,725,920	2,831,757
OTHER ASSETS		
Deposits	53,778	48,151
Total assets	\$ 7,496,684	\$ 7,403,875

The Notes to Consolidated Financial Statements are an integral part of these statements.

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

June 30, 2016 and 2015

LIABILITIES AND NET ASSETS

	2016	2015
CURRENT LIABILITIES		
Accounts payable	\$ 1,059,495	\$ 1,001,913
Accrued expenses and other liabilities	633,278	672,120
Lines of credit	344,598	918,723
Current portion of capital leases	305	10,478
Current portion of deferred grant obligation	24,144	24,144
Current portion of long-term debt	26,994	27,011
Total current liabilities	2,088,814	2,654,389
LONG-TERM LIABILITIES		
Long-term portion capital leases	-	305
Long-term portion of deferred grant obligation	144,865	169,009
Long-term debt	377,359	403,996
Total liabilities	2,611,038	3,227,699
NET ASSETS		
Unrestricted		
General operating	2,394,352	1,655,879
Investment in capital assets	2,321,567	2,389,967
Board designated	60,000	-
Total unrestricted net assets	4,775,919	4,045,846
Temporarily restricted	109,727	130,330
Total net assets	4,885,646	4,176,176
Total liabilities and net assets	\$ 7,496,684	\$ 7,403,875

The Notes to Consolidated Financial Statements are an integral part of these statements.

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF ACTIVITIES

For the Year Ended June 30, 2016

	Unrestricted	Temporarily Restricted	Total
REVENUES			
Federal and government grants	\$ 22,637,649	\$ -	\$ 22,637,649
Parent fees	518,577	-	518,577
Other grants	89,007	78,850	167,857
Contributions	473,670	-	473,670
Other program revenue	95,515	-	95,515
Other revenue	709,384	-	709,384
In-kind contributions	41,692	-	41,692
United Way	20,908	-	20,908
Investment loss	(5,325)	-	(5,325)
Net assets released from restrictions	99,453	(99,453)	-
	<u>24,680,530</u>	<u>(20,603)</u>	<u>24,659,927</u>
Total revenues			
EXPENSES			
Program services	21,366,256	-	21,366,256
General and administrative	2,274,719	-	2,274,719
Fund-raising	309,482	-	309,482
	<u>23,950,457</u>	<u>-</u>	<u>23,950,457</u>
Total expenses			
CHANGE IN NET ASSETS	730,073	(20,603)	709,470
NET ASSETS, BEGINNING OF YEAR	<u>4,045,846</u>	<u>130,330</u>	<u>4,176,176</u>
NET ASSETS, END OF YEAR	<u>\$ 4,775,919</u>	<u>\$ 109,727</u>	<u>\$ 4,885,646</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF ACTIVITIES

For the Year Ended June 30, 2015

	Unrestricted	Temporarily Restricted	Total
REVENUES			
Federal and government grants	\$ 20,931,913	\$ -	\$ 20,931,913
Parent fees	499,388	-	499,388
Other grants	297,337	133,600	430,937
Contributions	242,600	75,000	317,600
Other revenue	34,851	-	34,851
In-kind contributions	34,590	-	34,590
United Way	19,500	-	19,500
Investment loss	(14,203)	-	(14,203)
Net assets released from restrictions	117,500	(117,500)	-
	22,163,476	91,100	22,254,576
EXPENSES			
Program services	19,925,746	-	19,925,746
General and administrative	2,042,112	-	2,042,112
Fund-raising	159,299	-	159,299
	22,127,157	-	22,127,157
CHANGE IN NET ASSETS	36,319	91,100	127,419
NET ASSETS, BEGINNING OF YEAR	4,009,527	39,230	4,048,757
NET ASSETS, END OF YEAR	\$ 4,045,846	\$ 130,330	\$ 4,176,176

The Notes to Consolidated Financial Statements are an integral part of these statements.

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

For the Year Ended June 30, 2016

	Program Services						Total	General and Administrative	Fundraising	Total
	Family and Community Services	Early Childcare and Education Services	Child Care	Nutrition	Program Services					
Personnel expense	\$ 6,486,912	\$ 2,542,772	\$ 241,098	\$ 23,845	\$ 9,294,627	\$ 858,910	\$ 184,755	\$ 10,338,292		
Payments to subrecipients and providers	-	5,327,394	-	-	5,327,394	-	-	5,327,394		
Professional and outside services	1,466,938	477,738	4,279	423	1,949,378	371,208	6,552	2,327,138		
Employee-related expenses	1,139,846	434,541	43,184	4,271	1,621,842	118,553	25,908	1,766,303		
Materials and supplies	346,133	924,145	46,676	317	1,317,271	99,427	34,208	1,450,906		
Other operating expenses	377,246	164,670	44,359	3,782	590,057	568,381	26,899	1,185,337		
Occupancy costs	313,988	165,196	33,152	3,232	515,568	187,226	27,877	730,671		
Travel and related	457,692	140,523	-	-	598,215	32,237	1,544	631,996		
Equipment	106,780	31,134	175	17	138,106	38,777	1,739	178,622		
Assistance to individuals	13,798	-	-	-	13,798	-	-	13,798		
Totals	\$ 10,709,333	\$ 10,208,113	\$ 412,923	\$ 35,887	\$ 21,366,256	\$ 2,274,719	\$ 309,482	\$ 23,950,457		

The Notes to Consolidated Financial Statements are an integral part of these statements.

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

For the Year Ended June 30, 2015

	Program Services							Total	General and Administrative	Fundraising	Total	
	Family and Community Services		Early Childcare and Education Services		Child Care		Nutrition					Program Services
Personnel expense	\$ 6,675,323	\$ 2,321,289	\$ 246,145	\$ 24,344	\$ 9,267,101	\$ 843,044	\$ 62,559	\$ 10,172,704				
Payments to subrecipients and providers	-	5,160,363	-	-	5,160,363	-	-	5,160,363				
Employee related expenses	1,225,208	417,751	36,103	3,571	1,682,633	135,786	7,335	1,825,754				
Professional and outside services	855,209	105,463	3,842	380	964,894	232,782	9,556	1,207,232				
Materials and supplies	331,963	621,571	46,481	36	1,000,051	121,091	14,208	1,135,350				
Other operating expenses	343,216	137,653	41,262	3,722	525,853	431,093	37,655	994,601				
Occupancy costs	335,072	170,707	31,949	3,159	540,887	200,970	22,498	764,355				
Travel and related	471,780	129,308	2,581	255	603,924	30,118	613	634,655				
Equipment	124,698	43,656	59	6	168,419	47,227	4,875	220,521				
Assistance to individuals	11,621	-	-	-	11,621	-	-	11,621				
Totals	\$ 10,374,091	\$ 9,107,761	\$ 408,422	\$ 35,473	\$ 19,925,747	\$ 2,042,111	\$ 159,299	\$ 22,127,157				

The Notes to Consolidated Financial Statements are an integral part of these statements.

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Years Ended June 30, 2016 and 2015

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ 709,470	\$ 127,419
Adjustments to reconcile change in net assets to net cash from operating activities		
Depreciation	176,044	189,325
Net realized and unrealized (gains) losses on investments	18,351	27,324
Reinvested interest and dividend income	(15,642)	(19,167)
Release of deferred grant obligation	(24,144)	(24,144)
Changes in operating assets and liabilities		
Grants and accounts receivable	(3,904)	180,646
Prepaid expenses	(26,384)	11,487
Other assets	-	(500)
Deposits	(5,627)	-
Accounts payable	57,582	15,615
Accrued expenses and other liabilities	(38,842)	(30,172)
Net cash provided by operating activities	846,904	477,833
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(70,207)	(87,566)
Purchases of investments	(52,226)	(504,604)
Proceeds from sales maturities of investments	59,972	497,455
Net cash used by investing activities	(62,461)	(94,715)

(continued)

The Notes to Consolidated Financial Statements are an integral part of these statements.

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

For the Years Ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment on lines of credit, net	(574,125)	(45,601)
Principal payments on capital leases	(10,478)	(9,482)
Principal payments on notes payables	(26,654)	(25,457)
	<u>(611,257)</u>	<u>(80,540)</u>
Net cash used by financing activities		
Net increase in cash and cash equivalents	173,186	302,578
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>705,272</u>	<u>402,694</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 878,458</u>	<u>\$ 705,272</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid during the year for interest	<u>\$ 57,611</u>	<u>\$ 68,290</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2016 and 2015

1. ORGANIZATION

Nature of Operations

Child & Family Resources, Inc. (“CFR”) was incorporated in Arizona in August 1970 as a private nonprofit, community-based organization whose goal is to promote strength and stability of families, to afford children and youth a supportive environment and to maximize the child’s physical, intellectual and emotional development. CFR documents community needs, develops innovative solutions and programs to resolve unmet needs and implements programs where there are no available resources. The mission of CFR is to enhance the quality of life for children and their families. CFR operates primarily in southern Arizona with offices in Tucson, Phoenix, Sierra Vista, Douglas, Nogales, Yuma, Stafford, Kingman, Casa Grande, Bullhead City and Apache Junction.

In March 2006, Child & Family Resources, Inc. entered an affiliation agreement with Tucson Nursery Schools and Child Care Centers, Inc. (“TNS”), which provides low cost child care for low-income working families, in order to further Child & Family Resources, Inc.’s mission. TNS is a nonprofit corporation organized to operate exclusively for education, scientific, literary and charitable purposes. The agreement required each organization to complete certain administrative and legal steps in order to complete the formal affiliation. Under the affiliation agreement, CFR has the authority to elect the directors of the Board of TNS. In July 2006, Child & Family Resources, Inc. completed all steps of the agreement and became the sole member of TNS.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of Child & Family Resources, Inc. and its commonly controlled subsidiary, Tucson Nursery Schools and Child Care Centers, Inc. (collectively referred to as the “Organization”). All intercompany accounts and transactions have been eliminated in consolidation.

Basis of Accounting

The Organization follows accounting standards set by the Financial Accounting Standards Board (“FASB”). The FASB sets the United States’ generally accepted accounting principles (“GAAP”), which are followed by the Organization in order to ensure the consistent reporting of its financial position, changes in net assets, and cash flows. The consolidated financial statements of the Organization have been prepared on the accrual basis of accounting and accordingly, reflect all significant receivables, payables, and other liabilities.

(continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Consolidated Financial Statement Presentation

The Organization reports information regarding its consolidated financial position and activities according to the presence or absence of donor-imposed restrictions, which are segregated into the following categories:

Unrestricted net assets – Net assets which are not subject to donor-imposed stipulations. A portion of the unrestricted net assets have been designated by the board of directors as expended for property and equipment to reflect the total carrying value after accumulated depreciation of all property and equipment, net of directly related liabilities. The board of directors has also designated \$60,000 to help fund the Youth Empowerment for Success program. Remaining unrestricted net assets are available for general operations of the Organization.

Temporarily restricted net assets – Net assets which are subject to donor-imposed stipulations that may or will be met by actions of the Organization and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions. Temporarily restricted net assets are \$109,727 and \$130,330 at June 30, 2016 and 2015, respectively.

Permanently restricted net assets – Net assets that are subject to donor-imposed stipulations that they be maintained permanently by the Organization. Generally, the donors of these assets permit the Organization to use all or part of the income earned on any related investments for general or specific purposes. No permanently restricted net assets existed at June 30, 2016 and 2015.

Donated Services, Materials and Facilities

Donated materials and facilities are valued at their fair market value. Donated services are recognized in the consolidated financial statements at their fair market value if the services require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not donated.

Although the Organization utilizes the services of many outside volunteers, the fair value of these services is not recognized in the accompanying consolidated financial statements since they do not meet the criteria for recognition under accounting principles generally accepted in the United States of America.

Use of Estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of support, revenue and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

(continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Functional Allocation of Expenses

The costs of providing the various programs have been summarized on a functional basis in the consolidated statement of activities. Expenses that can be identified with a specific program are allocated directly according to their natural classification. Other expenses that are common to several functions are allocated by other reasonable methods.

Advertising

The Organization uses advertising to promote its programs. Advertising costs are expensed as incurred. The total amounts of advertising expensed were \$79,654 and \$76,301 for the years ended June 30, 2016 and 2015, respectively.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, available funds on deposit at financial institutions, and highly liquid investments with a maturity of three months or less when purchased.

Grants and Accounts Receivable

The Organization grants unsecured credit under contracts primarily with governmental agencies in Arizona. The Organization considers accounts over 30 days past due to be delinquent. At June 30, 2016 and 2015, the balance of grants and accounts receivable included \$316,699 and \$616,134, respectively, of amounts over 30 days past due. Management provides for probable uncollectible amounts through a provision for bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. At June 30, 2016 and 2015, the allowance for doubtful accounts was \$10,000 and \$0, respectively.

Investments

In accordance with accounting principles generally accepted in the United States of America applicable to nonprofit organizations, investments in marketable securities with readily determinable fair values and all investments in debt securities are valued at their fair values in the consolidated statement of financial position. Unrealized gains and losses are included with the change in net assets.

(continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property and Equipment

Purchased property and equipment is recorded at cost. Donations of property and equipment are recorded as support at estimated fair value. Such donations are reported as unrestricted support unless the donor has restricted the donated assets to a specific purpose. Assets donated with explicit restrictions regarding their use and contributions of cash that must be used to acquire property and equipment are reported as restricted support. Absent donor stipulations regarding how long those donated assets must be maintained, the Organization reports expirations of donor restrictions when the donated or acquired assets are placed in service as instructed by the donor. The Organization reclassifies temporarily restricted net assets to unrestricted net assets at that time.

The cost of repairs and maintenance is charged to expense in the year incurred. Expenditures that increase the useful lives of the assets are capitalized and depreciated. The Organization's policy is to capitalize expenditures for property and equipment that exceed \$5,000. Property and equipment is depreciated using the straight-line method over the following estimated useful lives of the assets:

Buildings and improvements	10 to 40 years
Furniture and equipment	3 to 15 years
Leasehold Improvements	10 years
Vehicles	5 years

Total depreciation and amortization expense was \$176,044 and \$189,325 for the years ended June 30, 2016 and 2015, respectively.

Income Taxes

CFR and TNS are nonprofit organizations exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code and from Arizona income tax under Arizona Revised Statute Section 43-1201(4). CFR and TNS are also public charities under the Internal Revenue Code Section 509(a)(1). This classification allows for donations to both organizations to be deductible as charitable contributions on income tax returns. There were no income taxes paid during the years ended June 30, 2016 and 2015.

Both CFR and TNS have a policy to disclose or recognize income tax positions based on management's estimate of whether it is reasonably possible or probable, respectively, that a liability has been incurred for unrecognized income tax positions. As of June 30, 2016, management is not aware of any uncertain tax positions that are potentially material. In addition, management is not aware of any matters which would cause CFR or TNS to lose their tax-exempt status. Income tax related interest and penalties, if any, are reported in general and administrative expenses when incurred. The accompanying consolidated financial statements do not include any interest or penalties related to income taxes. No income tax examinations are currently underway or anticipated. The statute of limitations is three years for federal income tax purposes and four years for the State of Arizona. All prior year returns have been timely filed.

(continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The Organization is annually required to file a Return of Organization Exempt from Income Tax (Form 990) with the IRS. In addition, the Organization is subject to income tax on net income that is derived from business activities that are unrelated to their exempt purposes. The Organization has determined that it is not subject to unrelated business income tax for the years ended June 30, 2016 and 2015.

Comparative Information

Certain reclassifications have been made to the June 30, 2015 consolidated financial statements in order to conform to the June 30, 2016 presentation. Such reclassifications did not represent a change in accounting principles and had no effect on the reported change in net assets.

Recent Accounting Pronouncements

- Revenue Recognition

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (Topic 606), which will supersede the current revenue recognition requirements in Topic 605, Revenue Recognition. The ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The ASU also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The new guidance will be effective for the Organization's year ending June 30, 2019. The ASU permits application of the new revenue recognition guidance to be applied using one of two retrospective application methods. The Organization has not yet determined which application method it will use or the potential effects on the new standard on the consolidated financial statements, if any.

- Leases

In February 2016, the Financial Accounting Standards Board issued ASU No. 2016-02, Leases (Topic 842), which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either financing or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital lease obligations recognized on the consolidated balance sheet. Lessor accounting under the new standard will remain similar to lessor accounting under current GAAP. The reporting of lease-related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the Organization's year ending June 30, 2020 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The effect of applying the new lease guidance on the consolidated financial statements has not yet been determined.

(continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

• Non-Profit Organizations

In August 2016, The Financial Accounting Standards Board issued ASU 2016-14, Not-for-Profit Entities (Topic 958), which will change how not-for-profit organizations will report and present certain items in their financial statements. The new guidance will take effect for the year ending June 30, 2019. The significant changes are:

- Simplification of net asset presentation – net assets will now be presented in two classes, “Net assets with donor restrictions,” and “Net assets without donor restrictions.”
- All not-for-profit organizations will be required to present expenses in their natural classification (advertising, payroll, rent, etc.) and by function (program, general and administrative, and fund raising).
- Enhanced disclosure requirements related to presenting liquidity information, and simplification of existing disclosure requirements related to investment returns and long lived assets purchased with donor-restricted funds.

The Organization has not yet determined the effect of applying the new standard on the consolidated financial statements.

3. CONCENTRATION OF RISK

The Federal Deposit Insurance Corporation (FDIC) insures cash accounts at banks up to \$250,000 per institution. Investments held by other institutions are covered up to \$500,000 under insurance provided by the Securities Investor Protection Corporation (SIPC). However, SIPC does not protect against losses in market value. The Organization’s investments are on deposit at a brokerage institution that provides additional insurance above SIPC limits. At June 30, 2016 and 2015, the Organization had \$613,659 and \$118,968 of cash and investments in excess of FDIC and SIPC limitations.

(continued)

4. GRANTS AND ACCOUNTS RECEIVABLE

Grants and accounts receivable consist of the following at June 30:

	<u>2016</u>	<u>2015</u>
Arizona Department of Economic Security and Arizona Department of Child Safety	\$ 1,494,954	\$ 1,463,456
Arizona First Things First	783,897	807,399
Arizona Department of Education	495,903	588,402
Other governmental agencies	217,944	173,356
Other receivables	<u>177,771</u>	<u>123,952</u>
Total grants and accounts receivable	3,170,469	3,156,565
Less: allowance for doubtful accounts	<u>(10,000)</u>	<u>-</u>
Total grants and accounts receivable, net	<u>\$ 3,160,469</u>	<u>\$ 3,156,565</u>

5. INVESTMENTS

Investments are stated at fair value and consist of the following as of June 30:

	<u>2016</u>	<u>2015</u>
Mutual Funds:		
Large value	\$ 110,456	\$ 110,370
Large blend	48,725	110,759
Large growth	111,901	110,396
Small growth	30,866	34,780
Small value	32,203	33,749
Diversified emerging markets	48,786	-
Government securities	124,506	137,013
Corporate bonds	<u>89,476</u>	<u>70,307</u>
Total investments	<u>\$ 596,919</u>	<u>\$ 607,374</u>

Investment (loss) income consists of the following for the years ended June 30:

	<u>2016</u>	<u>2015</u>
Interest and dividend income	\$ 15,642	\$ 19,167
Realized and unrealized (loss) gain, net	(18,351)	(27,324)
Investment fees	<u>(2,616)</u>	<u>(6,046)</u>
Total investment loss, net	<u>\$ (5,325)</u>	<u>\$ (14,203)</u>

(continued)

6. FAIR VALUE MEASUREMENTS

U.S. generally accepted accounting principles establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. This hierarchy consists of three broad levels: Level 1 inputs consists of unadjusted quoted prices in active markets for identical assets and have the highest priority, Level 2 inputs consist of observable inputs other than quoted prices for identical assets, and Level 3 inputs have the lowest priority. The Organization uses appropriate valuation techniques based on the available inputs to measure the fair value of its investments. When available, the Organization measures fair values using Level 1 input because they generally provide the most reliable evidence of fair value.

Level 1 Fair Value Measurements are based on quoted prices (unadjusted) in active markets for identical assets that the reporting entity has the ability to access at the measurement date. An active market for the assets is a market in which transactions for the asset occur with sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 Fair Value Measurements are based on inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. If the asset has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset.

Level 3 Fair Value Measurements are based on unobservable inputs for the asset. Unobservable inputs shall be used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the assets at the measurement date. However, the fair value measurement objective remains the same, that is, an exit price from the perspective of a market participant that holds the asset. Therefore, unobservable inputs shall reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing the asset (including assumption about risk). Unobservable inputs shall be developed based on the best information available in the circumstances, which might include the reporting entity's own data.

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, 2016 and 2015.

Stocks, Bonds, Mutual Funds: Valued at the closing price reported on the active market on which the individual securities are traded.

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

(continued)

6. FAIR VALUE MEASUREMENTS (continued)

Fair values of Level 1 investment assets measured on a recurring basis at June 30, are:

	<u>2016</u>	<u>2015</u>
Mutual Funds:		
Large value	\$ 110,456	\$ 110,370
Large blend	48,725	110,759
Large growth	111,901	110,396
Small growth	30,866	34,780
Small value	32,203	33,749
Diversified emerging markets	48,786	-
Government securities	124,506	137,013
Corporate bonds	<u>89,476</u>	<u>70,307</u>
Total investments	<u>\$ 596,919</u>	<u>\$ 607,374</u>

7. PROPERTY AND EQUIPMENT

Property and equipment and related accumulated depreciation at June 30, 2016 and 2015 consist of the following:

	<u>2016</u>	<u>2015</u>
Land	\$ 457,499	\$ 455,464
Buildings and improvements	3,656,740	3,706,049
Furniture and equipment	1,775,529	1,658,047
Leasehold improvements	194,801	194,801
Vehicles	<u>25,617</u>	<u>25,617</u>
Total	6,110,186	6,039,978
Less accumulated depreciation	<u>(3,384,266)</u>	<u>(3,208,221)</u>
Net property and equipment	<u>\$ 2,725,920</u>	<u>\$ 2,831,757</u>

(continued)

8. LINES OF CREDIT

CFR has a revolving line of credit with Wells Fargo Bank, which matures December 20, 2016. Interest is payable monthly at the prime rate of interest (3.25% at June 30, 2016 and 2015). If CFR defaults on any terms of the line of credit, the interest rate increases to the prime rate plus 4%. The line of credit is primarily collateralized by a deed of trust. The outstanding balance at June 30, 2016 and 2015 was \$321,492 and \$676,492, respectively. Under the terms of this agreement, CFR is required to maintain a debt coverage ratio of at least 1.25:1. At June 30, 2016 and 2015, CFR was in compliance with the debt coverage ratio.

CFR has a portfolio loan account with Morgan Stanley Bank, N.A., which is collateralized by investments held by Morgan Stanley. Interest is payable monthly at 3.65%. The outstanding balance at June 30, 2016 and 2015 was \$0 and \$220,000, respectively.

TNS has a \$25,000 line of credit with Compass Bank. This line of credit requires interest payments on the outstanding balance at a variable annual interest rate which was 5.75% at June 30, 2016 and 2015. The outstanding balance at June 30, 2016 and 2015 was \$23,106 and \$22,231, respectively.

9. NOTE PAYABLE

The note payable consists of the following at June 30:

	<u>2016</u>	<u>2015</u>
CFR note payable, due in monthly installments of \$3,907 through April 2029, including interest at 4.75%, collateralized by a deed of trust on real property.	\$ 404,353	\$ 431,007
Less current portion	<u>(26,994)</u>	<u>(27,011)</u>
Non-current portion	<u>\$ 377,359</u>	<u>\$ 403,996</u>

Principal maturities of the note payable are as follows at June 30, 2016:

2017	\$ 26,994
2018	28,304
2019	29,678
2020	31,119
2021	32,630
Thereafter	<u>255,628</u>
	<u>\$ 404,353</u>

(continued)

10. CAPITAL LEASE PAYABLE

CFR is obligated under a capital lease through July 2016. At June 30, 2016 and 2015, the total cost of office equipment under the lease is \$76,296 and accumulated depreciation is \$39,511 and \$30,771, respectively.

The capital lease payable consists of the following at June 30:

	<u>2016</u>	<u>2015</u>
CFR capital lease, Bank of the West, \$929 per month including interest; collateralized by office equipment	\$ <u>305</u>	\$ <u>10,783</u>
Net minimum lease payments	305	10,783
Capital lease payable, current portion	<u>(305)</u>	<u>(10,478)</u>
Capital lease payable, non-current portion	<u>\$ -</u>	<u>\$ 305</u>

11. DEFERRED GRANT OBLIGATION

During the year ended June 30, 2013, Angel Charity of Tucson, Inc. (Angel Charity) made a pledge to TNS in the amount of \$241,441. The proceeds of the pledge are to be used to discharge the existing loan secured by the deed of trust on the land and buildings owned by TNS. In accordance with the terms of the agreement, TNS executed a nonrecourse, non-interest bearing promissory note in favor of Angel Charity during the year ended June 30, 2014. The note provides that, on the condition TNS continues to utilize the facility to provide children and youth programs, Angel Charity will forgive the note at a rate of \$24,144 per year over a ten year period beginning with the year ended June 30, 2014. The outstanding balance on the deferred grant obligation is \$169,009 and \$193,153 as of June 30, 2016 and 2015, respectively.

Future maturities of the deferred grant obligation at June 30, 2016 are:

2017	\$ 24,144
2018	24,144
2019	24,144
2020	24,144
2021	24,144
Thereafter	<u>48,289</u>
Total deferred grant obligation	169,009
Less: deferred grant obligation, current portion	<u>(24,144)</u>
Deferred grant obligation, non-current portion	<u>\$ 144,865</u>

(continued)

12. OPERATING LEASES

CFR has 11 facility and 10 office equipment leases for their programs and administrative offices under non-cancelable, long-term operating leases with various expirations through December 2020. Two of the leases contain a one-year renewal. All of the facility leases allow cancellation with 30 to 90 days' notice if CFR can prove loss of grant funding for programs operated out of those locations. During the years ended June 30, 2016 and 2015, total rent and usage expense under these agreements was \$409,066 and \$420,862, respectively.

Future minimum lease payments under these leases are as follows for the years ending June 30:

2017	\$ 243,596
2018	159,959
2019	155,036
2020	91,676
Thereafter	<u>15,367</u>
	<u>\$ 665,634</u>

CFR has two sublease agreements to rent out a portion of its facilities. Total sublease income during the years ended June 30, 2016 and 2015 was \$26,820 and \$32,675, respectively.

13. PENSION PLAN

The Organization maintains a defined contribution pension plan (the "Plan"). The plan allows eligible employees to contribute a portion of their wages on a pretax basis into the plan. The plan also allows for discretionary matching and/or profit sharing contributions by CFR. The Organization's contributions under the plan totaled \$75,018 and \$65,832 for the years ended June 30, 2016 and 2015, respectively.

(continued)

14. CONTRACTS WITH GOVERNMENTAL AGENCIES

Revenue from contracts with governmental agencies consists of the following for the years ended June 30:

	<u>2016</u>	<u>2015</u>
Arizona Department of Economic Security and Arizona Department of Child Safety	\$ 8,666,338	\$ 7,187,882
Arizona Department of Education	6,091,688	5,895,737
Arizona First Things First	2,080,802	3,263,107
United Way First Things First	2,787,527	2,715,785
Arizona Department of Health Services	1,288,281	1,365,493
U.S. Department of Health and Human Services	1,522,692	399,663
Pima County	40,101	57,482
Other Government Contracts	<u>160,220</u>	<u>46,764</u>
Total contracts with governmental agencies	<u>\$ 22,637,649</u>	<u>\$ 20,931,913</u>

15. COMMITMENTS AND CONTINGENCIES

The Organization participates in a number of federal, state and local grant programs. A significant reduction in the level of this support, if it were to occur, would have a material effect on the programs and activities of the Organization. The governmental funding is subject to compliance audits by the respective governmental agencies. Assessments from such audits, if any, are recorded when the amounts of such assessments are reasonably determinable. Some of the governmental contracts are also subject to termination for convenience clauses. The Organization has received no such termination notices.

16. SUBSEQUENT EVENTS

In December 2016, the Child & Family Resources Board of Directors resolved to move all programs currently offered by its subsidiary organization, Tucson Nursery School, into CFR and operate them as all other CFR programs.

Management evaluated subsequent events through December 16, 2016, which is the date on which the consolidated financial statements were available to be issued, and noted no material subsequent events that required recognition or additional disclosure in these consolidated financial statements.

SUPPLEMENTARY INFORMATION

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATING STATEMENTS OF FINANCIAL POSITION

June 30, 2016

ASSETS

	CFR	TNS	Eliminations	Consolidated Total
CURRENT ASSETS				
Cash and cash equivalents	\$ 856,109	\$ 22,349	\$ -	\$ 878,458
Grants and accounts receivable, net	3,129,846	30,623	-	3,160,469
Investments	596,919	-	-	596,919
Notes receivable, related party	100,530	-	(100,530)	-
Prepaid expenses	81,140	-	-	81,140
Total current assets	4,764,544	52,972	(100,530)	4,716,986
PROPERTY AND EQUIPMENT, NET	2,323,315	402,605	-	2,725,920
OTHER ASSETS				
Deposits	53,778	-	-	53,778
Total assets	<u>\$ 7,141,637</u>	<u>\$ 455,577</u>	<u>\$ (100,530)</u>	<u>\$ 7,496,684</u>

See Independent Auditor's Report

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATING STATEMENTS OF FINANCIAL POSITION

June 30, 2016

LIABILITIES AND NET ASSETS

	CFR	TNS	Eliminations	Consolidated Total
CURRENT LIABILITIES				
Accounts payable	\$ 1,050,054	\$ 9,441	\$ -	\$ 1,059,495
Accrued expenses and other liabilities	583,463	17,324		600,787
Note payable, related party	-	100,530	(100,530)	-
Deferred revenues	32,491	-	-	32,491
Lines of credit	321,492	23,106	-	344,598
Current portion of capital leases	305	-	-	305
Current portion of deferred grant obligation	-	24,144	-	24,144
Current portion of long-term debt	26,994	-	-	26,994
	<u>2,014,799</u>	<u>174,545</u>	<u>(100,530)</u>	<u>2,088,814</u>
LONG-TERM LIABILITIES				
Long-term portion of deferred grant obligation	-	144,865	-	144,865
Long-term debt	377,359	-	-	377,359
	<u>2,392,158</u>	<u>319,410</u>	<u>(100,530)</u>	<u>2,611,038</u>
NET ASSETS				
Unrestricted				
General operating	2,660,790	(266,438)	-	2,394,352
Investment in capital assets	1,918,962	402,605	-	2,321,567
Board designated	60,000	-	-	60,000
Temporarily restricted	109,727	-	-	109,727
	<u>4,749,479</u>	<u>136,167</u>	<u>-</u>	<u>4,885,646</u>
Total liabilities and net assets	<u>\$ 7,141,637</u>	<u>\$ 455,577</u>	<u>\$ (100,530)</u>	<u>\$ 7,496,684</u>

See Independent Auditor's Report

CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATING STATEMENTS OF FINANCIAL POSITION

June 30, 2015

ASSETS

	CFR	TNS	Eliminations	Consolidated Total
CURRENT ASSETS				
Cash and cash equivalents	\$ 684,815	\$ 20,457	\$ -	\$ 705,272
Grants and accounts receivable, net	3,128,181	28,384	-	3,156,565
Investments	607,374	-	-	607,374
Notes receivable, related party	102,000	-	(102,000)	-
Prepaid expenses	54,756	-	-	54,756
Total current assets	4,577,126	48,841	(102,000)	4,523,967
PROPERTY AND EQUIPMENT, NET	2,408,806	422,951	-	2,831,757
OTHER ASSETS				
Deposits	48,151	-	-	48,151
Total assets	\$ 7,034,083	\$ 471,792	\$ (102,000)	\$ 7,403,875

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CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY
CONSOLIDATING STATEMENTS OF FINANCIAL POSITION

June 30, 2015

LIABILITIES AND NET ASSETS

	CFR	TNS	Eliminations	Consolidated Total
CURRENT LIABILITIES				
Accounts payable	\$ 993,480	\$ 8,433	\$ -	\$ 1,001,913
Accrued expenses and other liabilities	599,883	15,608	-	615,491
Note payable, related party	-	102,000	(102,000)	-
Deferred revenues	56,629	-	-	56,629
Lines of credit	896,492	22,231	-	918,723
Current portion of capital leases	10,478	-	-	10,478
Current portion of deferred grant obligation	-	24,144	-	24,144
Current portion of long-term debt	27,011	-	-	27,011
	<u>2,583,973</u>	<u>172,416</u>	<u>(102,000)</u>	<u>2,654,389</u>
LONG-TERM LIABILITIES				
Long-term portion capital leases	305	-	-	305
Long-term portion of deferred grant obligation	-	169,009	-	169,009
Long-term debt	403,996	-	-	403,996
	<u>2,988,274</u>	<u>341,425</u>	<u>(102,000)</u>	<u>3,227,699</u>
NET ASSETS				
Unrestricted:				
General operating	1,948,463	(292,584)	-	1,655,879
Investment in capital assets	1,967,016	422,951	-	2,389,967
Temporarily restricted	130,330	-	-	130,330
	<u>4,045,809</u>	<u>130,367</u>	<u>-</u>	<u>4,176,176</u>
Total liabilities and net assets	<u>\$ 7,034,083</u>	<u>\$ 471,792</u>	<u>\$ (102,000)</u>	<u>\$ 7,403,875</u>

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CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY

CONSOLIDATING STATEMENTS OF ACTIVITIES

For the Year Ended June 30, 2016

	CHILD & FAMILY RESOURCES, INC.			TUCSON NURSERY SCHOOLS			Eliminations	Consolidated Total
	Unrestricted	Temporarily Restricted	Total CFR	Unrestricted	Temporarily Restricted	Total TNS		
REVENUES								
Federal and government grants	\$ 22,351,001	\$ -	\$ 22,351,001	\$ 286,648	\$ -	\$ 286,648	\$ -	\$ 22,637,649
Parent fees	392,197	-	392,197	126,380	-	126,380	-	518,577
Other grants	49,725	78,850	128,575	39,282	-	39,282	-	167,857
Contributions	432,670	-	432,670	41,000	-	41,000	-	473,670
Other program revenue	95,515	-	95,515	-	-	-	-	95,515
Other revenue	705,360	-	705,360	4,024	-	4,024	-	709,384
In-kind contributions	41,692	-	41,692	-	-	-	-	41,692
United Way	12,000	-	12,000	8,908	-	8,908	-	20,908
Investment loss	(5,325)	-	(5,325)	-	-	-	-	(5,325)
Net assets released from restrictions	99,453	(99,453)	-	-	-	-	-	-
Total revenues	<u>24,174,288</u>	<u>(20,603)</u>	<u>24,153,685</u>	<u>506,242</u>	<u>-</u>	<u>506,242</u>	<u>-</u>	<u>24,659,927</u>
EXPENSES								
Program services	20,917,446	-	20,917,446	448,810	-	448,810	-	21,366,256
General and administrative	2,223,087	-	2,223,087	51,632	-	51,632	-	2,274,719
Fund-raising	309,482	-	309,482	-	-	-	-	309,482
Total expenses	<u>23,450,015</u>	<u>-</u>	<u>23,450,015</u>	<u>500,442</u>	<u>-</u>	<u>500,442</u>	<u>-</u>	<u>23,950,457</u>
CHANGE IN NET ASSETS	724,273	(20,603)	703,670	5,800	-	5,800	-	709,470
NET ASSETS, BEGINNING OF YEAR	3,915,479	130,330	4,045,809	130,367	-	130,367	-	4,176,176
NET ASSETS, END OF YEAR	<u>\$ 4,639,752</u>	<u>\$ 109,727</u>	<u>\$ 4,749,479</u>	<u>\$ 136,167</u>	<u>\$ -</u>	<u>\$ 136,167</u>	<u>\$ -</u>	<u>\$ 4,885,646</u>

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CHILD & FAMILY RESOURCES, INC. AND SUBSIDIARY

CONSOLIDATING STATEMENTS OF ACTIVITIES

For the Year Ended June 30, 2015

	CHILD & FAMILY RESOURCES, INC.			TUCSON NURSERY SCHOOLS			Consolidated Total
	Unrestricted	Temporarily Restricted	Total CFR	Unrestricted	Temporarily Restricted	Total TNS	
REVENUES							
Federal and government grants	\$ 20,668,447	\$ -	\$ 20,668,447	\$ 263,466	\$ -	\$ 263,466	\$ 20,931,913
Parent fees	365,525	-	365,525	133,863	-	133,863	499,388
Other grants	253,288	133,600	386,888	44,049	-	44,049	430,937
Contributions	215,445	75,000	290,445	27,155	-	27,155	317,600
Other revenue	34,851	-	34,851	-	-	-	34,851
In-kind contributions	34,590	-	34,590	-	-	-	34,590
United Way	12,000	-	12,000	7,500	-	7,500	19,500
Investment loss	(14,203)	-	(14,203)	-	-	-	(14,203)
Net assets released from restrictions	117,500	(117,500)	-	-	-	-	-
Total revenues	21,687,443	91,100	21,778,543	476,033	-	476,033	22,254,576
EXPENSES							
Program services	19,481,851	-	19,481,851	443,895	-	443,895	19,925,746
General and administrative	1,989,316	-	1,989,316	52,796	-	52,796	2,042,112
Fund-raising	159,299	-	159,299	-	-	-	159,299
Total expenses	21,630,466	-	21,630,466	496,691	-	496,691	22,127,157
CHANGE IN NET ASSETS	56,977	91,100	148,077	(20,658)	-	(20,658)	127,419
NET ASSETS, BEGINNING OF YEAR	3,858,502	39,230	3,897,732	151,025	-	151,025	4,048,757
NET ASSETS, END OF YEAR	\$ 3,915,479	\$ 130,330	\$ 4,045,809	\$ 130,367	\$ -	\$ 130,367	\$ 4,176,176

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