

T.E.R.I., INC. & AFFILIATES

CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2017

INDEPENDENT AUDITORS' REPORT

T.E.R.I., INC. & AFFILIATES

June 30, 2017

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KAKU & MERSINO, LLP
CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

Board of Directors
T.E.R.I., Inc. & Affiliates

Report on the Financial Statements

We have audited the accompanying financial statements of T.E.R.I., Inc. & Affiliates (nonprofit organizations), 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.

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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 T.E.R.I., Inc. & Affiliates' as of June 30, 2017, 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 11, 2018, on our consideration of T.E.R.I., Inc. & Affiliates' 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 T.E.R.I., Inc. & Affiliates' internal control over financial reporting and compliance.

Kaku + Mersino, LLP

KAKU & MERSINO, LLP

January 11, 2018

T.E.R.I., INC. & AFFILIATES
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
JUNE 30, 2017

ASSETS

Cash	\$ 1,692,818
Accounts Receivable	1,727,197
Grants Receivable	452,006
Contributions Receivable	309,956
Prepaid Expenses	138,661
Investments	9,826
Client Trust Accounts	87,897
Deposits	158,157
Construction in Progress	5,703,480
Property and Equipment, net	<u>10,763,148</u>
TOTAL ASSETS	<u><u>\$ 21,043,146</u></u>

LIABILITIES

Accounts Payable	\$ 1,215,225
Salaries and Benefits Payable	692,169
Accrued Expenses	773,587
Deferred Revenue	68,667
Line of Credit	725,000
Accrued Interest	104,042
Client Trust Accounts	87,897
Capital Lease	7,505
Notes Payable	<u>2,787,588</u>
TOTAL LIABILITIES	<u>6,461,680</u>

NET ASSETS

Unrestricted	12,733,862
Temporarily Restricted	<u>1,847,604</u>
TOTAL NET ASSETS	<u>14,581,466</u>
TOTAL LIABILITIES AND NET ASSETS	<u><u>\$ 21,043,146</u></u>

The accompanying notes are an integral part of the financial statements.

T.E.R.I., INC. & AFFILIATES
CONSOLIDATED STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2017

	Unrestricted	Temporarily Restricted	Total
REVENUE and SUPPORT			
Program Service Fees			
Residential	\$ 5,611,012		\$ 5,611,012
Adult Day Programs	5,152,625		5,152,625
Non Public Schools	4,135,385		4,135,385
Respite	1,132,807		1,132,807
Rental Income	562,205		562,205
Transportation	564,187		564,187
Total Program Service Fees	17,158,221	-	17,158,221
Public Support			
Contributions	1,207,136	564,321	1,771,457
Grants	166,688		166,688
Total Public Support	1,373,824	564,321	1,938,145
Other Revenue			
Thrift Store Sales \$116,273			
Cost of Sales <u>(36,198)</u>	80,075		80,075
Miscellaneous	539,744		539,744
Loss on Investments	(559)		(559)
Total Other Revenue	619,260	-	619,260
Net assets released from restrictions	187,266	(187,266)	-
TOTAL SUPPORT and REVENUE	19,338,571	377,055	19,715,626
EXPENSES			
Program Services	16,540,553		16,540,553
Supporting Services			
Management and General	2,243,877		2,243,877
Development	632,761		632,761
Total Supporting Services	2,876,638	-	2,876,638
TOTAL EXPENSES	19,417,191	-	19,417,191
INCREASE/(DECREASE) IN NET ASSETS	(78,620)	377,055	298,435
NET ASSETS, BEGINNING OF YEAR	12,812,482	1,470,549	14,283,031
NET ASSETS, END OF YEAR	\$ 12,733,862	\$ 1,847,604	\$ 14,581,466

The accompanying notes are an integral part of the financial statements.

T.E.R.I., INC. & AFFILIATES
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2017

	Program Services						
	Residential	Adult Day Programs	Non Public Schools	Respite	Transportation	TERI Inspired Resale	Equestrian
Salaries	\$ 3,139,093	\$ 3,022,075	\$ 2,634,360	\$ 628,361	\$ 426,416	\$ 64,400	\$ 114,881
Payroll taxes	234,015	216,662	192,549	47,352	32,137	5,666	8,447
Health insurance/Wellness	109,709	280,280	246,120	12,437	5,950	10,886	6,096
Workers compensation	163,666	57,340	50,167	31,181	22,672	3,562	1,872
Client activities	29,036	4,910	2,698	12,175	-	-	-
Vocational service	-	37,536	1,992	-	-	-	-
Vehicle expense	-	-	-	-	369,605	-	-
Information Technology	15,576	25,596	23,499	2,432	20,001	5,187	5,521
Office supplies and expense	4,191	4,980	9,057	648	198	3,241	1,385
Advertising	13,019	12,762	6,362	4,620	1,470	2,969	574
Utilities	71,362	85,855	105,272	7,277	-	3,966	25,898
Interest	-	-	-	-	-	-	-
Dues and subscriptions	1,955	873	6,127	300	30	312	1,168
Insurance	802	2,490	2,408	38	-	3,716	5,165
Depreciation	1,068	2,898	1,478	-	244,554	143	131,625
Rent	205,207	254,105	207,016	16,717	2,250	21,827	-
Unreimbursed Services	-	842	1,542	95	-	163	-
Bank charges	-	-	-	-	-	1,760	-
Business promotion	-	-	-	-	-	-	-
Taxes and licenses	59,614	737	2,825	-	-	-	-
Seminars	-	8,885	628	-	300	-	155
Auto allowance and mileage	40,961	46,435	18,066	85,835	8,280	3,060	1,778
Food	242,060	-	-	-	-	-	-
Household supplies	84,194	6,752	4,212	741	1,437	2,891	6,582
Equipment rental	5,477	23,116	13,634	584	22	2,487	4,874
Outside services	79,943	72,803	162,240	1,186	3,849	3,294	22,806
Program supplies	41,857	131,800	31,942	6,249	1,848	8,657	26,697
Repairs and maintenance	7,973	41,065	40,449	2,556	141	3,427	13,861
Medi-Cal quality assurance fee	291,048	-	-	-	-	-	-
Medications	34,910	-	-	-	-	-	-
	\$ 4,876,736	\$ 4,340,797	\$ 3,764,643	\$ 860,784	\$ 1,141,160	\$ 151,614	\$ 379,385
Percentage	25.1%	22.4%	19.4%	4.4%	5.9%	0.8%	2.0%

The accompanying notes are an integral part of the financial statements.

T.E.R.I., INC. & AFFILIATES
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2017

	Program Services			Supporting Services			Total
	IALQ	HUD Affiliates	Program Services Total	Management and General	Development	Supporting Services Total	
Salaries	\$ 6,790	\$ 219,197	\$ 10,255,573	\$ 1,142,673	\$ 228,024	\$ 1,370,697	\$ 11,626,270
Payroll taxes	489	7,460	744,777	125,880	16,080	141,960	886,737
Health insurance/Wellness	447	10,277	682,202	24,338	12,673	37,011	719,213
Workers compensation	66	6,254	336,780	14,292	1,980	16,272	353,052
Client activities	-	-	48,819	-	-	-	48,819
Vocational service	-	-	39,528	-	-	-	39,528
Vehicle expense	-	-	369,605	-	-	-	369,605
Information Technology	41	15,707	113,560	109,373	10,330	119,703	233,263
Office supplies and expense	-	-	23,700	28,201	8,143	36,344	60,044
Advertising	165	-	41,941	10,605	3,949	14,554	56,495
Utilities	-	203,426	503,056	37,806	2,690	40,496	543,552
Interest	-	-	-	64,820	-	64,820	64,820
Dues and subscriptions	33	4,005	14,803	66,675	6,205	72,880	87,683
Insurance	-	29,199	43,818	46,393	-	46,393	90,211
Depreciation	-	283,050	664,816	1,152	-	1,152	665,968
Rent	1,050	-	708,172	56,358	5,655	62,013	770,185
Unreimbursed Services	-	-	2,642	-	-	-	2,642
Bank charges	-	5,449	7,209	21,802	9,579	31,381	38,590
Business promotion	-	-	-	29,500	989	30,489	30,489
Taxes and licenses	-	8,008	71,184	2,872	-	2,872	74,056
Seminars	-	-	9,968	11,324	4,373	15,697	25,665
Auto allowance and mileage	310	6,548	211,273	77,278	6,747	84,025	295,298
Food	-	-	242,060	-	-	-	242,060
Household supplies	127	27,631	134,567	23,459	945	24,404	158,971
Equipment rental	-	1,363	51,557	23,751	24,203	47,954	99,511
Outside services	5,500	113,228	464,849	264,502	262,663	527,165	992,014
Program supplies	386	3,480	252,916	41,899	26,751	68,650	321,566
Repairs and maintenance	-	65,748	175,220	18,924	782	19,706	194,926
Medi-Cal quality assurance fee	-	-	291,048	-	-	-	291,048
Medications	-	-	34,910	-	-	-	34,910
	<u>\$ 15,404</u>	<u>\$ 1,010,030</u>	<u>\$ 16,540,553</u>	<u>\$ 2,243,877</u>	<u>\$ 632,761</u>	<u>\$ 2,876,638</u>	<u>\$ 19,417,191</u>
Percentage	0.1%	5.2%	85.2%	11.6%	3.3%	14.8%	100.0%

The accompanying notes are an integral part of the financial statements.

T.E.R.I., INC. & AFFILIATES
CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2017

CASH FLOWS FROM OPERATING ACTIVITIES	
Change in Net Assets	\$ 298,435
Adjustments to reconcile change in net assets to net cash from operating activities:	
Depreciation	665,968
Provision for Bad Debts	236,150
Unrealized (Gain)/Loss on Investments	559
(Increase) Decrease in Assets:	
Accounts Receivable	(161,913)
Grants Receivable	(351,055)
Contribution Receivable	170,446
Prepaid Expenses and Other Assets	(62,873)
Deposits	(20,523)
Increase (Decrease) in Liabilities:	
Accounts Payable	925,112
Salaries and Benefits Payable	126,827
Accrued Expenses	434,755
Deferred Revenue	(69,166)
Accrued Interest	7,360
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>2,200,082</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Acquisition of Property and Equipment	(442,900)
Increase Construction in Progress	(96,884)
Change in Investments	(334)
NET CASH USED BY INVESTING ACTIVITIES	<u>(540,118)</u>
CASH FLOWS FROM FINANCING ACTIVITIES	
Advances on Line of Credit	1,045,000
Paydown on Line of Credit	(970,000)
Payments on Capital Lease	(9,006)
Proceeds on New Debt	458,641
Payments on Debt	(776,671)
NET CASH USED BY FINANCING ACTIVITIES	<u>(252,036)</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,407,928
BEGINNING CASH AND CASH EQUIVALENTS	<u>284,890</u>
ENDING CASH AND CASH EQUIVALENTS	<u>\$ 1,692,818</u>

Supplemental Disclosures of Cash Flow Information:

Cash paid during year for interest \$118,565.

Noncash Financing: - Debt of \$278,025 for purchase of vehicles.

The accompanying notes are an integral part of the financial statements.

T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 1 – Nature of Activities

T.E.R.I., Inc. (Training, Education, Research, & Innovation) (the Agency) was incorporated August 21, 1980, as a California nonprofit corporation dedicated to the rehabilitation and therapy of developmentally disabled individuals in San Diego County. The Agency provides residential group homes as intermediate care facilities, operates an adult development center with community based and behavior management programs, two non-public schools, related transportation services and a therapeutic equestrian program, as well as other programs for its clients and their families. In addition, it operates a thrift store and carries out various research and fundraising activities.

Medi-Cal provides partial reimbursement for the operation of the residential group homes, and the State of California provides partial reimbursement for the operation of vocational training, transportation, and respite programs. Local school districts provide partial reimbursement for the operation of educational programs.

Note 2 – Summary of Significant Accounting Policies

Principles of Consolidation

The Agency consolidates related nonprofit corporations in which it has a controlling financial interest. The corporations were established to operate residential facilities to provide individuals with developmental and learning disabilities with housing and services specifically designed to meet their physical, social, and psychological needs and to promote their health, security, happiness and usefulness. The accompanying financial statements reflect the consolidation of the financial statements of the Agency and its affiliates: The Roher Foundation, Ted Williams Housing Corporation, Mitchell Housing Corporation, Martin Housing Corporation, Mara Housing Corporation, Jarred DeZonia Foundation, Wendell Starling Home, McNealy Housing Corporation, Susan Parham Housing Corporation, and Joseph Michalowski Housing Corporation. The affiliate organizations are regulated by the U.S. Department of Housing & Urban Development (HUD) and are nonprofit public benefit corporations exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Service Code. The Roher Foundation is also audited separately as a single audit in accordance with Uniform Guidance as required by HUD.

Basis of Accounting

The financial statements of the Agency are prepared on the accrual basis of accounting and accordingly reflect all significant receivables, payables, and liabilities.

See Independent Auditors' Report

T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 2 – Summary of Significant Accounting Policies (Continued)

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions regarding certain types of assets, liabilities, revenues, and expenses. Accordingly, actual results could differ from those estimates.

Basis of Presentation

The Agency is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Unrestricted net assets are not restricted by donors, or the donor-imposed restrictions have expired. The Agency considers all contributions as available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods, or restricted by the donor for specific purposes are reported as either temporarily restricted or permanently restricted. However, if a restriction is fulfilled in the same time period in which the contribution is received, the Agency reports the contribution as unrestricted.

Temporarily restricted net assets contain donor-imposed restrictions that permit the Agency to use or expend the assets as specified. The restrictions are satisfied by either the passage of time, or by the actions of the Agency.

Permanently restricted net assets contain donor-imposed restrictions that stipulate the resource be maintained permanently, but may or may not permit the Agency to use, or expend part or all of the income derived from the donated assets for either specified or unspecified purposes.

Contributed Volunteer Services

Contributed services throughout the year are not recognized as contributions in the financial statements since there is no provision in the accounting regulations. However, many individuals volunteer time and perform a variety of tasks that assist the Agency.

See Independent Auditors' Report

T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 2 – Summary of Significant Accounting Policies (Continued)

Expense Allocations

The costs of providing various programs and other activities have been summarized on a functional basis in the Statement of Activities and in the Statement of Functional Expenses. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Cash and Cash Equivalents

For the purpose of the Statement of Cash Flows, the Agency considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Investments

Investments in marketable equity securities with readily determinable fair values are stated at fair value. Unrealized gains and losses are included in the change in net assets in the accompanying Statement of Activities.

Accounts and Grants Receivable

Accounts receivable are amounts due from various agencies and entities for services performed under fee for service contracts. Grants receivable are amounts due from federal, state, or local funding sources for services performed under cost reimbursement contracts. Management estimated a provision of \$352,971 for allowance for doubtful accounts which is included in accounts and grants receivable.

Promises to Give

Unconditional promises to give are recognized as revenues or gains in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Conditional promises to give are recognized only when the conditions on which they depend are substantially met and the promise becomes unconditional. Due to the nature of contributions, significant increases and decreases in net assets may occur. These significant fluctuations can arise as contributions are recognized as support in the fiscal period in which they are contributed, but the expense incurred with such contributions occur in a different period. Or, the contributions may be used to purchase property and equipment that is capitalized and depreciated over several periods.

See Independent Auditors' Report

T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 2 – Summary of Significant Accounting Policies (Continued)

Property and Equipment

Property and equipment purchased with Agency funds are capitalized at cost and depreciated over the useful estimated lives of the asset using the straight-line method. Amortization of building improvements is based on the estimated useful life of the improvements. Expenditures for property and equipment in excess of \$5,000 are capitalized.

Contributed property and equipment are recorded at fair value on the date of donation. Contributions of property and equipment are recorded as unrestricted support, unless the donor stipulates how long the assets must be used.

In the unlikely event of a contract termination, certain funding sources require title to property and equipment previously purchased with grant funds revert to the funding source. Certain funding sources also limit the use of property and equipment for specific programs and require approval for disposition of property and equipment from the funding source.

Depreciation is calculated based on the following estimated useful lives:

<u>Type of Asset</u>	<u>Estimated Useful Life</u>
Equipment	4-10 years
Improvements	5-20 years
Buildings - residences	25 years

Deferred Revenue

Unearned grant awards that are determined to be exchange transactions are classified as deferred revenue until expended for the purpose of the grants.

Income Taxes

The Agency is a nonprofit organization defined in Section 501 (c)(3) of the Internal Revenue Code (the "Code") and is, therefore, exempt from federal income taxation under Section 501(a) of the Code. Furthermore, the Agency is exempt from state income taxation under Section 23701d of the California Revenue and Taxation Code. The Agency's returns are subject to examination by federal and state taxing authorities, generally for three and four years, respectively, after they are filed.

Subsequent Events

Management has evaluated subsequent events through January 11, 2018, the date the financial statements were available to be issued.

See Independent Auditors' Report

T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 3 – Cash and Cash Equivalents

Cash and Cash Equivalents consist of the following at June 30, 2017:

	<u>Amount</u>
Cash	\$ 1,559,402
Replacement Reserves	133,416
Total	<u>\$ 1,692,818</u>

The Agency maintains cash balances at two financial institutions located in San Diego, California. The balances are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. The amount in excess of the insured limits at June 30, 2017, total \$1,029,352.

In accordance with applicable regulations, HUD requires the affiliate corporations to maintain a replacement reserve to help fund extraordinary maintenance, repairs, and replacement of capital items. Monthly deposits are required. Use of the replacement reserve account is contingent upon HUD's prior written approval.

Note 4 – Contributions Receivable

Contributions receivable represent promises to give made by donors that are not yet received by the Agency. Contributions that will be received in subsequent years are discounted using a risk-free rate of return. The Agency considers contributions receivable fully collectible. Accordingly, no allowance for uncollectible contributions has been provided.

	<u>Amount</u>
Amount of Receivable due:	
Less than one year	\$ 60,000
One to five years	249,656
More than five years	300
Total	<u>\$ 309,956</u>

Contributions receivable at June 30, 2017, consist primarily of unconditional promises to give from individual donors that are restricted for the construction of the Charles R. Cono Campus of Life (the Campus). The Agency has an ongoing capital campaign to raise funds for the Campus. The Campus will accommodate the Agency's model programs and research and will serve as a diagnostic and training center not only for San Diego, but is anticipated to be accessed worldwide. The Campus will allow the Agency's non-residential programs to relocate to one site and will provide space for future model program development.

See Independent Auditors' Report

T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 5 – Investments – Fair Value Measurements

Fair values measured on a recurring basis at June 30, 2017 are as follows:

	<u>Fair Value</u>	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>
Investment in Equity Securities	<u>\$ 9,826</u>	<u>\$ 9,826</u>

Note 6 – Construction in Progress

The following is a summary of Construction in Progress at June 30, 2017. Interest cost of \$45,795 were capitalized during the fiscal year:

	<u>Amount</u>
Charles R. Cono Campus of Life	\$ 5,703,480
	<hr/>
Total	<u>\$ 5,703,480</u>

Charles R. Cono Campus of Life - In July 2003, the Agency purchased about 20 acres of land for the future site of the Charles R. Cono Campus of Life located in the Twin Oaks Valley area of unincorporated San Diego County, California. The Campus will accommodate the educational, research and therapeutic programs operated by the Agency, including relocation of the adult training and education programs, the Learning Academy, the Country School, and the corporate-sponsored child care programs.

See Independent Auditors' Report

T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 7 – Client Trust Accounts

Client trust funds of \$87,897 at June 30, 2017, represent cash held in a fiduciary capacity for the personal and incidental cost of the residents of the various properties. Accordingly, there is an equivalent liability reported on the statement of financial position as this cash is not available for general Agency use.

Note 8 – Property and Equipment, Net

Property and equipment consist of the following at June 30, 2017:

	<u>Amount</u>
Residences	\$ 6,444,724
Deer Springs Campus	3,180,201
Land	2,010,395
Leasehold Improvements	2,446,706
Vehicles	1,470,701
Equipment	<u>204,700</u>
Total	15,757,427
Less Accumulated Depreciation	<u>(4,994,279)</u>
Property and Equipment, Net	<u>\$ 10,763,148</u>

Depreciation expense was \$665,968 for the year ended June 30, 2017.

Note 9 – Line of Credit

The Agency has a \$1,300,000 line of credit with a financial institution. The line of credit is secured by the Agency's inventory, equipment, accounts receivable, and general intangibles and requires compliance with certain loan covenants. Interest on outstanding borrowings is 4.5% and has a balance of \$725,000 as of June 30, 2017. The line of credit matures on March 15, 2018, which management expects to renew.

See Independent Auditors' Report

T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 10 – Notes Payable

Notes payable consist of the following at June 30, 2017:

	<u>Amount</u>
Promissory note payable to a financial institution in monthly payments of principal and interest of \$18,648. Interest is at 5.162% per annum. The note is due November 22, 2021, and is secured by a first deed of trust.	\$ 877,663
Promissory note payable to a financial institution in monthly payments of principal and interest of \$17,242. Variable interest at 4.27% per annum. The note is due November 10, 2018, and is secured by accounts receivable, equipment and general intangibles.	283,516
Promissory note payable to State of California with interest at 3%. Principal and interest due June 30, 2012, or upon receipt of construction or permanent financing. The note is secured by a deed of trust.	350,000
Note payable to the County of San Diego, Department of Housing and Community Development. The note bears interest at 3% per annum, which shall not be compounded. The principal and accrued interest is deferred until 2042. This note is secured by a deed of trust, subordinate to the deed of trust in favor of HUD. See Capital Advance Note below.	70,000
Note payable to the County of San Diego, Department of Housing and Community Development. The note bears interest at 3% per annum, which shall not be compounded. The principal and accrued interest is deferred until 2042. This note is secured by a deed of trust, subordinate to the deed of trust in favor of HUD. See Capital Advance Note below.	61,831
Note payable to the County of San Diego, Department of Housing and Community Development. The note bears interest at 3% per annum, which shall not be compounded. The principal and accrued interest is deferred until 2041. This note is secured by a deed of trust, subordinate to the deed of trust in favor of HUD. See Capital Advance Note below.	110,313
Note payable held by a lender through Federal Home Loan Bank of San Francisco in the amount of \$40,000. The indebtedness by the note does not bear any interest. The maturity date of the note is December 2028. The deed of trust contains certain provisions for acceleration of the maturity of the note.	40,000
Ten notes payable to a financial institution, payable in monthly installments totaling approximately \$6,500 including interest at 5% per annum, until July 2024. The notes are secured by business assets.	458,641
Twenty three notes payable in monthly payments of interest and principal totaling approximately \$11,000 including interest at rates ranging from 0 to 5.75%. The notes are generally 60 months and are collateralized by vehicles.	<u>535,624</u>
Total	<u>\$ 2,787,588</u>

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T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 10 – Notes Payable (continued)

Current portion of the Line of Credit and Notes Payable is \$1,321,580 for year ending June 30, 2017.

The following is a schedule of future minimum principal payments as of June 30, 2017:

<u>Year Ending June 30:</u>	<u>Amount</u>
2018	\$ 596,580
2019	471,854
2020	370,103
2021	366,137
2022	198,695
Thereafter	<u>784,219</u>
	<u>\$ 2,787,588</u>

Note 11 – Related Party Transactions

TERI rents a residence from a key employee for use as a residential group home. TERI pays \$3,703 per month on a ten-year lease. The amount paid for the year ending June 30, 2017 was \$44,436. TERI has started the process to purchase the home and has paid a \$100,000 deposit which is included in deposits on the statement of financial position.

Note 12 – Commitments and Contingencies

Operating Leases

The Agency has commitments under various operating leases for facilities and equipment used for programs and administrative offices. Property and equipment rental expense incurred under these leases totaled \$869,696 for the year ended June 30, 2017.

Future minimum lease payments under operating lease are as follows:

<u>Year Ending June 30:</u>	
2018	\$ 470,449
2019	254,429
2020	250,154
2021	137,184
2022	93,888

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T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 12 – Commitments and Contingencies (continued)

Capital Leases

The Agency leases an auto under a capital lease. The economic substance of the lease is that the Agency is financing the acquisition of the asset through the lease, and, accordingly, it's recorded in the Agency's assets and liabilities. Property and equipment includes \$40,938 and accumulated depreciation of \$40,938 as of June 30, 2017. Amortization of assets held under capital lease is included in depreciation expense.

Future minimum payments required under the lease are as follows:

Year Ending June 30:

2018	\$	7,505
2019		0
2020		0
2021		0
2022		0

Capital Advance Note

HUD holds Capital Advance Notes on residential real property. The notes bear no interest and are not required to be repaid as long as the housing remains available to eligible disabled persons for 40 years. If the housing becomes unavailable for such purposes, the entire capital advance outstanding and interest since inception would be due and payable. The affiliate corporations have met the requirements during its operating period and intend to continue to meet these requirements for the remaining term of the loan. Accordingly, the Capital Advance Note proceeds were previously recorded as grant revenue and are classified as unrestricted net assets. The Capital Advance Notes are secured by deeds of trust on the affiliate corporation's real property. The Capital Advance Notes are as follows:

The Roher Foundation	\$ 710,200
Ted Williams Housing Corporation	372,500
Mitchell Housing Corporation	380,600
Martin Housing Corporation	380,600
Mara Housing Corporation	386,900
Jarred DeZonia Foundation	386,900
Wendell Starling Home	518,500
McNealy Housing Corporation	561,700
Susan Parham Housing Corporation	582,993
Joseph Michalowski Housing Corporation	<u>582,900</u>
Total	<u>\$ 4,863,793</u>

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T.E.R.I., INC. & AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2017

Note 12 – Commitments and Contingencies (continued)

Community Development Block Grant Funding

In November 2008 the Joseph Michalowski Housing Corporation entered into an agreement with the City of Carlsbad for Community Development Block Grant (CDBG) funding of \$795,000 for the acquisition of residential property for a group home in Carlsbad to serve persons with autism or developmental disabilities. The term of the note is 20 years. The loan shall be due and payable in full upon 1) the date the property is first sold or transferred, or, 2) upon failure to operate a group home on the property, if it occurs prior to the expiration of the term of the loan. The loan shall be forgivable upon expiration of the term of the loan if the property has been maintained and operated as a group home. The Corporation has met these requirements during its operating period and intends to continue to meet these requirements during the remaining period of the agreement. These funds are included in unrestricted net assets.

Community Development Loan Funding

In November 2009 TERI, Inc. entered into an agreement with the City of Vista for loan funding of \$325,000. The agreement requires the use of funds to improve real property and the real property be used for limited purposes. Interest accrues at 5% per annum. The term of the note is 55 years. The loan shall be due and payable in full upon 1) the date the property is first sold or transferred, or, 2) upon failure to operate a group home on the property, if it occurs prior to the expiration of the term of the loan. The loan shall be forgivable upon expiration of the term of the loan if the property has been maintained and operated as a group home. TERI, Inc. has met these requirements during its operating period and intends to continue to meet these requirements during the remaining period of the agreement. These funds are included in unrestricted net assets.

See Independent Auditors' Report

KAKU & MERSINO, LLP
CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL
OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER
MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Directors
T.E.R.I., Inc. & Affiliates

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 T.E.R.I., Inc. & Affiliates (nonprofit organizations), which comprise the statement of financial position as of June 30, 2017, and the related statements of activities, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated January 11, 2018.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether T.E.R.I., Inc. & Affiliates' 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 organization'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 Organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Kaku + Mersino, LLP

KAKU & MERSINO, LLP

January 11, 2018