

**FAMILY SERVICE OPERATIONS,
INC. AND SUBSIDIARIES**

**CONSOLIDATED FINANCIAL STATEMENTS
AND
SUPPLEMENTARY INFORMATION**

June 30, 2018

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

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INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
Family Service Operations, Inc. and Subsidiaries

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Family Service Operations, Inc. and Subsidiaries (the "Organization"), which comprise the consolidated statement of financial position as of June 30, 2018, and the related consolidated statements of activities, functional expenses and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America 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 auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

INDEPENDENT AUDITORS' REPORT (CONTINUED)

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Organization as of June 30, 2018, 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.

Emphasis of Matter

As discussed in Note B to the consolidated financial statements, the Organization will merge with Center for Family Services, Inc., on January 1, 2019. These financial statements are prepared assuming that the Organization is a going concern.

Other Matters

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying consolidating statements of financial position and activities, and the accompanying schedules of expenditures of federal awards and state financial assistance as required by Title 2 U.S. CFR Part 200, *Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards* and State of New Jersey Circular Letter 15-08-OMB (the "Circular"), *Single Audit Policy for Recipients of Federal Grants, State Grants and State Aid* are presented for purposes of additional analysis and are 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 November 15, 2018, on our consideration of the Organization'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 the Organization's internal control over financial reporting and compliance.

Mercedien, P.C.
Certified Public Accountants

November 15, 2018

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

June 30, 2018

ASSETS

Current assets

Cash and cash equivalents	\$ 338,978
Accounts and grants receivable	477,431
Investments	21,779
Prepaid expenses	38,195
Total current assets	<u>876,383</u>
Investments	346,099
Property and equipment	3,196,511
Total Assets	<u>\$ 4,418,993</u>

LIABILITIES AND NET ASSETS

Current liabilities

Accounts payable and accrued expenses	\$ 327,407
Refundable advances	205,185
Current portion of mortgages payable	178,767
Fair value of interest rate swap agreement	2,710
Total current liabilities	<u>714,069</u>
Mortgages payable	<u>820,659</u>
Total Liabilities	<u>1,534,728</u>

Net Assets

Unrestricted	2,863,757
Temporarily restricted	20,508
Total Net Assets	<u>2,884,265</u>
Total Liabilities and Net Assets	<u>\$ 4,418,993</u>

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF ACTIVITIES

Year Ended June 30, 2018

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Support and revenues				
Government grants	\$ 3,893,595	\$ -	\$ -	\$ 3,893,595
Medicaid fees	1,534,766	-	-	1,534,766
Contributions	251,168	-	-	251,168
Client and third-party fees	260,005	-	-	260,005
Investment return	23,589	-	-	23,589
Miscellaneous	14,587	-	-	14,587
Rent	36,400	-	-	36,400
Net assets released from restrictions	66,424	(66,424)	-	-
Total support and revenues	<u>6,080,534</u>	<u>(66,424)</u>	<u>-</u>	<u>6,014,110</u>
Expenses				
Program services	6,658,079	-	-	6,658,079
Management and general	84,260	-	-	84,260
Fundraising	84,191	-	-	84,191
Total expenses	<u>6,826,530</u>	<u>-</u>	<u>-</u>	<u>6,826,530</u>
Change in net assets from operations	(745,996)	(66,424)	-	(812,420)
Non-operating revenues (expenses)				
Forgiveness of debt- State of NJ	25,000	-	-	25,000
Gain on sale of property and equipment	17,609	-	-	17,609
Net depreciation in fair value of interest rate swap	(29,669)	-	-	(29,669)
Total non-operating revenues (expenses)	<u>12,940</u>	<u>-</u>	<u>-</u>	<u>12,940</u>
Change in net assets	(733,056)	(66,424)	-	(799,480)
Net assets, beginning of year	<u>3,596,813</u>	<u>86,932</u>	<u>-</u>	<u>3,683,745</u>
Net assets, end of year	<u>\$ 2,863,757</u>	<u>\$ 20,508</u>	<u>\$ -</u>	<u>\$ 2,884,265</u>

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES**

Year Ended June 30, 2018

	<u>Program</u>	<u>Management and General</u>	<u>Fundraising</u>	<u>Total</u>
Salaries	\$ 2,702,238	\$ 683,584	\$ 38,500	\$ 3,424,322
Fringe benefits	742,876	231,704	9,705	984,285
Consulting fees	456,239	52,466	9,378	518,083
Travel	43,326	3,271	195	46,792
Occupancy	733,685	136,571	2,018	872,274
Materials and supplies	206,405	24,805	14,801	246,011
Client assistance	434,101	-	-	434,101
Other expenses	100,936	72,594	9,594	183,124
Depreciation	76,852	40,686	-	117,538
Total expenses before management and general	5,496,658	1,245,681	84,191	6,826,530
Allocated management and general	1,161,421	(1,161,421)	-	-
Total expenses	<u>\$ 6,658,079</u>	<u>\$ 84,260</u>	<u>\$ 84,191</u>	<u>\$ 6,826,530</u>

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS

Year Ended June 30, 2018

Cash Flows from Operating Activities	
Change in net assets	\$ (799,480)
Adjustments to reconcile change in net assets to net cash from operating activities:	
Depreciation	117,538
Net gain on sale of investments	(15,621)
Net gain on sale of property and equipment	(17,609)
Forgiveness of debt	(25,000)
Change in fair value of interest rate swap	29,669
Increase (decrease) in cash from	
Accounts and grants receivable	(6,505)
Prepaid expenses	(5,187)
Accounts payable and accrued expenses	19,432
Refundable advances	(187,021)
Net cash from operating activities	<u>(889,784)</u>
Cash Flows from Investing Activities	
Purchase of property and equipment	(34,485)
Proceeds from sale of property and equipment	17,609
Proceeds from sale of investments	323,239
Net cash from investing activities	<u>306,363</u>
Cash Flows from Financing Activities	
Repayment of mortgages payable	(148,211)
Net cash from financing activities	<u>(148,211)</u>
Net change in cash and cash equivalents	(731,632)
Cash and cash equivalents, beginning of year	1,070,610
Cash and cash equivalents, end of year	<u>\$ 338,978</u>
Supplemental Disclosure of Cash Flow Information:	
Cash paid during the year for	
Interest	<u>\$ 34,793</u>
Non-cash investing and financing activities	
Donated rent	<u>\$ 138,620</u>
Forgiveness of debt	<u>\$ 25,000</u>

See notes to the consolidated financial statements.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A. NATURE OF ORGANIZATION

Family Service Operations, Inc. and Subsidiaries (the "Organization") provides services to improve the quality of life for individuals and families in the community. Family Service Operations, Inc. ("FSO") serves as a holding company to manage assets and provide management services to the three subordinate organizations: Family Service Association ("FSA"), Family Service Development, Inc. ("FSD") and Family Service Enterprise, Inc. ("FSE").

Subsidiaries

The following wholly-owned subsidiaries of FSO operate programs as follows:

FSA:

Behavioral Health programming focuses on every individual's healing and recovery journey, partnering with them to achieve their definition of health and well-being. These programs include Outpatient Counseling, First Day Adult Partial Care Program, Children's Partial Care, Rainbow Place and Safe Harbor. FSA offers individual, family and group counseling for people of all ages to develop the coping skills necessary to address life's challenges. First Day provides psychiatric adult partial care services for individuals diagnosed with a severe and persistent mental illness. Children's Partial Care provides structured and intensive group treatment to enable youth who are at risk of psychiatric hospitalization to remain in their homes. Rainbow Place, for children aged 6-12 and Safe Harbor, for adolescents aged 13-17 use evidence based curriculums to encourage youth experiencing emotional and behavioral challenges to make positive changes that will promote their healing and recovery.

Youth and Family Services includes Family Life Center, Parents as Teachers, Teen Center and the Home Electronic Detention System ("HEDS"). The Family Life Center's objective is to decrease the risk of abuse/neglect and eliminate the need for continued involvement with the Division of Child Protection and Permanency through strengthening parenting skills. The Egg Harbor Township High School Teen Center program is to help young people navigate the adolescent years, finish their education, obtain skills leading to employment or continuing their education, graduate healthy, and drug free. Parents as Teachers is an evidence based home visitation program that provides parenting education to pregnant and new mothers through the first 3 years of a child's life. The HEDS program is designed for youth who are court-ordered to electronic monitoring as an alternative to detention.

Community Services includes Inland and the New Day Family Success Centers, Kinship Legal Guardianship and Kinship Wraparound Program. The family success centers are a neighborhood gathering place where residents can go for support, information and services. Kinship Legal Guardianship is responsible in promoting safety, permanency, and enhancing financial assistance for low income kinship caregivers who are raising relatives' children in their home. Kinship Wraparound maintains safe and stable home environments for low income kinship caregivers by providing client assistance funds to purchase needed goods and/or services. FSA's family strengthening and community programs strive to empower individuals and families to successfully meet life's challenges and thrive as secure, stable families.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A. NATURE OF ORGANIZATION (CONTINUED)

Anti-Poverty Services includes Supportive Assistance to Individuals and Families ("SAIF"). FSA's anti-poverty work is focused on assisting individuals who are at the end of their welfare eligibility. FSA provides assistance in building their lives through the provision of intensive case management, financial literacy and employment skills. FSA administers the Supportive Aid to Individuals and Families (SAIF Program) in Atlantic, Cape May, Cumberland, and Salem counties. SAIF works in close partnership with the county welfare authorities to assist individuals who are facing the end of their welfare eligibility.

MultiCultural Training provides up to date cultural competence training to Division of Mental Health and Addictions funded agencies within the seven southern counties of New Jersey. This initiative is designed to educate and train individual practitioners and provider agencies in curriculum that addresses how to better serve mental health clients within therapeutic modalities. FSA simultaneously provides technical assistance to this same audience, consulting and providing suggestions in improving infrastructures to better address culturally and ethnically diverse consumers.

FSD acts exclusively for the benefit of FSA, a 501(c)(3) organization, sharing its mission of improving the quality of life for individuals and families in our community. Through the engagement process, FSD will grow FSA's networking base and further its potential for future cultivation of donors. The activities of FSD include soliciting foundations, corporations and individuals for the purpose of philanthropic support. Under the umbrella of FSD, revenue is generated through fundraising special events. Activities of the corporation are reinvested for future use by FSA or distributed to FSA to be used in furtherance of its exempt purpose. FSD also has oversight and responsibility for public relations, marketing, and volunteer functions of the organization thereby expanding FSA's community outreach by increasing its visibility and brand.

FSE's sole purpose is to provide creative and innovative programming that is self-sustaining. The programming of FSE will benefit the emerging needs of the community. A function of FSE is the agency's Employee Assistance Program, which provides brief counseling to employees with alcoholism, drug abuse and personal problems.

Effective January 1, 2019, FSA will merge into Center for Family Services, Inc. ("CFS"). FSO, FSD, and FSE's names will be changed and these entities will become subsidiaries of CFS, with CFS being a sole member. See Note B.

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of FSO, FSA, FSD and FSE. All significant intercompany accounts and transactions have been eliminated in consolidation.

Basis of Presentation

The consolidated financial statements of the Organization have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). Net assets and revenues, gains and losses are classified based on the existence or absence of donor-imposed restrictions.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Basis of Presentation (Continued)

The Organization is required to report information regarding its financial position and activities according to three classes of net assets:

- Unrestricted net assets - net assets not subject to donor-imposed stipulations, and therefore are expendable for operating purposes.
- Temporarily restricted net assets - net assets subject to donor-imposed stipulations that will be met by actions of the Organization and/or by the passage of time.
- Permanently restricted net assets - net assets 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 related investments for general or donor-specified purposes. The Organization has no permanently restricted net assets.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Cash and Cash Equivalents

The Organization considers cash equivalents to be all highly liquid debt instruments with an initial maturity of ninety days or less. Cash and cash equivalents consist mainly of cash, sweep accounts and money market funds.

Accounts and Grants Receivable

Accounts and grants receivable consists primarily of Medicaid fees and grants receivable. The Organization considers all accounts and grants receivable to be fully collectible; accordingly, no allowance for doubtful amounts is required. If amounts become uncollectible, they will be charged to the change in net assets when that determination is made.

Investments

Investments, including certificates of deposit held by a bank, are stated at fair value in the consolidated statement of financial position. Investments in certificates of deposit are classified between current and non-current based on the maturity date of the investment. All interest, dividends and realized and unrealized gains and losses are reported in the statement of activities as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by law.

The estimated fair value amounts have been determined by the Organization using available market information and appropriate valuation methodologies. Considerable judgment is required in interpreting market data to develop the estimates of fair value, and, accordingly, the estimates are not necessarily indicative of the amounts that the Organization could realize in a current market exchange.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property and Equipment

Property and equipment purchased, costing in excess of \$5,000, are capitalized as assets and recorded at cost, except for donated items, which are recorded at the fair value on the date of donation. Depreciation is computed on a straight-line method over the estimated useful lives of the assets as follows:

Buildings	15 to 39 years
Improvements	6 to 40 years
Furniture, equipment and vehicles	5 to 15 years

Repairs and maintenance which do not extend the useful lives of the related assets are expensed as incurred.

Public Support and Revenue Recognition

Contributions are recognized when the donor makes a promise to give to the Organization that is, in substance, unconditional. Unconditional promises to give due in the next year are reflected as current promises to give and are recorded at their net realizable value. Unconditional promises to give due in subsequent years are reflected as long-term promises to give and are recorded at the present value of their net realizable value, using risk-free interest rates applicable to years in which the promises are received to discount the amounts. Conditional promises to give are recognized when the conditions on which they are dependent are substantially satisfied.

Cost reimbursement based federal and state grant awards are classified as refundable advances until expended for the purposes of the grants, since they are considered conditional promises to give.

Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the support is recognized. All other donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets as net assets released from restrictions.

Contributions of donated noncash assets are recorded at their fair values in the period received. Contributions of donated services that create or enhance nonfinancial assets or that require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation, are recorded at their fair values in the period received.

Medicaid, client fees and third-party fees are recognized as services are provided.

Rental income is recognized on a monthly basis on the first of the month for which the service will be provided to the tenant.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income Taxes

FSO, FSA, FSD and FSE are exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and applicable state law. Income generated by activities that would be considered unrelated to the Organization's mission would be subject to tax, which, if incurred, would be recognized as a current expense. No such tax has been recognized by the Organization for the year ended June 30, 2018.

U.S. GAAP requires management to evaluate tax positions taken by the Organization and recognize a tax liability if the Organization has taken an uncertain position that more likely than not would not be sustained upon examination by taxing authorities. Management evaluated the Organization's tax positions and concluded that the Organization had taken no uncertain tax positions that require adjustment to the financial statements to comply with the provisions of this guidance.

The Organization did not record any interest or penalties on uncertain tax positions in the accompanying statement of financial position as of June 30, 2018, or in the accompanying statement of activities for the year then ended. If the Organization were to incur any income tax liability in the future, interest on any income tax liability would be reported as interest expense and penalties on any income tax liability would be reported as income taxes.

Functional Allocation of Expenses

Certain operating expenses have been allocated to program services based on the reasonable benefit that the program derived from these expenses. There are various funding sources providing support towards the Organization's programs and some of the expenses charged to the programs represent direct expenses related to program operations and objectives.

Subsequent Events

Management has evaluated subsequent events for potential recognition and disclosure through November 15, 2018, the date the consolidated financial statements were available to be issued. The item below was determined by management to require disclosure:

Effective January 1, 2019, FSA will merge into CFS. FSO, FSD, and FSE's names will be changed and these entities will become subsidiaries of CFS, with CFS being a sole member. Through the merger, the organizations seek to further their common mission to support and empower individuals, families, and communities to achieve a better life through vision, hope and strength. As of the merger date, CFS will assume all assets and liabilities of FSA, as well as all contracts, leases, bank accounts, debt, property liens, etc. As part of the merger transaction, the current debt will be refinanced.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Recent Accounting Pronouncement

ASU 2016-14, issued in August 2016, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, which now requires net assets to be presented in two classes - net assets with donor restrictions and net assets without donor restrictions. ASU 2016-14 requires the entity to communicate qualitative and quantitative information on how it manages its liquid resources available to meet the cash flow needs for general expenditures within one year of the statement of financial position date, including disclosure of the availability of financial assets at the statement of financial position date, affected by 1) its nature, 2) external limits imposed by donors, grantors, laws and contracts with others, and 3) internal limits imposed by governing board decisions. ASU 2016-14 requires reporting of expenses by both their natural and functional classification. ASU 2016-14 also requires reporting of investment returns net of external and direct internal investment expenses and removes the requirement to disclose the netting of such investment expenses. ASU 2016-14 will be effective for the Organization for the reporting periods beginning after December 15, 2017.

ACCOUNTS AND GRANTS RECEIVABLE

Accounts and grants receivable consist of the following:

Atlantic County	\$ 204,549
Division of Family Development	136,548
Medicaid and third-party fees	101,301
Department of Agriculture	6,684
Miscellaneous receivables	<u>28,349</u>
Total	<u>\$ 477,431</u>

PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

Land	\$ 803,790
Buildings	2,961,013
Improvements	1,676,707
Furniture and fixtures	390,089
Office equipment	936,509
Program equipment	93,013
Vehicles	<u>629,697</u>
Subtotal	<u>7,490,818</u>
Less accumulated depreciation	<u>4,294,307</u>
Total	<u>\$ 3,196,511</u>

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

INVESTMENTS

Investments (excluding cash) are as follows:

	<u>Cost</u>	<u>Fair Value</u>	<u>Unrealized Depreciation</u>
Certificates of Deposit	<u>\$ 387,000</u>	<u>\$ 367,878</u>	<u>\$ (19,122)</u>

The following schedule summarizes the investment return and its classification in the statement of activities:

	<u>Unrestricted</u>
Interest and dividend income	\$ 7,968
Realized gain	13,532
Unrealized gain	<u>2,089</u>
Total investment return	<u>\$ 23,589</u>

FAIR VALUE MEASUREMENT

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Organization uses various methods including market, income and cost approaches. Based on these approaches, the Organization often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborate, or generally unobservable inputs. The Organization utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used in the valuation techniques, the Organization is required to provide the following information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Valuation techniques used to measure fair value are prioritized into the following hierarchy:

Level 1 - Quoted prices for identical assets and liabilities traded in active exchange markets.

Level 2 - Observable inputs other than Level 1 including quoted prices for similar assets or liabilities, quoted prices in less active markets, or other observable inputs that can be corroborated by observable market data.

Level 3 - Unobservable inputs supported by little or no market activity for financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation; also includes observable inputs for nonbinding single dealer quotes not corroborated by observable market data.

While the Organization believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

During the year ended June 30, 2018, there were no changes to the Organization's valuation techniques that had, or are expected to have, a material impact on its financial position or changes in net assets.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FAIR VALUE MEASUREMENT (CONTINUED)

Certificates of deposit are measured based on quoted market prices, when available, or market prices provided by recognized broker-dealers. If listed prices or quotes are not available, fair value is based upon externally developed models that use unobservable inputs due to the limited market activity of the instrument.

Assets measured at fair value on a recurring basis, are summarized as follows:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Certificates of Deposit	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 367,878</u>	<u>\$ 367,878</u>

The following table presents a reconciliation of assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3 assets).

Balance, July 1, 2017	\$ 425,506
Sales	(62,093)
Net unrealized gain	4,465
Balance, June 30, 2018	<u>\$ 367,878</u>

The following table presents quantitative information about the investments:

	<u>Fair Value</u>	<u>Unfunded Commitments</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Certificates of Deposit	<u>\$ 367,878</u>	<u>\$ -</u>	Annually	1 day

MORTGAGES PAYABLE

Mortgages payable (See Note B - subsequent events) consist of the following:

Mortgage payable with Bank of America, dated April 11, 2014, due in monthly installments of \$2,168; interest at 5.250%; matures April 11, 2024, collateralized by real property at White Horse Pike in Absecon, New Jersey and certain furniture, fixtures, equipment and receivables owned. \$ 277,845

Mortgage payable with the New Jersey Economic Development Authority, dated February 13, 2001, due in varying monthly installments based on the amortization schedule; interest at 4.08% (See interest rate swap below); matures February 13, 2021, collateralized by real property at English Creek in Egg Harbor, New Jersey as well as accounts receivable and equipment. 396,581

Mortgage payable to the State of New Jersey, Department of Human Services dated July 24, 2011, 5% of the original principal of \$500,000 is forgiven every year if contract requirements are met; non-interest bearing. See Note M. 325,000

Subtotal 999,426

Less: current portion 178,767

Non-current portion of mortgages payable \$ 820,659

MILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

MORTGAGES PAYABLE (CONTINUED)

Total future scheduled maturities of long-term debt, which will be transferred to CFS on January 1, 2019, are as follows:

Years ending June 30:	
2019	\$ 178,767
2020	176,595
2021	152,599
2022	38,485
2023	39,221
Thereafter (includes a balloon payment)	<u>413,759</u>
Total	<u>\$ 999,426</u>

The Organization is required to meet certain financial covenants under the terms of the mortgage payable. As of June 30, 2018, the Organization was not in compliance with the debt service ratio covenant, and obtained a debt covenant waiver from the bank.

INTEREST RATE SWAP AGREEMENT

Objective of the swap. On February 1, 2011, the Organization entered into an interest rate swap agreement with Bank of America, N.A., in connection with its Tax Exempt Variable Rate Bond, also known as New Jersey Economic Development Bond ("Project"), to hedge against future interest rates.

Terms. The swap will mature on February 16, 2021 (See Note B - subsequent events) and was priced at a fixed rate of 4.12% based on an amortizing notional schedule with a \$1,252,444 initial notional amount. Under the swap starting February 14, 2011, the Organization pays a fixed rate of 4.12% and receives a variable payment equal to 62.5% of the one-month IM LIBOR and 206 basis points.

Fair Value. As of June 30, 2018, the swap had a negative fair value of \$2,710 which is recorded in the statement of financial position as a liability.

NET ASSETS

Temporarily Restricted

Temporarily restricted net assets are available for the following purposes or period:

Charity League - Client Assistance	<u>\$ 20,508</u>
------------------------------------	------------------

Net assets were released from donor restrictions as follows:

Purpose restriction accomplished:	
Expense incurred to satisfy donor restrictions	<u>\$ 66,424</u>

RETIREMENT PLANS

An employee deferral plan, as approved by the Board of Trustees, is provided through Mutual of America 403(b) Deferred Compensation Plan and is available to all employees as a salary reduction agreements. After one year of continuous employment with at least 1,000 hours of service, the employees are eligible to receive pension contributions through the agency at a rate of 3% of the employees' salary. All current employees participating in the previous pension plan were deemed eligible. As of June 30, 2018, the Board has elected to contribute \$42,004 to this plan. The contributions are at the discretion of the Board and are re-evaluated each year.

MILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

RETIREMENT PLANS (CONTINUED)

The Organization sponsors a flexplus cafeteria plan, which covers eligible employees. To be eligible for the plan benefits, an employee must be at least 21 years of age, have a minimum of 6 months service to the Organization, and work 35 or more hours per week. The amount of each participant's compensation which may be converted to cafeteria plan dollars for any plan year shall be determined by the employer prior to commencement of each plan year in the case of insured benefits, and by each participant in the case of flexible spending arrangements.

OPERATING LEASE

The Organization has a noncancelable operating lease for business premises that expires on October 31, 2023 (See Note B - subsequent events). Rent expense for this lease was \$27,000. Future minimum payments under the operating lease (See Note B - subsequent events) are as follows:

<u>Years ending June 30,</u>	
2019	\$ 29,000
2020	30,000
2021	30,000
2022	30,000
2023	30,000
2024	10,000
Total	<u>\$ 159,000</u>

DONATED RENT

The Organization occupies building space at Egg Harbor Township High School related to the school based youth services program. In addition, the Organization occupies a building owned by the County of Atlantic for their family success center. The landlords have estimated the approximate fair value of the rentals to be \$138,620. The fair value of the rentals is recorded as contribution income and rent expense in the consolidated statement of activities.

COMMITMENTS AND CONTINGENCIES

The Organization operates programs funded by federal and state grants that are renewed annually depending on the availability of funds and the Organization's compliance with the requirements of the contracts and grants. Therefore, annual funding under these grants is not guaranteed.

Mortgage Payable with the State of New Jersey

On June 24, 2011, the State of New Jersey, Department of Human Services, placed a mortgage on a property located in Egg Harbor, New Jersey in the amount of \$500,000. The mortgage will be forgiven by the State at the rate of 5% on the anniversary date of the mortgage, and on each successive anniversary date for twenty years thereafter upon submission by the Organization to the State that the property is being utilized for the purpose of the Organization. Upon completion of all terms of this mortgage, the mortgage will be cancelled. See Note G regarding the mortgage payable.

MILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

COMMITMENTS AND CONTINGENCIES (CONTINUED)

Noncompliance with Grantors

Financial awards from federal, state and local governmental entities in the form of grants are subject to audit. Such audits could result in claims against the Organization for disallowed costs or noncompliance with grantor restrictions. No provision has been made for any liabilities that may arise from such audits since the amounts, if any, cannot be determined at this date.

CONCENTRATION OF RISK AND UNCERTAINTIES

The Organization maintains cash and investment balances which may, at times, exceed federally insured limits. The Organization historically has not experienced any credit related losses. Management believes that it is not subject to any significant credit risk on its cash or investment accounts.

During the year ended June 30, 2018, the Organization received approximately 65% of its total revenue from government grants passed through various divisions at the State of New Jersey. At June 30, 2018, approximately 73% of receivables were due from the same divisions at the State of New Jersey.

SUPPLEMENTARY INFORMATION

	FSA	FSD	FSE	FSO	Eliminations	Consolidated
ASSETS						
Current assets						
Cash and cash equivalents	\$ 41,714	\$ 74,596	\$ -	\$ 222,668	\$ -	\$ 338,978
Accounts and grants receivable	476,871	-	560	-	-	477,431
Investments	-	21,779	-	-	-	21,779
Prepaid expenses	9,504	2,000	-	26,691	-	38,195
Due from subsidiaries	-	356,395	10,245	1,428,266	(1,794,906)	-
Total current assets	528,089	454,770	10,805	1,677,625	(1,794,906)	876,383
Investments	-	346,099	-	-	-	346,099
Property and equipment	813,807	-	-	2,382,704	-	3,196,511
Total Assets	\$ 1,341,896	\$ 800,869	\$ 10,805	\$ 4,060,329	\$ (1,794,906)	\$ 4,418,993

LIABILITIES AND NET ASSETS

Current liabilities						
Accounts payable and accrued expenses	\$ 280,876	\$ 7,674	\$ 225	\$ 38,632	\$ -	\$ 327,407
Refundable advances	205,185	-	-	-	-	205,185
Due to subsidiaries	1,794,906	-	-	-	(1,794,906)	-
Current portion of mortgages payable	25,000	-	-	153,767	-	178,767
Fair value of interest rate swap agreement	-	-	-	2,710	-	2,710
Total current liabilities	2,305,967	7,674	225	195,109	(1,794,906)	714,069
Mortgages payable	300,000	-	-	520,659	-	820,659
Total Liabilities	2,605,967	7,674	225	715,768	(1,794,906)	1,534,728
Net Assets	(1,264,071)	793,195	10,580	3,344,561	-	2,884,265
Total Liabilities and Net Assets	\$ 1,341,896	\$ 800,869	\$ 10,805	\$ 4,060,329	\$ (1,794,906)	\$ 4,418,993

See independent auditors' report.

	FSA	FSD	FSE	FSO	Eliminations	Consolidating
Support and revenues						
Government grants	\$ 3,893,595	-	-	-	-	\$ 3,893,595
Medicaid fees	1,534,766	-	-	-	-	1,534,766
Contributions	138,620	112,548	-	-	-	251,168
Client and third party fees	250,565	-	9,440	-	-	260,005
Investment return	-	21,190	-	2,399	-	23,589
Miscellaneous	14,087	-	500	-	-	14,587
Rent	-	-	-	178,210	(141,810)	36,400
Total support and revenues	<u>5,831,633</u>	<u>133,738</u>	<u>9,940</u>	<u>180,609</u>	<u>(141,810)</u>	<u>6,014,110</u>
Expenses						
Salaries	2,698,748	38,500	3,490	683,584	-	3,424,322
Fringe benefits	741,886	9,705	990	231,704	-	984,285
Consulting fees	455,659	9,378	580	52,466	-	518,083
Travel	43,326	195	-	3,271	-	46,792
Occupancy	732,772	2,018	913	278,381	(141,810)	872,274
Materials and supplies	206,405	14,801	-	24,805	-	246,011
Client assistance	434,101	-	-	-	-	434,101
Other expenses	100,849	9,594	87	72,594	-	183,124
Depreciation	76,852	-	-	40,686	-	117,538
Total expenses before management and general	<u>5,490,598</u>	<u>84,191</u>	<u>6,060</u>	<u>1,387,491</u>	<u>(141,810)</u>	<u>6,826,530</u>
Allocated management and general	1,159,907	-	1,514	(1,161,421)	-	-
Total expenses	<u>6,650,505</u>	<u>84,191</u>	<u>7,574</u>	<u>226,070</u>	<u>(141,810)</u>	<u>6,826,530</u>
Change in net assets from operations	<u>(818,872)</u>	<u>49,547</u>	<u>2,366</u>	<u>(45,461)</u>	<u>-</u>	<u>(812,420)</u>
Non-operating revenues (expenses)						
Forgiveness of debt - State of NJ	25,000	-	-	-	-	25,000
Gain on sale of property and equipment	17,609	-	-	-	-	17,609
Net depreciation in fair value of interest rate swap	-	-	-	(29,669)	-	(29,669)
Total non-operating revenues (expenses)	<u>42,609</u>	<u>-</u>	<u>-</u>	<u>(29,669)</u>	<u>-</u>	<u>12,940</u>
Change in net assets	<u>(776,263)</u>	<u>49,547</u>	<u>2,366</u>	<u>(75,130)</u>	<u>-</u>	<u>(799,480)</u>
Net assets, beginning of year	<u>(487,808)</u>	<u>743,648</u>	<u>8,214</u>	<u>3,419,691</u>	<u>-</u>	<u>3,683,745</u>
Net assets, end of year	<u>\$ (1,264,071)</u>	<u>\$ 793,195</u>	<u>\$ 10,580</u>	<u>\$ 3,344,561</u>	<u>\$ -</u>	<u>\$ 2,884,265</u>

See independent auditors' report.

Federal Grantor/Pass-Through Grantor/ Program or Cluster Title	Federal CFDA Number	Pass-Through Entity Identification Number	Grant Period	Total Federal Expenditures
U.S. Department of Agriculture, Passed through the State of New Jersey, Department of Agriculture, Division of Food and Nutrition, Child and Adult Care Program	10.558	100-010-3350-029 / 100-010-3350-031	10/01/16 - 09/30/18	\$ 40,793
U.S. Department of Health and Human Services, Passed through the State of New Jersey, Department of Human Services, Division of Family Development	93.558	100-054-7550-292	10/01/16 - 09/30/17	60,438
SAIF - TANF	93.558	100-054-7550-292	10/01/17 - 09/30/18	179,858
SAIF - TANF				
Administration for Children and Families, Passed through the State of New Jersey, Department of Children and Families, Division of Family and Community Partnerships	93.558	100-016-1630-033	07/01/17 - 06/30/18	168,423
School Based Services- EHT				408,719
Subtotal				
U.S. Department of Health and Human Services, Passed through the State of New Jersey, Department of Human Services, Division of Family Development	10.561	100-054-7550-295	10/01/16 - 09/30/17	75,601
Initiative SAIF- GA	10.561	100-054-7550-295	10/01/17 - 09/30/18	162,823
Initiative SAIF- GA				238,424
Subtotal				
U.S. Department of Health and Human Services, Passed through the State of New Jersey, Department of Law and Public Safety, Juvenile Justice Commission, Passed through the County of Atlantic	93.052	K.16.244	01/01/17 - 12/31/17	16,597
Grandparents Raising Grandchildren	93.052	K.16.244	01/01/18 - 12/31/18	16,929
Grandparents Raising Grandchildren				33,126
Subtotal				
Administration for Children and Families, Passed through the State of New Jersey, Department of Children and Families, Division of Family and Community Partnerships	93.870	100-016-1630-044	07/01/17 - 06/30/18	226,253
Parents as Teachers				
Total Expenditures of Federal Awards				\$ 947,315

See notes to the Schedules.

State Grantor Department and Program Title	State Grant Award or Account Number	Grant Award Period	Fiscal Year Grant Expenditures	Total Grant Expenditures to Date
State of New Jersey, Department of Health, Division of Mental Health Services Multi-Cultural Competency Training	40103 / 100-054-7700-029	07/01/17 - 06/30/18	\$ 284,078	\$ 284,078
State of New Jersey, Department of Children and Families Division of Children's System of Care, Outpatient Safe Harbor Rainbow Place Subtotal Division of Children's System of Care	18CXAR / 100-016-1620-014 18CXAR / 100-016-1620-014	07/01/17 - 06/30/18 07/01/17 - 06/30/18	191,625 153,766 345,391	191,625 153,766 345,391
Division of Child Protection and Permanency Outpatient Family Life Center Subtotal Division of Child Protection and Permanency	18AMAS / 100-016-1610-023 & 100-016-1610-039	07/01/17 - 06/30/18	82,258 569,316 651,574	82,258 569,316 651,574
Division of Family and Community Partnerships School Based Services - EHT Kinship Legal Guardianship Kinship Wraparound Subtotal Division of Family and Community Partnerships	18DTAP / 100-016-1630-013 18DTAP / 100-016-1630-024 18DTAP / 100-016-1630-024	07/01/17 - 06/30/18 07/01/17 - 06/30/18 07/01/17 - 06/30/18	90,514 117,855 659,495 867,864	90,514 117,855 659,495 867,864
Division of Family and Community Partnerships, Passed through the County of Atlantic Inland Family Success Center New Day Family Center Subtotal County of Atlantic	18DRAP 18DRAP	07/01/17 - 06/30/18 07/01/17 - 06/30/18	234,649 291,904 526,553	234,649 291,904 526,553
Direct Service Professional Wage Increase	100-059-1600-059	07/01/17 - 06/30/18	9,245	9,245
State of New Jersey, Department of Human Services, Division of Family Development SAIF - Cumberland County Initiative SAIF - GA	100-054-7550-072 100-054-7550-308	01/01/17 - 12/31/17 10/01/17 - 09/30/18	14,074 61,487 75,561	14,074 61,487 75,561

See notes to the Schedules.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

SCHEDULE OF EXPENDITURES OF STATE FINANCIAL ASSISTANCE (CONTINUED)

Year Ended June 30, 2018

State Grantor Department and Program Title	State Grant Award or Account Number	Grant Award Period	Fiscal Year Grant Expenditures	Total Grant Expenditures to Date
State of New Jersey, Department of Law and Public Safety, Juvenile Justice Commission, Passed through the County of Atlantic				
JDAI - HEDS CM	K.16.229A	01/01/17 - 12/31/18	79,691	79,691
JDAI - HEDS JDAI	K16.229	01/01/17 - 12/31/18	54,507	54,507
Grandparents Raising Grandchildren	K.16.244	01/01/17 - 12/31/18	11,042	11,042
Adolescent Sex Offenders	K.16.225	01/01/17 - 12/31/18	8,774	8,774
Subtotal County of Atlantic			<u>154,014</u>	<u>154,014</u>
State of New Jersey, Department of Labor, Employment Services Skills Partnership Training Grant Program	780-D62-4545-003	07/01/17 - 06/30/18	32,000	32,000
Total Expenditures of State Financial Assistance			<u>\$ 2,946,280</u>	<u>\$ 2,946,280</u>

See notes to the Schedules.

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

**NOTES TO THE SCHEDULES OF EXPENDITURES OF FEDERAL AWARDS AND STATE
FINANCIAL ASSISTANCE
Year Ended June 30, 2018**

Note 1. Basis of Presentation

The accompanying schedules of expenditures of federal awards and state financial assistance (the "Schedules") include the federal and state grant activity of FSA under programs of the federal and state government for the year ended June 30, 2018. The information in these Schedules 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* ("Uniform Guidance") and State of New Jersey, Circular Letter 15-08-OMB, *Single Audit Policy for Recipients of Federal Grants, State Grants and State Aid* (the "Circular"). Because the Schedules present only a selected portion of the operations of FSA, they are not intended to and do not present the financial position, change in net assets or cash flows of FSA.

Note 2. Summary of Significant Accounting Policies

Expenditures reported on the Schedules are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance and the State of New Jersey, Departments of Human Services and Children and Families Cost Reimbursement Manuals, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

Note 3. Indirect Cost Rate

FSA has elected not to use the 10-percent de minimis indirect cost rate allowed under the Uniform Guidance.

Note 4. Reconciliation of Government grants to Schedules

Government grants revenue per audit:	\$ 3,893,595
Expenses per Schedules	
Federal awards	947,315
State financial assistance	<u>2,946,280</u>
Total expenses per Schedules	<u>3,893,595</u>
Variance	<u>\$ -</u>

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended June 30, 2018

Section I - Summary of Auditors' Results

Consolidated Financial Statements

Type of auditors' report issued on whether the consolidated financial statements audited were prepared in accordance with U.S. GAAP: ***Unmodified***

Internal control over financial reporting:

- Material weaknesses identified? Yes No
- Significant deficiencies identified? Yes None Reported

Noncompliance material to consolidated financial statements noted?

Yes No

Federal Awards and State Financial Assistance

Internal control over major programs:

- Material weaknesses identified? Yes No
- Significant deficiencies identified? Yes None Reported

Type of auditors' report issued on compliance for major federal and state programs: ***Unmodified***

Any audit findings disclosed that are required to be reported in accordance with section 2 CFR 200.516(a) or the Circular?

Yes No

Identification of major federal and state programs:

<u>CFDA Number/ State Account Number</u>	<u>Name of Federal or State Program or Cluster</u>
93.870	Administration for Children and Families, Passed through the State of New Jersey, Department of Children and Families, Division of Family and Community Partnerships - Parents as Teachers - 18 DTAP
40103 / 100-054-7700-029	State of New Jersey, Department of Health, Division of Mental Health Services - Multi-Cultural Competency Training
18DTAP / 100-016-1630-013 & 100-016-1630-024	Division of Family and Community Partnerships- School Based Services- EHT, Kinship Legal Guardianship and Kinship Wraparound

Dollar threshold used to distinguish between type A and type B programs:

\$750,000

Auditee qualified as low-risk auditee?

Yes No

FAMILY SERVICE OPERATIONS, INC. AND SUBSIDIARIES

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
Year Ended June 30, 2018

Section II - Consolidated Financial Statement Findings

No matters were reported.

Section III - Findings and Questioned Costs for Federal Awards and State Financial Assistance

No matters were reported.

Section IV - Prior Year Audit Findings

No matters were reported.

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

To the Board of Trustees of
Family Service Operations, Inc. and Subsidiaries

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 consolidated financial statements of Family Service Operations, Inc. and Subsidiaries (the "Organization"), as of and for the year ended June 30, 2018, 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, and have issued our report thereon dated November 15, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the Organization's internal control over financial reporting ("internal control") to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Organization's 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 consolidated 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.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organization's consolidated 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 consolidated 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.

Mercedien, P.C.

Certified Public Accountants

November 15, 2018

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL AND STATE PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE

To the Board of Trustees of
Family Service Association

Report on Compliance for Each Major Federal and State Program

We have audited Family Service Association's ("FSA") compliance with the types of compliance requirements described in the *OMB Compliance Supplement and New Jersey State Grant Compliance Supplement* that could have a direct and material effect on each of FSA's major federal and state programs for the year ended June 30, 2018. FSA's major federal and state programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the federal and state statutes, regulations and the terms and conditions of its federal and state awards applicable to its federal and state programs.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for each of FSA's major federal and state programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. CFR Part 200, *Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards* ("Uniform Guidance") and State of New Jersey Circular Letter 15-08-OMB (the "Circular"), *Single Audit Policy for Recipients of Federal Grants, State Grants and State Aid*. Those standards and the Uniform Guidance and the Circular 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 or state program occurred. An audit includes examining, on a test basis, evidence about FSA's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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

Opinion on Each Major Federal and State Program

In our opinion, FSA complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal and state programs for the year ended June 30, 2018.

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL AND STATE PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE
(CONTINUED)**

Report on Internal Control Over Compliance

Management of FSA 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 FSA's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal and state program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal and state program and to test and report on internal control over compliance in accordance with the Uniform Guidance and the Circular, 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 FSA's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal or state program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal or state 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 or state 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 and the Circular. Accordingly, this report is not suitable for any other purpose.

Mercedien, P.C.
Certified Public Accountants

November 15, 2018