



**Report of Independent Auditors and
Financial Statements with
Additional Information for**
Episcopal Community Services
June 30, 2012 and 2011

MOSS ADAMS_{LLP}

Certified Public Accountants | Business Consultants

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REPORT OF INDEPENDENT AUDITORS

Board of Directors
Episcopal Community Services

We have audited the accompanying statements of financial position of Episcopal Community Services ("ECS") as of June 30, 2012 and 2011, and the related statements of activities, functional expenses, and cash flows for the years then ended. These financial statements are the responsibility of ECS' management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of ECS' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Episcopal Community Services as of June 30, 2012 and 2011, and the changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Moss Adams LLP

San Diego, California
October 16, 2012

EPISCOPAL COMMUNITY SERVICES

STATEMENTS OF FINANCIAL POSITION JUNE 30, 2012 AND 2011

	2012	2011
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 1,576,550	\$ 1,202,834
Funds held by others	588,920	193,743
Receivables, net	1,136,278	716,770
Prepaid expenses and other current assets	241,367	228,500
Property held for sale or reconveyance	-	498,149
Total current assets	3,543,115	2,839,996
Deposits and Other Assets	118,313	103,405
Unconditional Promises to Give, net	552,126	387,972
Property and Equipment, net	2,063,666	2,033,868
Total assets	<u>\$ 6,277,220</u>	<u>\$ 5,365,241</u>
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts payable and accrued expenses	\$ 892,104	\$ 776,876
Accrued payroll	976,879	747,986
Deferred revenue	127,711	188,313
Conditional contribution for property held for sale or reconveyance	97,094	97,094
Current portion of long-term debt	42,550	42,438
Total current liabilities	2,136,338	1,852,707
Long-term Debt	477,337	505,089
Conditional Contribution	320,400	345,000
Total liabilities	<u>2,934,075</u>	<u>2,702,796</u>
Commitments and Contingencies (Notes 7, 10, and 12)		
Net Assets		
Unrestricted	2,760,520	2,242,998
Temporarily restricted	582,625	419,447
Total net assets	<u>3,343,145</u>	<u>2,662,445</u>
Total liabilities and net assets	<u>\$ 6,277,220</u>	<u>\$ 5,365,241</u>

EPISCOPAL COMMUNITY SERVICES

STATEMENTS OF ACTIVITIES YEARS ENDED JUNE 30, 2012 AND 2011

	2012			2011		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
REVENUES, GAINS, AND OTHER SUPPORT						
Grants and contracts	\$ 20,288,318	\$ -	\$ 20,288,318	\$ 18,230,757	\$ -	\$ 18,230,757
Service fees	3,010,589	-	3,010,589	2,793,215	-	2,793,215
Contributions	704,354	-	704,354	419,243	1,226	420,469
Other	284,826	-	284,826	219,342	-	219,342
Change in value of beneficial interests in charitable remainder trusts	-	164,154	164,154	-	(37,709)	(37,709)
Net assets released from restrictions	976	(976)	-	169,415	(169,415)	-
Total revenues, gains, and other support	<u>24,289,063</u>	<u>163,178</u>	<u>24,452,241</u>	<u>21,831,972</u>	<u>(205,898)</u>	<u>21,626,074</u>
EXPENSES						
Programs:						
Child development	15,271,822	-	15,271,822	12,578,483	-	12,578,483
Clinical services	2,925,397	-	2,925,397	2,650,930	-	2,650,930
Housing and supportive services	2,128,464	-	2,128,464	2,800,344	-	2,800,344
Nutrition services	916,319	-	916,319	853,537	-	853,537
Total program expenses	21,242,002	-	21,242,002	18,883,294	-	18,883,294
Management and general	2,272,814	-	2,272,814	2,096,088	-	2,096,088
Fundraising and communications	256,725	-	256,725	233,572	-	233,572
Total expenses	<u>23,771,541</u>	<u>-</u>	<u>23,771,541</u>	<u>21,212,954</u>	<u>-</u>	<u>21,212,954</u>
CHANGE IN NET ASSETS	517,522	163,178	680,700	619,018	(205,898)	413,120
NET ASSETS						
Beginning of year	2,242,998	419,447	2,662,445	1,623,980	625,345	2,249,325
End of year	<u>\$ 2,760,520</u>	<u>\$ 582,625</u>	<u>\$ 3,343,145</u>	<u>\$ 2,242,998</u>	<u>\$ 419,447</u>	<u>\$ 2,662,445</u>

EPISCOPAL COMMUNITY SERVICES

STATEMENT OF FUNCTIONAL EXPENSES YEAR ENDED JUNE 30, 2012

	<u>Programs</u>	<u>Management and General</u>	<u>Fundraising and Communications</u>	<u>Total</u>
Personnel	\$ 14,066,430	\$ 1,615,074	\$ 143,223	\$ 15,824,727
Other direct costs	4,197,835	316,669	64,058	4,578,562
Occupancy	2,601,624	315,861	43,394	2,960,879
Depreciation	367,678	20,391	6,050	394,119
Interest	8,435	4,819	-	13,254
Total expenses	<u>\$ 21,242,002</u>	<u>\$ 2,272,814</u>	<u>\$ 256,725</u>	<u>\$ 23,771,541</u>

EPISCOPAL COMMUNITY SERVICES

STATEMENT OF FUNCTIONAL EXPENSES YEAR ENDED JUNE 30, 2011

	<u>Programs</u>	<u>Management and General</u>	<u>Fundraising and Communications</u>	<u>Total</u>
Personnel	\$ 13,021,998	\$ 1,337,442	\$ 151,612	\$ 14,511,052
Other direct costs	2,860,406	384,969	40,535	3,285,910
Occupancy	2,677,243	337,050	41,425	3,055,718
Depreciation	316,681	28,915	-	345,596
Interest	6,966	7,712	-	14,678
Total expenses	<u>\$ 18,883,294</u>	<u>\$ 2,096,088</u>	<u>\$ 233,572</u>	<u>\$ 21,212,954</u>

EPISCOPAL COMMUNITY SERVICES

STATEMENTS OF CASH FLOWS YEARS ENDED JUNE 30, 2012 AND 2011

	2012	2011
OPERATING ACTIVITIES		
Change in net assets	\$ 680,700	\$ 413,120
Adjustments to reconcile change in net assets to net cash and cash equivalents provided by operating activities:		
Depreciation	394,119	345,596
Allowance for uncollectible receivables	20,000	-
Change in value of charitable remainder trusts	(164,154)	37,709
Loss on sale or reconveyance of property	68,149	-
Loss on disposal of property and equipment	207,392	27,989
Accrued interest added to note payable	7,535	6,785
Conditional contribution forgiveness	(24,600)	(38,470)
Deferred revenue	(60,602)	96,016
(Increase) decrease in operating assets:		
Receivables	(439,508)	306,611
Prepaid expenses and other current assets	(12,867)	(31,827)
Deposits and other assets	(14,908)	4,346
Unconditional promises to give	-	120,000
Increase (decrease) in operating liabilities:		
Accounts payable and accrued expenses	115,228	(72,186)
Accrued payroll	228,893	(176,840)
Advances	-	(24,143)
Net cash provided by operating activities	<u>1,005,377</u>	<u>1,014,706</u>
INVESTING ACTIVITIES		
Purchases of property and equipment	(631,309)	(723,909)
Proceeds from sale of property held for sale or reconveyance	430,000	-
Increase in funds held by others	(395,177)	(193,743)
Net cash (used in) investing activities	<u>(596,486)</u>	<u>(917,652)</u>
FINANCING ACTIVITIES		
Proceeds from long-term debt	39,479	-
Repayment of long-term debt	(74,654)	(730,120)
Net cash (used in) financing activities	<u>(35,175)</u>	<u>(730,120)</u>
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	373,716	(633,066)
CASH AND CASH EQUIVALENTS		
Beginning of year	1,202,834	1,835,900
End of year	<u>\$ 1,576,550</u>	<u>\$ 1,202,834</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash payments for interest	<u>\$ 5,719</u>	<u>\$ 14,678</u>
SUPPLEMENTAL DISCLOSURE OF NON-CASH ACTIVITY		
Transfer of property to property held for sale or reconveyance	<u>\$ 288,301</u>	<u>\$ 498,149</u>

See accompanying notes.

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 1 – Nature of Organization

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

Programs offered by ECS are:

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

Other Programs: ECS also offers programs that assist individuals and families through the often difficult transition from an existence which is dependent on social services, unhealthy relationships, or substance abuse to one of self-sufficiency. ECS offers a full spectrum of services to Southern Californians in transition, including emergency assistance and crisis intervention, drug and alcohol education and support services, domestic violence programs, employment assistance, food, counseling services for the chronically mentally ill, and short-term and long-term housing for the special-needs homeless population.

Income Taxes: As a California not-for-profit public benefit corporation, ECS is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code. ECS may be subject to federal or state income taxes on unrelated business income. For each of the years ended June 30, 2012 and 2011, no provision for such taxes is required. ECS had no unrecognized tax benefits or liabilities as of June 30, 2012 and 2011. ECS files an exempt organization return in the United States federal jurisdiction and with the Franchise Tax Board in the state of California. ECS is no longer subject to income tax examinations by taxing authorities for years before 2009 for its federal filings and for years before 2008 for its state filings.

Note 2 – Summary of Significant Accounting Policies

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

Financial Statement Presentation: Net assets are classified as unrestricted, temporarily restricted, and permanently restricted based upon the following criteria:

- Unrestricted net assets represent expendable funds available for operations that are not otherwise limited by donor restrictions.
- Temporarily restricted net assets consist of contributed funds subject to specific donor-imposed restrictions, which are contingent upon a specific performance of a future event or a specific passage of time before ECS may spend the funds.
- Permanently restricted net assets are subject to irrevocable donor restrictions requiring that the assets be maintained in perpetuity, primarily for generating investment income to fund current operations. ECS has no permanently restricted net assets at June 30, 2012 and 2011.

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 2 – Summary of Significant Accounting Policies (Continued)

Revenue Recognition

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

Service Fees: Revenue from service fees is recognized when services are provided.

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

Deferred Revenue: Fees received prior to performing services under contractual agreements are recorded as deferred revenue.

Advances: Advances represent funds received for the Head Start program prior to the new program year.

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

Cash: In accordance with the terms of a contract with a funding agency, funds received for the Head Start program are required to be maintained in a separate bank account. As of June 30, 2012 and 2011, approximately \$580,000 and \$314,000, respectively, of the Head Start program funds were held in a separate bank account. These funds are included in cash in the accompanying statements of financial position.

Funds Held by Others: Funds held by others are funds invested at the Rancho Santa Fe Foundation ("RSFF"). Under a custodial agreement, RSFF manages the investment of the funds, which are primarily invested in publicly-traded fixed income and equity funds. RSFF reports the fair value of the amounts due to ECS on a regular basis. ECS did not grant variance power over the investments to RSFF. Distributions can be made from the funds only with written authorization from ECS. The fair value of investments held at RSFF is based on the unit value of ECS' interest in the pools in which it has invested. The unit value is based on the fair value of the underlying assets in the pools. Investment income or loss (including interest and realized gains and losses) is included in unrestricted revenues unless restricted by donor or law.

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

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

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 2 - Summary of Significant Accounting Policies (Continued)

Included in unconditional promises to give are beneficial interests ECS has received in irrevocable charitable remainder trusts. The trust agreements require the trusts to make periodic payments, as defined, to the grantors or other designated beneficiaries of the trust over the beneficiary's lifetime and, in some cases, after the beneficiary's death. The trusts terminate upon the death of the grantors or completion of the specified benefit periods after their death. Upon termination of the trusts, ECS will receive its share of the remaining trust assets as designated in the trust agreements. The portion of a trust attributable to the fair value of the future benefits to be received by ECS is recorded in the statement of activities as temporarily restricted contributions in the year the trust is established. The fair value of the remainder interests at June 30, 2012 and 2011 is calculated based on a discounted cash flow model using interest rates of approximately 2 and 4 percent, respectively, and applicable mortality tables.

Allowance for Estimated Uncollectible Accounts: The allowance for estimated uncollectible accounts is based on past experience and on an analysis of current receivable balances. ECS does not obtain collateral. Accounts deemed uncollectible are written-off against the allowance in the year deemed uncollectible. Management established an allowance of approximately \$20,000 on receivables from client service fees as of June 30, 2012. Management did not consider an allowance necessary as of June 30, 2011.

Property Held for Sale or Reconveyance: Property held for sale or reconveyance is recorded at the lower of its carrying amount or fair value, less cost to sell. Assets classified as "held for sale or reconveyance" are no longer depreciated.

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

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

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

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions related to the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may materially differ from those estimates.

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 2 - Summary of Significant Accounting Policies (Continued)

Subsequent Events: Subsequent events are events or transactions that occur after the statements of financial position date, but before the financial statements are issued. ECS recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the statements of financial position, including the estimates inherent in the process of preparing the financial statements. ECS' financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statements of financial position, but arose after the statements of financial position date and before the financial statements are available to be issued. ECS has evaluated subsequent events through October 16, 2012, which is the date the financial statements were available to be issued.

Note 3 - Concentrations

Unconditional Promises to Give: Unconditional promises to give include charitable remainder trusts which are exposed to various risks such as interest rates and donor life expectancies. Changes in the near-term are not expected to materially affect the amounts reported in the financial statements. As of June 30, 2012 and 2011, approximately 96 percent of unconditional promises to give is due from two donors.

Grants and Contracts: Included in revenue from grants and contracts is approximately \$17,080,000 and \$14,249,000 during the years ended June 30, 2012 and 2011, respectively, earned from one funding source, which represents approximately 70 and 78 percent of total revenues, gains, and other support for each of the years ended June 30, 2012 and 2011, respectively.

Note 4 - Unconditional Promises to Give

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

	2012	2011
Due in one to five years:		
Beneficial interest in charitable remainder trust	\$ -	\$ 14,134
Less discount to net present value	<u>-</u>	<u>(4,933)</u>
Net unconditional promises to give due in one to five years	<u>-</u>	<u>9,201</u>
Due in more than five years:		
Beneficial interest in charitable remainder trusts	925,903	935,824
Less discount to fair value	<u>(373,777)</u>	<u>(557,053)</u>
Net unconditional promises to give due in more than five years	<u>552,126</u>	<u>378,771</u>
Total long-term unconditional promises to give	<u>\$ 552,126</u>	<u>\$ 387,972</u>

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 5 - Fair Value

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. The fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. There are three levels of inputs that may be used to measure fair value:

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

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

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

See Note 2 for the valuation methodologies used for funds held by others and beneficial interests in irrevocable charitable remainder trusts that are measured at fair value on a recurring basis and recognized in the accompanying statements of financial position. The funds held by others and the beneficial interests in charitable remainder trusts are classified as Level 3 in the fair value hierarchy.

The following table discloses the summary of changes in the fair value of ECS' Level 3 assets for the year ended June 30:

	2012		
	Beneficial Interests	Funds Held by Others	Total
Balance, beginning of year	\$ 387,972	\$ 193,743	\$ 581,715
Additions	-	393,838	393,838
Change in value of beneficial interests	164,154	-	164,154
Unrealized gains net of fees	-	1,339	1,339
Balance, end of year	<u>\$ 552,126</u>	<u>\$ 588,920</u>	<u>\$ 1,141,046</u>
	2011		
	Beneficial Interests	Funds Held by Others	Total
Balance, beginning of year	\$ 425,681	\$ -	\$ 425,681
Additions	-	190,016	190,016
Change in value of beneficial interests	(37,709)	-	(37,709)
Unrealized gains net of fees	-	3,727	3,727
Balance, end of year	<u>\$ 387,972</u>	<u>\$ 193,743</u>	<u>\$ 581,715</u>

Unrealized gains are reported in the statements of activities as a component of other income. The change in value of the beneficial interests is a separate line in the statements of activities. For the year ended June 30, 2012, both amounts are from Level 3 assets still held as of June 30, 2012.

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 6 - Property and Equipment

As of June 30, property and equipment consists of:

	2012	2011
Leasehold improvements	\$ 1,848,684	\$ 2,214,989
Equipment	935,909	1,836,298
Buildings and improvements	615,555	535,637
Vehicles	<u>162,772</u>	<u>85,222</u>
	3,562,920	4,672,146
Less accumulated depreciation and amortization	<u>(1,622,954)</u>	<u>(2,761,978)</u>
	1,939,966	1,910,168
Land	<u>123,700</u>	<u>123,700</u>
	<u>\$ 2,063,666</u>	<u>\$ 2,033,868</u>

As of June 30, 2011, property held for sale or reconveyance consisted of:

Buildings and improvements	\$ 672,868
Land	<u>64,611</u>
	737,479
Less accumulated depreciation and amortization	<u>(239,330)</u>
	<u>\$ 498,149</u>

On October 21, 2011, ECS sold a building and land, with a net book value of approximately \$210,000, which was used in one of ECS' programs (Julian's) for approximately \$430,000. A conditional contribution of approximately \$97,000 related to this property will be returned to the grantor.

On October 27, 2011, ECS reconveyed a building used in one of ECS' programs with a book value of approximately \$288,000 to the original grantor. No funds were exchanged in the reconveyance transaction.

Total additions of property and equipment for the child development programs were approximately \$384,000 and \$570,000 for the years ended June 30, 2012 and 2011, respectively. Of these total additions for the year ended June 30, 2011, \$333,000 was funded by Program Improvement and American Recovery and Reinvestment Act grants.

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 7 - Debt

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

	2012	2011
Note payable of \$226,150, San Diego Housing Commission ("SDHC"), secured by deed of trust on land and building. Bears simple interest of 3 percent per annum. Principal and interest are due the earlier of November 2051, upon the generation of residual receipts, or upon acceleration of the loan as defined in the agreement	\$ 324,019	\$ 316,484
Note payable, Diocese of Los Angeles, unsecured. Annual payments of \$25,000; due December 2018; non-interest bearing	150,000	175,000
Note payable, Diocese of San Diego, unsecured. Monthly principal and interest payments of \$538; interest of 4.8 percent; due March 2018	31,948	36,740
Notes payable, finance company, secured by software. 2011 note paid in full; 2012 note has monthly payments of \$2,623; non-interest bearing; due September 2012	7,262	7,867
Note payable, finance company, secured by vehicle. Monthly principal and interest payments of \$473; interest of 9.19 percent; due September 2013	<u>6,658</u>	<u>11,436</u>
	519,887	547,527
Less current portion	<u>42,550</u>	<u>42,438</u>
	<u>\$ 477,337</u>	<u>\$ 505,089</u>

Future minimum debt service payments are as follows:

Years ending June 30,	
2013	\$ 42,550
2014	31,669
2015	30,532
2016	30,804
2017	31,088
Thereafter	<u>353,244</u>
	<u>\$ 519,887</u>

Line of Credit: ECS has a revolving bank line of credit in the amount of \$250,000 secured by assets of ECS. No balance was outstanding on the line of credit as of June 30, 2012 and 2011. The interest rate on the line is the bank's prime rate plus 2.00 percent (3.25 percent at June 30, 2012).

Total interest expense on debt was approximately \$13,000 and \$15,000 for the years ended June 30, 2012 and 2011, respectively.

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 8 - Conditional Contributions

During 1998 and 1999, ECS was awarded two conditional contributions for \$138,705 and \$394,200 from the United States Department of Housing and Urban Development ("HUD") and the SDHC, respectively. Both contributions were used to purchase or rehabilitate facilities that were placed into service during August 1998 and November 1999, respectively, and are utilized by ECS to provide supportive housing to the homeless. The HUD funds were used for the Julian's Anchorage facility and the SDHC funds were used for the San Diego Downtown Safe Haven facility.

Of the total SDHC conditional contribution, \$246,000 was considered fully revocable until ten years from the date the facilities were placed into supportive housing program operations. Ten percent of these contributions become unconditional each year subsequent to the tenth year of operation. The ten-year period of operation for the SDHC facilities was completed in November 2009. During each of the years ended June 30, 2012 and June 30, 2011, ECS recognized 10 percent of the SDHC conditional contribution totaling \$24,600. The remaining \$148,200 of the conditional contribution from SDHC is considered fully revocable until 55 years from the date of contribution. This contribution will become unconditional in February 2054 provided ECS has used the facility to provide supportive housing to the homeless until that time. The remaining SDHC conditional contribution at June 30, 2012 and 2011 is \$320,400 and \$345,000, respectively.

The SDHC conditional contribution and a note payable to SDHC (Note 7) are secured by a first trust deed on a building and land with a net book value of approximately \$440,000 and \$438,000 at June 30, 2012 and 2011, respectively.

The HUD conditional contribution was considered fully revocable until ten years from the date the facilities were placed into supportive housing program operations. Ten percent of this contribution becomes unconditional each year subsequent to the tenth year of operation. The ten-year period of operation for the HUD facilities was completed August 2008. During the year ended June 30, 2011, ECS recognized 10 percent of the HUD conditional contribution totaling \$13,870. During the year ended June 30, 2012, the Julian's Anchorage facility was sold and no amount of the conditional contribution was recognized. In August 2012, the remaining conditional contribution of approximately \$97,000 was returned to HUD.

Note 9 - Temporarily Restricted Net Assets

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

	2012	2011
Time restrictions:		
Charitable remainder trusts	\$ 552,126	\$ 387,972
Purpose restrictions - programs	<u>30,499</u>	<u>31,475</u>
	<u>\$ 582,625</u>	<u>\$ 419,447</u>

For the years ended June 30, temporarily restricted net assets were released for:

Program administration	\$ 976	\$ -
Payment received on pledge receivable	-	120,000
Women's and Children's programs	-	43,352
Desert Vista - Change a Life	<u>-</u>	<u>6,063</u>
	<u>\$ 976</u>	<u>\$ 169,415</u>

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 10 - Employee Benefit Plan

ECS has a 401(k) retirement plan (the "Plan") covering all employees, except Episcopal clergy, who have completed one year of service and are at least 18 years of age. ECS' contributions to the Plan are determined annually by the Board of Directors. ECS has expensed and accrued matching and profit-sharing contributions to the Plan totaling approximately \$262,000 and \$237,000 for the years ended June 30, 2012 and 2011, respectively.

Note 11 - Union Contract

A substantial portion of ECS' labor force has been subject to a collective bargaining agreement. The agreement expired on June 30, 2012. A new agreement for the period of July 1, 2012 through June 30, 2015 has been ratified by the union.

Note 12 - Commitments and Contingencies

ECS occupies facilities in various locations under month-to-month and long-term operating leases with terms extending through June 2017. Rental expense under operating leases was approximately \$1,586,000 and \$1,825,000 for the years ended June 30, 2012 and 2011, respectively.

Future minimum annual rentals under long-term operating leases at June 30, 2012 are as follows:

Years ending June 30,	
2013	\$ 1,528,385
2014	787,531
2015	638,563
2016	479,988
2017	208,511
	<u>\$ 3,642,978</u>

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

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

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

EPISCOPAL COMMUNITY SERVICES

NOTES TO FINANCIAL STATEMENTS

Note 13 - Related-party Transactions

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

	2012	2011
Note payable to Episcopal Diocese of Los Angeles	\$ 150,000	\$ 175,000
Note payable to Episcopal Diocese of San Diego	31,948	36,740
Contribution from Episcopal Diocese of San Diego	-	20,000

Also, ECS has a beneficial interest in a charitable remainder trust for which a member of the Board of Directors is a trustee. ECS' beneficial interest is valued at approximately \$282,000 and \$181,000 as of June 30, 2012 and 2011, respectively.

ADDITIONAL INFORMATION

REPORT OF INDEPENDENT AUDITORS ON THE ADDITIONAL INFORMATION

Board of Directors
Episcopal Community Services

We have audited the financial statements of Episcopal Community Services as of and for the year ended June 30, 2012, and have issued our report thereon dated October 16, 2012, which contained an unqualified opinion on those financial statements and appears on page 1. Our audit was performed for the purpose of forming an opinion on the financial statements as a whole. The schedule of revenue and expenses by activity is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Moss Adams LLP

San Diego, California
October 16, 2012

EPISCOPAL COMMUNITY SERVICES

ADDITIONAL INFORMATION SCHEDULE OF REVENUE AND EXPENSES BY ACTIVITY YEAR ENDED JUNE 30, 2012

	Child Development Programs	Housing and Supportive Services Programs	Clinical Services Programs	Nutrition Services	Fundraising	Management and General	Capital Fund Activity	Eliminations	Total
	(1)	(2)	(3)						
Revenues, Gains, and Other Support									
Grants and contracts	\$ 18,042,119	\$ 1,765,803	\$ 526,099	\$ -	\$ -	\$ -	\$ -	\$ (45,703)	\$ 20,288,318
Service fees	-	-	2,993,465	1,053,248	-	-	-	(1,036,124)	3,010,589
Contributions and change in value of of beneficial interests in CRTs	500	31,603	-	-	835,505	900	-	-	868,508
Other	-	277,856	2,415	-	119	4,436	-	-	284,826
Total revenues, gains, and other support	<u>18,042,619</u>	<u>2,075,262</u>	<u>3,521,979</u>	<u>1,053,248</u>	<u>835,624</u>	<u>5,336</u>	<u>-</u>	<u>(1,081,827)</u>	<u>24,452,241</u>
Expenses									
Personnel	10,518,047	1,111,130	2,101,783	335,470	143,223	1,615,074	-	-	15,824,727
Other direct costs	3,666,742	678,506	386,143	514,385	64,058	316,669	33,886	(1,081,827)	4,578,562
Occupancy	2,160,536	398,225	358,425	54,054	43,394	315,861	(369,616)	-	2,960,879
Depreciation	-	20,792	-	-	-	22,237	351,090	-	394,119
Interest	-	7,535	-	900	-	4,819	-	-	13,254
Management and general	1,702,628	225,796	404,787	90,481	12,534	(2,436,226)	-	-	-
Total expenses	<u>18,047,953</u>	<u>2,441,984</u>	<u>3,251,138</u>	<u>995,290</u>	<u>263,209</u>	<u>(161,566)</u>	<u>15,360</u>	<u>(1,081,827)</u>	<u>23,771,541</u>
Net Activity	<u>\$ (5,334)</u>	<u>\$ (366,722)</u>	<u>\$ 270,841</u>	<u>\$ 57,958</u>	<u>\$ 572,415</u>	<u>\$ 166,902</u>	<u>\$ (15,360)</u>	<u>\$ -</u>	<u>\$ 680,700</u>

(1) **Child Development Programs:** Head Start, Early Head Start, T&TA, and Preschool for All

(2) **Housing and Supportive Services Programs:** Friend to Friend, San Diego Safe Havens, and Women's and Children's Programs

(3) **Clinical Services Programs:** ACCORD and Para Las Familias

Eliminations represent the reversal of revenue and expenses generated from Nutrition Services provided to Child Development and Housing and Supportive Services programs and Para Las Familias Clinical Services provided to Head Start students.

Revenue and Expenses shown are based on the accounting methods prescribed by the program grants and contracts.