INLAND COUNTIES
REGIONAL CENTER, INC.

FINANCIAL STATEMENTS
WITH INDEPENDENT AUDITOR'S REPORT

JUNE 30, 2018

EADIE + PAYNE LLP

Celebrating a Century of Quality Service

INLAND COUNTIES REGIONAL CENTER, INC.
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JUNE 30, 2018

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Inland Counties Regional Center, Inc.
San Bernardino, California

Report on the Financial Statements

We have audited the accompanying financial statements of Inland Counties Regional Center, Inc. (the Center), a California non-profit corporation, which consist of the statement of financial position as of June 30, 2018 and the related statements of activities, functional expenses, and cash flows for the year then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Center 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 19, 2019 on our consideration of the Center'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 Center's internal control over financial reporting and compliance.

Eadie and Payne LLP

March 19, 2019
Riverside, CA

INLAND COUNTIES REGIONAL CENTER, INC.
STATEMENT OF FINANCIAL POSITION
JUNE 30, 2018

ASSETS

ASSETS		
Cash and cash equivalents	$	24,803,471
Cash held for clients - restricted		1,793,134
Contracts receivable - State of California		16,722,037
Receivable from Intermediate Care Facility vendors		7,645,609
Other receivables		492,028
Investments		561,001
Investments - restricted for Master Trust		22,254,140
Prepaid expenses and other assets		1,592,769
Receivable from State of California - accrued vacation and sick leave benefits		4,644,385
TOTAL ASSETS	$	80,508,574

LIABILITIES AND NET DEFICIT

LIABILITIES		
Accounts payable	$	43,548,588
Accrued payroll		1,157,776
Accrued vacation and other leave benefits		4,644,385
Due to State		3,314,737
Amounts held for clients		1,763,324
Other liabilities		9,174,480
Deferred rent		13,679,573
Master Trust obligations		22,254,140
Obligation for pension benefits		33,169,649
Total liabilities		132,706,652
NET ASSETS (DEFICIT)		
Unrestricted		(52,220,739)
Temporarily restricted		22,661
Total net deficit		(52,198,078)
TOTAL LIABILITIES AND NET DEFICIT	$	80,508,574

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

INLAND COUNTIES REGIONAL CENTER, INC.

STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2018

CHANGE IN UNRESTRICTED NET DEFICITS	
SUPPORT AND REVENUE	
Contracts - State of California	$ 481,295,625
Intermediate Care Facility supplemental services income	19,803,812
Interest and dividend income	262,923
Contributions and grants	539,882
Realized and unrealized gain on investments	19,504
Other income	637,264
Total Unrestricted Revenue and Gains	502,559,010
Net assets released from restriction	17,006
Total support and Revenue	502,576,016
EXPENSES	
Program Services	
Direct client services	471,112,314
Supporting Services	
General and administrative	32,115,222
Fundraising	170,108
Total Expenses	503,397,644
CHANGE IN NET DEFICIT FROM OPERATIONS	(821,628)
Change in defined benefit plan liability	660,208
CHANGE IN UNRESTRICTED NET DEFICITS	(161,420)
CHANGE IN TEMPORARILY RESTRICTED NET ASSETS	
Contributions	12,179
Net assets released from restriction	(17,006)
DECREASE IN TEMPORARILY RESTRICTED NET ASSETS	(4,827)
CHANGE IN NET DEFICIT	(166,247)
NET DEFICIT AT BEGINNING OF YEAR	(52,031,831)
NET DEFICIT AT END OF YEAR	$ (52,198,078)

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

INLAND COUNTIES REGIONAL CENTER, INC.
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2018

	Program Services	Supporting Services			
	Direct Client Services	General and Administrative	Fundraising	Total Supporting Services	Total Expenses
Salaries	$ 29,257,154	$ 14,336,086	$ -	$ 14,336,086	$ 43,593,240
Employee health					
and retirement benefits	10,288,941	3,944,226	-	3,944,226	14,233,167
Payroll taxes	453,706	230,146	-	230,146	683,852
Total Salaries					
and Related Expenses	39,999,801	18,510,458	-	18,510,458	58,510,259
Purchase of Services					
Residential care facilities	132,597,341	-	-	-	132,597,341
Day program	146,926,400	-	-	-	146,926,400
Other purchased services	150,352,956	-	-	-	150,352,956
Communication	-	501,156	-	501,156	501,156
Printing	-	901	-	901	901
Data processing	-	791,912	-	791,912	791,912
Insurance	336,521	247,619	-	247,619	584,140
General expenses	-	775,657	170,108	945,765	945,765
Rent expense	-	8,141,292	-	8,141,292	8,141,292
Equipment and facility					
maintenance	-	81,529	-	81,529	81,529
Equipment purchases	-	465,638	-	465,638	465,638
Board expenses	-	14,390	-	14,390	14,390
Staff travel	899,295	132,440	-	132,440	1,031,735
Legal fees	-	255,712	-	255,712	255,712
Legal settlements		1,795,845	-	1,795,845	1,795,845
Accounting fees	-	90,195	-	90,195	90,195
Consultant fees	-	204,072	-	204,072	204,072
ARCA dues	-	106,406	-	106,406	106,406
TOTAL EXPENSES	$ 471,112,314	$ 32,115,222	$ 170,108	$ 32,285,330	$503,397,644

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

INLAND COUNTIES REGIONAL CENTER, INC.

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED JUNE 30, 2018

CASH FLOWS FROM OPERATING ACTIVITIES	
Change in net deficit	$ (166,247)
Adjustments to reconcile change in net deficit to net cash provided by (used in) operating activities	
Obligation for pension benefits	(660,208)
Deferred rent	1,025,120
Net realized and unrealized investment gains	(19,504)
Dividends reinvested	(12,218)
(Increase) Decrease in Operating Assets	
Cash held for clients	(254,547)
Contracts receivable - State of California	(10,429,881)
Receivable from Intermediate Care Facility vendors	838,287
Other receivables	(117,805)
Investments - Master Trust	152,814
Prepaid expenses	(222,487)
Receivable from State of California - accrued vacation and sick leave benefits	211,515
Receivable from State of California - other post-retirement benefits	13,567,651
Increase (Decrease) in Operating Liabilities	
Accounts payable	4,370,418
Accrued payroll	(193,413)
Due to state	(570,695)
Accrued vacation and sick leave benefits	(211,516)
Obligation for other post-retirement benefits	(13,567,651)
Accounts held for clients	275,779
Master Trust obligations	(152,814)
Other liabilities	1,350,416
Net Cash Provided By (Used In) Operating Activities	(4,786,986)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(4,786,986)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	29,590,457
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 24,803,471

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

NOTE 1 – NATURE OF OPERATIONS

Inland Counties Regional Center, Inc. (IRC or the Center), was incorporated on August 5, 1971 as a California not-for-profit corporation for the purpose of operating Inland Regional Center and related activities. The Center was organized in accordance with the provisions of the Lanterman Developmental Disabilities Services Act (the Act) of the Welfare and Institutions Code of the State of California (the State). In accordance with the Act, the Center provides diagnostic evaluations, client program management, and lifelong planning services for persons with developmental disabilities and their families. The areas served include the Counties of San Bernardino and Riverside.

The Act includes governance provisions regarding the composition of the Center's board of directors. The Act states that the board shall be comprised of individuals with demonstrated interest in, or knowledge of, developmental disabilities, and other relevant characteristics, and requires that a minimum of 50 percent of the governing board be persons with developmental disabilities or their parents or legal guardians; and that no less than 25 percent of the members of the governing board shall be persons with developmental disabilities. In addition, a member of a required advisory committee, composed of persons representing the various categories of providers from which the Center purchases client services, shall serve as a member of the regional center board. To comply with the Act, the Center's board of directors includes persons with developmental disabilities, or their parents or legal guardians, who receive services from the Center and a client service provider of the Center.

The Center contracts with the State Department of Developmental Services (DDS) to operate a regional center for the developmentally disabled and their families. Under the terms of these contracts, the Center's expenses incurred in the performance of the contracts are compensable. Such expenses are billable and reimbursable under the DDS contract when they are paid. For the 2017-2018 contract year, funded expenditures were not to exceed $482,072,197. Actual net expenditures under the regional center contract for the 2017-2018 contracts were $476,437,351 as of June 30, 2018.

As discussed above, the Center operates under contracts with the DDS and is only funded on a cost reimbursement basis as expenses are paid. However, generally accepted accounting principles in the United States of America (GAAP) require the Center to recognize and accrue expenses when incurred, which has resulted in a net deficit for the Center (see Note 5).

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. FINANCIAL STATEMENT PRESENTATION

The Center reports information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted, and permanently restricted. Accordingly, the net assets are classified and reported as described below:

Unrestricted Net Assets – net assets that are neither permanently restricted nor temporarily restricted.

Temporarily Restricted Net Assets – net assets subject to donor-imposed stipulations that may or will be met either by actions of the Center and/or the passage of time. As the restrictions are satisfied, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the accompanying statements of activities as net assets released from restrictions.

Permanently Restricted Net Assets – Net assets subject to donor-imposed restrictions that the corpus be invested in perpetuity and only the income be made available for program operations in accordance with donor restrictions. Such income generally includes interest, dividends, and realized and unrealized earnings from the corpus. As of June 30, 2018, the Center had no permanently restricted net assets.

B. CONTRIBUTIONS

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Contributions received that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset classes. When a donor's stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Permanently restricted contributions and net assets have restrictions stipulated by the donor that the corpus be invested in perpetuity and only the income be made available for operations.

C. USE OF ESTIMATES AND ASSUMPTIONS

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and 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 could differ from those estimates.

Principal areas requiring the use of estimates are assumptions utilized for the obligation for pension benefits and the functional allocation of expenses.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. CASH AND CASH EQUIVALENTS AND CONCENTRATION OF CREDIT RISK

For purposes of the statement of cash flows, the Center considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents. Cash held for clients is presented separately on the statement of financial position.

At June 30, 2018 and at various times during the year, the Center maintained cash balances in its financial institution in excess of federally insured limits. The Center had uninsured cash of $28,750,000 as of June 30, 2018.

E. INVESTMENTS

Investments in marketable securities with readily determinable fair values and all investments in debt securities are stated at their fair values in the statements of financial position. Unrealized gains and losses are included in the accompanying statements of activities, except for the Master Trust investments as described in Note 9.

F. REVENUE RECOGNITION

Receivables from the State are recorded on the accrual method as related reimbursable expenses are incurred. Receivables from Intermediate Care Facility vendors and supplemental services income are recorded on the accrual method as revenue is earned.

G. OTHER RECEIVABLES

Other receivables primarily consist of client support receivables and loans and vendor receivables. Other receivables and loans are recorded when support or loans are granted to clients and when vendor audits have been completed and overpayments have been determined. Other receivables and loans are presented on the statement of the financial position net of an allowance for doubtful accounts and are written off when they are determined to be uncollectible. Management determined there was no allowance necessary as of June 30, 2018.

H. PROPERTY AND EQUIPMENT

Pursuant to the terms of the State of California contract, equipment purchases become the property of the State and, accordingly, are expensed as incurred. For the year ended June 30, 2018, sensitive and nonexpendable equipment purchases totaled $271,877.

The State requires all sensitive and nonexpendable equipment to be tagged and reported annually. Sensitive equipment is defined as having a normal useful life of greater than one year, costing less than $5,000, and being highly desirable or susceptible to theft. Nonexpendable equipment is defined as having a useful life of greater than one year and costing more than $5,000.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

I. ACCRUED VACATION AND SICK LEAVE BENEFITS

The Center has accrued a liability and a receivable from the State for accrued vacation and sick benefits earned. These expenses are compensable costs per the terms of the DDS contract and will become billable and reimbursable under the terms of the DDS contract when they are actually paid to employees.

J. OBLIGATION FOR PENSION BENEFITS

The Center is required to recognize the unfunded status of the California Public Employees' Retirement System (CalPERS) pension plans, measured as the difference between plan assets at fair value and the pension obligation, in the statement of financial position. The Center has accrued a liability for the CalPERS pension. The liability and pension expenses required to be recognized by GAAP are incurred in the performance of the DDS contract and are compensable under the terms of the DDS contract. These expenses become billable and reimbursable when the Center makes its annual contribution to the CalPERS pension plan.

K. DEFERRED RENT

The Center leases its office facilities under a lease agreement that is subject to scheduled increases of rental payments. Total rent expense is amortized evenly over the life of the lease. The deferred rent liability represents the difference between the payments made and the amount expensed since inception of the lease.

L. ALLOCATION OF FUNCTIONAL EXPENSES

Salaries and related expenses, purchase of services, and travel expenses are allocated to the program and supporting services categories on a direct-cost basis. All other operating expenses are allocated to the supporting services category.

M. CONTRIBUTED SERVICES

A number of volunteers have donated significant amounts of their time to the Center and its programs. The donated services are not reflected in the financial statements since these services do not meet the criteria for recognition as contributed services.

N. TAX STATUS

The Center is exempt from federal and state income under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the Revenue and Taxation Code. Consequently, the accompanying financial statements do not include any provisions for income taxes.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

N. TAX STATUS (CONTINUED)

The Center recognizes the financial statement benefit of tax positions, such as a filing status of tax-exempt, only after determining that the relevant tax authority would more likely than not sustain the position following an audit. The Center is subject to potential income tax audits on open tax years by any tax authority in the jurisdiction in which it operated. The statute of limitation for federal and California purposes is generally three and four years, respectively.

O.SUBSEQUENT EVENTS

The Center's management has evaluated subsequent events from the statement of financial position date through March 19, 2019, the date the financial statements were available to be issued for the year ended June 30, 2018, and, determined there are no other items to disclose.

P. NEW ACCOUNTING PRONOUNCEMENTS

Presentation of Financial Statements

Accounting Standards Update 2016-14 *Presentation of Financial Statements for Not-for-Profit Entities* was released on August 18, 2016. Some of the main provisions of this Update include a change to two classes of net assets, rather than the three classes currently required. The two classes would be net assets with donor restrictions and net assets without donor restrictions. Other changes include a variety of enhanced disclosures and the requirement for all NFP's to disclose amounts of expenses by both their natural classification and the functional classification. The amendments in this Update are effective for annual financial statements issued for fiscal years beginning after December 15, 2017. Early application of the amendments in this Update is permitted. The impact of the implementation of the Update on the entity's financial statements has not been assessed at this time.

Revenue Recognition

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity is expected to be entitled for those goods or services. ASU 2014-09 defines a five-step process to achieve this core principle and, in doing so, it is possible more judgement and estimates may be required within the revenue recognition process than required under existing U.S. GAAP, including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each performance obligation. Revenue from contributions and investment income are not impacted by this new standard. ASU 2014-09 will be effective for annual reporting periods beginning after December 15, 2018 using either of two methods: (a) retrospective to each prior reporting period presented with the option to

NOTE 2 – SUMMARYOF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

P. NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

elect certain practical expedients as defined within; or (b) retrospective with the cumulative effect of initially applying ASU 2014-09 recognized at the date of initial application and providing certain additional disclosures as defined in ASU 2014-09. Management has not yet selected a transition method and is currently evaluating the effect that the updated standard will have on the financial statements.

Leases

In February 2016, the FASB issued ASU 2016-02 (Topic 842), which sets out the principles for the recognition, measurement presentation and disclosure of leases for both parties to a contract (i.e. lessees and lessors). The new standard requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase by the lessee. This classification will determine whether lease expense is recognized based on an effective interest method or on a straight-line basis over the term of the lease, respectively. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months. An election can be made to account for leases with a term of 12 months or less similar to existing guidance for operating leases today. The standard is effective for years beginning after December 15, 2019, with early adoption permitted. Management is currently evaluating the effect that the updated standard will have on the financial statements.

NOTE 3 – STATE CONTRACTS

The Center's major source of revenue is from the State of California in the form of reimbursement of qualified expenses. Each fiscal year, the Center enters into a new contract with the State for a specified funding amount subject to the Center's approved budget amendments. Revenue is recognized monthly when a claim for reimbursement of actual expenses is filed with the State. These reimbursement claims are paid either through direct payments to the Center or by applying the claims reimbursements against advances already made to the Center by the State.

As of June 30, 2018, DDS had advanced the Center $70,270,224, under the regional center contracts. For financial statement presentation, to the extent there are claims receivable, these claims have been offset against the advances from the State as follows.

Contract receivables	$ 86,992,261
Contract advances	(70,270,224)
Net contract receivables	$ 16,722,037

The Center has renewed its contract with the State for the fiscal year ending June 30, 2019. The contract provides for initial funding of $513,854,913.

NOTE 3 – STATE CONTRACTS (CONTINUED)

In addition, the Center has recorded a receivable from the State for future compensable costs for accrued vacation and sick leave of $4,644,385 as of June 30, 2018.

The Center's contract with DDS includes various fiscal provisions, which provide that the State retains all rights, title, and interest to the funds provided by DDS and that funds received from the DDS may only be used for the purpose of satisfying claims against or expenses of the Center incurred pursuant to, and in the performance of, its contract with DDS.

NOTE 4 – RECEIVABLE FROM INTERMEDIATE CARE FACILITY

The Centers for Medicare and Medicaid Services (CMS) approved federal financial participation in the funding of day and related transportation services purchased by the Center for consumers who reside in Intermediate Care Facilities (ICFs). CMS agreed that the day and related transportation services are part of the ICF service; however, the federal rules allow for only one provider of the ICF service. Accordingly, all the Medicaid funding for the ICF residents must go through the applicable ICF provider. The Center receives 1.5% administrative fee based on the funds received to cover the additional workload.

DDS has directed the Center to prepare billings for these services on behalf of the ICFs and submit a separate state claim report for these services. The Center reduces the amount of the regular state claim to DDS by the amount of these services.

Reimbursement for these services will be received from the ICFs. The DDS advances the amount according to the state claim to the ICFs. The ICFs are then required to pass on the payments received, as well as the Center's administrative fee, within 30 days of receipt of funds from the State.

NOTE 5 – NET ASSETS (DEFICIT)

The Center uses fund accounting to maintain accountability for various activities. Grants or contributions received in response to specific grant applications or with donor-imposed stipulations that limit the use of the donated assets are considered temporarily restricted.

Temporarily Restricted Net Assets are available for the following purposes:

Temporarily restricted	
Another Way Program	$ 14,669
Staff Training	7,992
	$ 22,661

NOTE 5 – NET ASSETS (DEFICIT) (CONTINUED)

The Unrestricted Net Assets of each fund are generally available for use within that activity. The Regional Center Fund accounts for the funds received from the state contracts. Another Way Program Fund accounts for grants and donations that are received with the understanding and intent that the funds are to be used for the purposes of providing additional funds to support the consumers of the Center, that are not reimbursable from state contracts. The General Fund and Master Trust Fund mainly account for trustee fees and administrative support services income collected for the operation of Master Trust of California (Master Trust).

Unrestricted net assets (deficits) consisted of balances in the following funds:

Unrestricted	
Regional Center Fund	$ (53,408,774)
Another Way Program	402,405
General Fund	689,386
Master Trust	96,244
	$ (52,220,739)

The Regional Center Fund deficit results from expenses recognized under GAAP that are not reimbursable under the state contract until paid in cash. A summary of those expenses are as follows:

DDS Audit Settlement	$ 6,588,703
Deferred rent	13,679,573
Obligation for pension benefits	33,169,649
Other	(29,151)
	$ 53,408,774

NOTE 6 – LINE OF CREDIT

The Center had a revolving loan in the maximum principal amount of $35,000,000, to meet immediate cash needs during the fiscal year. That loan agreement was available to the Center through September 9, 2017.

In February of 2018, the Center executed another revolving loan in the maximum principal amount of $42,000,000, to meet immediate cash needs for the remaining portion of the fiscal year. That note is available to the Center through February 15, 2019.

At June 30, 2018, there were no balances outstanding.

NOTE 7 – CLIENT TRUST FUNDS AND UNEXPENDABLE CLIENT SUPPORT

The Center functions as custodian for the receipt of certain governmental payments and resulting disbursements made to providers on behalf of regional center clients for authorized services. The cash balances are segregated from the operating cash accounts of the Center and are restricted for client support. Since the Center is acting as an agent in processing these transactions, no revenue or expense is reflected on the accompanying statement of activities. The following is a summary of the operating cash activity related to cash held for clients during the year ended June 30, 2018:

Social Security and other client support received	$ 17,782,789
Residential care and other disbursements	17,507,010
Support over disbursements	275,779
Changes to reconcile support over disbursement (disbursements over support) to net cash for support and care activities:	
Decrease in amounts due to the Center	(106,091)
Decrease in receivable from state and federal agencies	84,859
Increase in cash	254,547
Add cash at beginning of year	1,538,587
Cash at end of year	$ 1,793,134

NOTE 8 – MASTER TRUST PROGRAM

A. BACKGROUND

Inland Regional Center, Inc. Master Trust of California (Master Trust) was established in 1978 to receive property from individuals or other entities (trustors), and administered for the benefit of specified developmentally disabled persons (beneficiaries). Property is admitted as a separate trust into the Master Trust upon approval of Inland Counties Regional Center, Inc. Trustee through the Master Trust of California Committee; then by the direction of a court order, or the execution of a Joinder and Trust Agreement by a Trustor.

Distributions from a trust are made in accordance with direction of the Master Trust of California Trust Committee. Termination of a Trust Agreement will occur upon the death of the beneficiary, depletion of the trust assets, according to court order, or according to the trust document.

Only the assets and obligations of the Master Trust are shown on the statement of financial position. Trustee fees charged by the Center are included in the Center's statement of activities.

NOTE 8 – MASTER TRUST PROGRAM (CONTINUED)

B. MASTER TRUST ASSETS

The Master Trust assets classified as restricted investments were as follows:

Investments in marketable securities	
International bonds	$ 423,667
Corporate bonds	2,504,185
Municipal bonds	3,473,998
Government securities	2,386,818
Certificates of deposit	596,273
Equities	2,926,211
Mutual funds	6,896,243
Other assets	
Pooled cash	564,114
Accrued interest receivable	60,302
Other assets	2,422,329
Total Investments - restricted for Master Trust	$ 22,254,140

NOTE 9 – FAIR VALUE OF INVESTMENTS

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

The three levels of the fair value hierarchy are described as follows:

Level 1 – Inputs are unadjusted quoted prices for identical assets or liabilities in active markets that the Center has the ability to access.

Level 2 – Inputs other than quoted prices included in Level 1 that are observable for the assets or liability either directly or indirectly.

Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement in its entirety. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

NOTE 9 – FAIR VALUE OF INVESTMENTS (CONTINUED)
Fair value is determined for each investment security as follows:

International and corporate bonds: Fair values of assets in this security type in markets that are not active are determined using model inputs that are observable either directly or indirectly using historical data from comparable bonds, relative level yield curve, or pricing matrix (Level 2 inputs – income approach).

Municipal bonds and government securities: Fair values of assets in this security type are valued by discounting their underlying assets, combining option pricing and expected cash flows (Level 2 inputs – income approach).

Certificates of deposit and Money Market Funds: Fair values are estimated to approximate deposit account balances, payable on demand, as no discounts for credit quality or liquidity were determined to be applicable (Level 2 inputs – income approach).

Equities and Mutual Funds: Fair values reflect the closing price reported in the active market in which the security is traded (Level 1 inputs)

The following table sets forth by level, with the fair value hierarchy, the Center's investments at fair value as of June 30, 2018:

	Total	Level 1	Level 2
Mutual funds	$ 244,985	$ 244,985	$ -
Money Market funds	188,891	-	188,891
Government Securities	127,125	-	127,125
TOTALS	$ 561,001	$ 244,985	$ 316,016

There were no investments classified as level three.

Investments held at fair value were as follows:	
Another Way Fund	$ 283,124
General Fund	181,632
Master Trust Fund	96,245
Total	$ 561,001

The following summarizes investment income:	
Interest and dividend income	$ 262,923
Realized and unrealized gain	19,504
Net investment income	$ 282,427

NOTE 9 – FAIR VALUE OF INVESTMENTS (CONTINUED)
The following table sets forth by level, within the fair value hierarchy, Master Trust's assets at fair value as of June 30, 2018:

	Cost	Total	Level 1	Level 2
International bonds	$ 432,899	$ 423,667	$ -	$ 423,667
Corporate bonds	2,611,446	2,504,185	-	2,504,185
Municipal bonds	3,563,769	3,473,998	-	3,473,998
Government securities	2,391,240	2,386,818	-	2,386,818
Certificates of deposit	602,491	596,273	-	596,273
Equities	1,991,093	2,926,211	2,926,211	-
Mutual funds	6,538,904	6,896,243	6,896,243	-
	$ 18,131,842	$ 19,207,395	$ 9,822,454	$ 9,384,941

The following summarizes the maturity of investments with stated maturity dates:

	Fair Value	Cost
Due in one year or less	$ 1,860,217	$ 1,859,106
Due in one to five years	6,160,472	6,243,603
Due in more than five years	1,364,252	1,499,136
	$ 9,384,941	$ 9,601,845

NOTE 10 – EMPLOYEE RETIREMENT BENEFITS

A. PERS RETIREMENT PLAN

Since 1998, the Center has participated in the California Public Employees' Retirement System (CalPERS), an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating public employers within the State of California. All eligible employees of the Center are enrolled in CalPERS.

The Public Employee's Retirement Law (Part 3 of the *California Government Code* § 20000, et seq.) establishes benefit provisions for CalPERS. CalPERS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalPERS annual financial report may be obtained from the CalPERS Executive Office, 400 Q Street, Sacramento, California, 95811 and at www.calpers.co.gov.

NOTE 10 – EMPLOYEE RETIREMENT BENEFITS (CONTINUED)

The Center has two retirement plans with CalPERS. One plan is a 2%-at-age-55 formula which closed as of December 31, 2012. All employees hired prior to January 1, 2013 participate in this plan. The second plan is a 2%-at-age-62 formula which was established by the Public Employees' Pension Reform Act of 2013 (PEPRA) and all employees hired on or after January 1, 2013 participate in this plan. The total required employee contributions are 7% of earnings for the 2%-at-age-55 plan and 6.5% of earnings for the 2%-at-age-62 plan.

The excess of the total actuarial accrued liability over the market value of plan assets is called the unfunded actuarial accrued liability. Funding requirements are determined by adding the normal cost and an amortization of the unfunded liability as a level percentage of assumed future payrolls.

The net periodic benefit cost for the year ended June 30, 2018 was $4,110,817.

Benefit obligation and funded status as of June 30, 2018 are as follows:

Change in benefit obligation	
Benefit obligation, beginning of year	189,816,520
Service cost	6,899,375
Interest cost	13,564,891
Assumption change (gain)	(758,940)
Benefits and expenses paid	(5,577,001)
Benefit obligation, end of year	203,944,845
Change in fair value of plan assets	
Fair value of plan assets, beginning of year	155,986,663
Employer contributions	4,771,025
Employee contributions	3,019,318
Benefit payments	(5,577,001)
Net investment income	13,280,249
Administrative and other expenses	(705,058)
Fair value of plan assets, end of year	170,775,196
Plan net pension liability	$ 33,169,649

The assumptions used in the measurement of the benefit obligations at June 30, 2018 are as follows:

Discount rate	7.15%
Expected long-term return on plan assets	7.15%
Rate of compensation increase	2.75%

NOTE 10 – EMPLOYEE RETIREMENT BENEFITS (CONTINUED)

The Plan is reported as a pension trust fund, and is accounted for using the accrual basis of accounting. Contributions to the Plan are recognized in the period in which the contributions are due pursuant to legal requirements. Member contribution rates are defined by law and depend on the respective employer's benefit formulas. Member and employer contribution rates are determined by periodic actuarial valuations. Actuarial valuations are based on the benefit provisions and employee groups of each employer. Benefits and refunds are recognized when currently due and payable in accordance with the terms of each rate plan.

The actual allocations for the pension assets and target allocations by asset class as of June 30, 2018 are as follows:

Asset Class	Current Allocation	Target Allocation
Global equity	48.9%	49.0%
Private equity	7.7%	8.0%
Global debt securities	22.5%	22.0%
Real assets	10.8%	12.0%
Liquidity	3.3%	3.0%
Inflation assets	5.9%	6.0%
Total Plan Level	0.9%	0.0%
	100.0%	100.0%

The Center has $170,775,196 held in a pooled investment account managed by CalPERS. The fair value measurement inputs can be found on the CalPERS Comprehensive Annual Financial Report (CAFR) at www.calpers.co.gov.

B. POST-RETIREMENT BENEFITS OTHER THAN PENSIONS

The Center instituted an unfunded Retiree Medical Reimbursement Plan (RMR Plan) and related trust, effective July 1, 1988. The RMR Plan was established to provide reimbursement of medical expenses for the medical care of each participant and eligible dependents up to their maximum yearly allowance. An employee of the Center who meets certain age and length of service requirements becomes a participant of the RMR Plan upon separation from service. The Center has the right to amend the RMR Plan at any time.

Investments are maintained in an irrevocable trust for the RMR Plan from funds set aside in previous years. The RMR Plan and its obligations will cease to exist once the funds in the RMR Trust are exhausted and the Center will be under no obligation for additional funding of this benefit. The Center did not contribute to the RMR Plan assets for the year ending June 30, 2018.

NOTE 10 – EMPLOYEE RETIREMENT BENEFITS (CONTINUED)

As such, neither the assets set aside nor the liability for the RMR Plan is reported on the statement of financial position.

In August 2018, the board voted to cap the amount of monthly reimbursements from the Plan in order to extend the benefits available from the funds set aside.

The following tables provide a reconciliation of the changes in the RMR plan's benefit obligations and a statement of the funded status as of June 30, 2018:

Change in benefit obligation	
Benefit obligation at beginning of year	$ 15,608,000
Service cost	213,768
Interest cost	475,050
Actuarial gain	(6,403,954)
Benefits paid	(391,864)
Obligation at end of year	$ 9,501,000

Change in plan assets	
Fair value of plan assets at beginning of year	$ 2,040,349
Actual return on plan assets	67,659
Expenses other than benefits	(22,712)
Benefit payments	(391,864)
Fair value of plan assets end of year	$ 1,693,432

NOTE 11 – COMMITMENTS AND CONTINGENCIES

A. COMMITMENTS

The Center is obligated under various operating leases for its office facilities, which expire at various dates through June 2045. The terms of the leases provide for payment of minimum annual rentals, with fixed increases in annual rents. In addition, the leases provide for adjustments relating to changes in property taxes and other operating expenses.

In November 2007, the Center entered into an operating lease agreement with California Housing Foundation to lease office facilities. The original lease term was 32 years and began on September 1, 2009. During the year ended June 30, 2016, the agreement was amended to extend the lease term to end June 30, 2045, and reduce the monthly base rent.

NOTE 11 – COMMITMENTS AND CONTINGENCIES (CONTINUED)

Future minimum facilities lease commitments for the years ending June 30 are as follows:

2019	$ 5,372,333
2020	5,530,386
2021	5,653,676
2022	5,330,319
2023	5,397,179
Thereafter	143,985,949
	$ 171,269,842

B. CONTINGENCIES

DDS Audit / Settlement

In accordance with the terms of the DDS contract, an audit may be performed by an authorized state representative. DDS conducted fiscal compliance audits of the Center for the period of July 1, 2008 through June 30, 2012 and issued its final audit reports with various findings and recommendations that the Center should repay to DDS. The Center entered into an agreement with DDS to settle the disputed audit findings. The provision for the total amount due to DDS is included in other liabilities on the statement of financial position and annual installment payments are beginning August 15, 2019.

DDS issued its final audit reports for July 1, 2012 through June 30, 2014 on April 17, 2018 with various findings and recommendations that the Center should repay to DDS various amounts in a combined total which is immaterial to the financial statements at June 30, 2018. The Center pursued its administrative appeal of the findings and recommendations. It is premature to state if any amount will have to be repaid to DDS. As such, provisions for the repayment have not been recorded on the statement of financial position. The Center has complied with, or is in the process of complying with, other findings and recommendations that are not being appealed and that have no direct fiscal impact on the Center.

On November 19, 2018, DDS issued its final audit reports for July 1, 2014 through June 30, 2015 with various findings and recommendations that have no direct fiscal impact on the Center. The Center has complied with, or is in the process of complying with, findings and recommendations.

DDS conducted fiscal compliance audits of the Center for the periods of July 1, 2015 through June 30, 2016 and July 1, 2016 through June 30, 2017. Final audit reports have not yet been issued. In the opinion of the Center's management, the effect of any findings or recommendations would have no direct fiscal impact on the Center.

NOTE 11 – COMMITMENTS AND CONTINGENCIES (CONTINUED)

DDS Funding

The Center is dependent on continued funding provided by DDS to operate and provide services for its clients. The Center's contract with DDS provides funding for services under the Lanterman Act. In the event that the operations of the Center result in a deficit position at the end of any contract year for client services, DDS may reallocate surplus funds within the Regional Center system to supplement the Center's funding. In the event that the State determines that the Center has insufficient funds to meet its contracted obligations, the State shall make its best efforts to secure additional funding and/or provide the Center with regulatory relief.

The Center is required to reimburse the State for state unemployment insurance benefits paid to its former employees. A trust fund is maintained to fund any reimbursements. As of June 30, 2018, the trust fund balance was approximately $786,000, which is included in other assets on the statement of financial position.

Landlord (Brier II) Settlement Agreements

Upon completion of its current headquarter building, the Center ceased paying rent on vacated office facilities (Brier II) and, in September 2010, the landlord of Brier II filed a complaint for breach of contract. The Center entered into a confidential settlement agreement with the landlord of Brier II during the fiscal year ended June 30, 2011. On December 8, 2014, the landlord for Brier II filed an action against the Center seeking payment of the amounts it claims are owed under the Brier II Settlement Agreement totaling approximately $421,000 plus interest, special damages and punitive damages.

Subsequent to the year ending June 30, 2018, the Center entered into a confidential settlement agreement with the landlord of Brier II. The provision for the total amount due to the landlord of Brier II is included in other liabilities on the statement of financial position.

Other Litigation

The Center is involved as a defendant in other various matters of litigation arising in the normal course of its business. The Center accrues for potential liability arising from proceedings when it is probable that such liability has been incurred and the amount of the loss can be reasonably estimated. In view of the inherent difficulty of predicting the outcome of legal proceedings, the Center cannot state what will be the eventual outcomes of the currently pending matters, the timing of their ultimate resolution or the eventual losses, fines, penalties or impact related to those matters. The Center believes, based upon its current knowledge, after consultation with counsel, that the legal proceedings currently pending against it should not have a material adverse effect on the Center's financial condition. The Center notes, however, that considering the uncertainties involved in such proceedings, there is no assurance of the ultimate resolution of these matters.

NOTE 12 – TRANSACTIONS WITH AFFILIATED ORGANIZATIONS

California Housing Foundation (Foundation or CHF) was formed by members of the Center's board of trustees for the purpose of providing support services for consumers of the Center. The Foundation and the Center have no common board members. The Foundation provides residential facilities for occupancy by persons with developmental disabilities.

The Center entered into an operating lease agreement with the Foundation in November 2007, as discussed in Note 11. Lease payments made to the Foundation amounted to $5,218,383 for the year ended June 30, 2018. These amounts are included within the Supporting Services: general and administrative expenses.

The Centered entered into multiple contracts with the Foundation to provide advance funding for the purchase of homes to be used as residential facilities for its consumers. The advances are secured by promissory notes, bear no interest, require no principal payments, and will be forgiven based on the terms of the agreement. In the event that the contract is breached, the Foundation would be responsible to repay the Center the total amount of the advance with interest at a rate equal to ten percent. During the year ended June 30, 2018, the Center made no advances to the Foundation. As of June 30, 2018, total advances which have not been forgiven were $150,000.

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

Board of Trustees
Inland Counties Regional Center, Inc.
San Bernardino, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, the financial statements of Inland Counties Regional Center, Inc. (the Center), a California nonprofit organization, which comprise the statement of financial position as of June 30, 2018, and the related statement of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 19, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Center'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 financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Center's internal control. Accordingly, we do not express an opinion on the effectiveness of the Center'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.

Certified Public Accountants
& Business Advisors

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Inland Counties Regional Center, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

The Center's Response to Findings

The Center's response to the finding described in the accompanying Schedule of Findings and Responses - Prior Year Finding was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

This report is intended solely for the information of the Board of Trustees, audit committee, management, others within the organization, and federal awarding agencies and pass-through agencies, and is not intended to be and should not be used by anyone other than these specified parties.

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Eadie and Payne LLP

March 19, 2019
Riverside, CA

Current Year Findings: None

Prior Year Findings:

2017-001 – Financial Reporting – (Material Weakness)

Criteria:
Post-retirement plans:
FASB Accounting Standards Codification (ASC) 715-30, "Defined Benefit Plans - Pension," requires entities to recognize the funded status of a defined benefit retirement plan as an asset or liability in its statements of financial position and to recognize changes in that funded status in unrestricted net assets in the year in which the change occurs.

Receivables from State of California
ASC 958-605 discusses transactions in which entities provide resources to not-for-profit (NFP) entities under programs referred to as grants, and specifies that such asset transfers are contributions if the resource providers receive no value in exchange for the assets transferred or if the value received by the resource providers is incidental to the potential public benefit from using the assets transferred. The recognition principles for contributions received are discussed in ASC 958-605 specifies that accounting for contributions depends on whether the transfer of assets, including promises to give, is received by the NFP with donor-imposed conditions, donor-imposed restrictions, or both. Donor-imposed conditions create a barrier that must be overcome before a contribution can be recognized; by definition, a contribution is unconditional.

The FASB ASC glossary defines a donor-imposed condition as a donor-imposed stipulation that specifies a future and uncertain event whose occurrence or failure to occur gives the donor the right of return of the assets or releases the donor from the obligation to transfer assets in the future.

Conditional transfers are not contributions yet; they may become contributions upon the occurrence of one or more future and uncertain events. Because of the uncertainty about whether they will be met, conditions imposed by resource providers may cast doubt on whether the resource provider's intent was to make a contribution, to make a conditional contribution, or to make no contribution. As a result of this uncertainty, donor- imposed conditions should be substantially met by the entity before the receipt of assets is recognized as a contribution or a contribution receivable.

Transfers of assets, including promises to give, on which resource providers have imposed conditions should be recognized as contributions if the likelihood of not meeting the conditions is remote. For example, a stipulation that an annual report must be provided by the donee to receive subsequent annual payments on a multiyear promise is not a condition if the possibility of not meeting that administrative requirement is remote (ASC 958-605-55-16).

FASB ASC 958-605-55-21 discusses promises that become unconditional in stages because they are dependent on several or a series of conditions—milestones—rather than on a single future and uncertain event. Those promises are recognized in increments as each of the conditions is met. Similarly, other promises are conditioned on promises incurring certain qualifying expenses (or costs). Those promises become unconditional and are recognized to the extent that the expenses are incurred. A portion of those contributions should be recognized as revenue as each of those stages is met.

The Center contracts with DDS to operate a regional center for individuals with developmental disabilities and their families. Under the terms of this contract, in Article III: Fiscal Provisions, 4. Payment Provisions, it states, “”In consideration of the services rendered by the Contractor pursuant to this contract, the State shall reimburse the Contractor, for cash expenditures, monthly in arrears”. The contract term is for the period from July 1, 2014, through June 30, 2021.

Condition:
During the course of our audit, we noted that the Center contributes to the California Public Employees' Retirement Systems (CalPERS) for retirement benefits. CalPERS is an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating public entities within California. During prior years, management did not record the unfunded status of the defined benefit retirement plan in its financial statements due to the Plan being incorrectly identified as a multi-employer plan, instead of a multiple employer plan in accordance with ASC 715-30. Under such circumstances, management elected to obtain the most readily available actuarial valuation provided by CalPERS which was prepared in accordance with standards promulgated by the Governmental Accounting Standards Board (GASB). As a result, the Center recorded a net pension liability and related pension expense in the amount of $33,829,857 as of June 30, 2017. However, the Center is a California nonprofit corporation where generally accepted accounting principles (GAAP) is based on the standards promulgated by the Financial Accounting Standards Board (FASB).

In addition, we noted that the Center has an unfunded Retiree Medical Reimbursement Plan (RMR Plan) to provide reimbursement of medical expenses for the medical care of each participant and eligible dependents up to their maximum yearly allowance. The Center recorded a post-retirement medical benefits receivable from the State in the amount of $13,567,651. While the Center has incurred certain qualifying expenses under their contract with the State, required payment provisions represent a donor-imposed condition that must be overcome before a contribution can be recognized as revenue. The receivable does not represent cash expenditures for contributions to the RMR Plan or premium payments. Rather, this amount represents an estimate for the unfunded post-retirement benefit obligation. The payment condition necessary to recognize grant revenue from the State has not been satisfied.

Context:
These findings were identified as part of our review of the types of benefit plans in place during our first year auditing the Center.

Cause:
Management did not record the unfunded projected benefit obligation in prior years due to the Plan being incorrectly identified as a multi-employer plan, instead of a multiple employer plan in accordance with ASC 715-30.

The Center recorded a receivable from the State to reflect the future reimbursement of the unfunded postretirement medical benefit liability. However, such expenses are reimbursed under the state contract only when actually paid by the Center.

Effect:
The amounts by which beginning net assets, net assets, liabilities, expenses, change in net assets, and footnote disclosures of the pension obligation are misstated in relation to the CalPERS pension plan have not been determined.

Regarding the RMR plan, if the $13,567,651 receivable had not been recorded, total assets would decrease by $13,567,651, beginning net assets would decrease by $12,214,319, post-retirement medical plan expense would increase by $1,353,332, and ending net assets would decrease by $13,567,651.

Recommendation:
We recommend that management consider implementing procedures to obtain actuarial valuations of the CalPERS plan in accordance with ASC 715-30 and record the funded status of the defined benefit retirement plan annually. In addition, we recommend that management ensure that receivables recorded represent reimbursements for cash expenditures in accordance with their contract with DDS.

Views of responsible officials and planned corrective actions:
<u>Responses to CalPERS Pension Plan's Recommendation</u>
The Center already has a procedure to obtain actuarial valuations from CalPERS annually. The Center's management disagrees that an implementation of another procedure to obtain an actuarial valuation outside CalPERS Actuary Office is needed for its pension plan. CalPERS Actuary Office has provided the Center an actuarial valuation for financial reporting purpose including an assumed discount rate sensitivity analysis. The analysis includes a hypothetical termination liability for the Center's pension plan in case the Center would terminate its pension plan with CalPERS and need to settle the pension benefits. The FASB ASC 715-30-35-1 requires the use of reasonable approximations to measure the pension obligation, and states that the guideline is intended to specify accounting objectives and results rather than specific computational means of obtaining those results. The guideline states that if estimates, averages, or computational shortcuts can reduce the cost of applying the measurement, their use is appropriate, provided the results are reasonably expected not to be materially different from the results of a detailed application. Should it become necessary; the Center may consider implementing a procedure to verify that the effect of the hypothetical termination liability provided by CalPERS for the Center's CalPERS plan is not materially different from the actuarial valuations in accordance with the FASB ASC 715-30.

The Center's management agrees to record the funded status of the CalPERS pension plan annually. However, the Center's CalPERS pension plan is a unique defined benefit plan. It is one of very few participating agencies subjected to the FASB guidelines; but is required to follow CalPERS funding and contribution methodology every year, based on CalPERS actuarial valuations in accordance with the GASB guidelines. The Center's operation is fully funded by the State of California (the State) through Department of Developmental Services (DDS). Even though it is a 501c(3) Corporation which falls within the FASB guidelines, the Center is allowed to participate in CalPERS due to the fact that CalPERS considers the Center an instrumentality of the State and is a public agency as defined in California Government Code Section 22009, "Public agency means the state, any city, county, city and county, district, municipal or public corporation or any instrumentality…the employees of which constitute one or more coverage groups or retirement system coverage groups." Also, the main audience of the Center's audited financial statements is DDS.

The Center's management is of the opinion that the projected CalPERS unfunded actuarial liability to be recorded should reflect the actual ongoing funding status of the Center with its CalPERS pension plan which is $33,829,857 as of June 30, 2017, calculated from the actuarial valuations provided by CalPERS for financial reporting of the on-going funding pension plan under Public Employees' Retirement Fund (PERF). In the absence of evidence that the Center's CalPERS pension plan will not continue, the Center's management is of the opinion that applying a different assumed discount rate other than the rate used by PERF in a calculation of the Center's projected CalPERS unfunded actuarial liability is not indicative of the future events that will determine the amount and timing of the benefit payments of the Center's CalPERS pension plan. It also does not represent the best estimate of the Center's future event. The FASB ASC 715-30-35-29 and 715-30-35-30 state that explicit estimates or assumptions must be made concerning the future events that will determine the amount and timing of the benefit payments, and each of explicit assumptions individually represents the best estimate of a particular future event. Moreover, the FASB ASC 715-30-35-42 requires an explicit approach to assumptions, and states that all assumptions shall presume that the plan will continue in effect in the absence of evidence that it will not continue.

<u>Responses to the Recommendation of Recording Receivables in The Financial Statements in Accordance with Article III: Fiscal Provisions, 4. Payment Provisions in the DDS Contract</u>

The following provision is in the DDS contracts:

> Article I Standard Terms and Conditions 7. General Provisions of the DDS contract states, "the consideration to be paid Contractor, as provided herein, shall be in compensation for all of Contractor's expenses incurred in the performance hereof,…unless otherwise expressly so provided."

The following provisions are in the accounting standards:

> The FASB ASC 958-605-55-21 "*Not-For-Profit Entities Revenue Recognition*" states, "…other promises are conditioned on promises' incurring certain qualifying expenses (or costs). Those promises become unconditional and are recognized to the extent that the expenses are incurred..."

The FASB ASC 958-605-25-15 "*Not-For-Profit Entities Revenue Recognition*" states, "Absence of a specified time for transfer of cash or other assets, by itself, does not necessarily lead to a determination that a promise to give is ambiguous…Promises to give that are silent about payment terms but otherwise are clearly unconditional shall be accounted for as unconditional promises to give."

The FASB Proposed ASU No. 2017-270, 958-605-25-5C, "*Not-for-Profit Entities (Topic 958)*" states, "If a recipient has broad discretion (for example, the only stipulation is that the transferred assets should be spent for general operating purposes…If a recipient has broad discretion on how to use the assets and the agreement contains no other stipulations that would indicate that a barrier exists, the agreement shall be deemed unconditional," and "The stipulations are related to the purpose of the agreement. This indicator would generally exclude administrative tasks..."

The FASB Proposed ASU No. 2017-270, 958-605-15-6e, "*Not-for-Profit Entities (Topic 958)*" states, "Transfers of assets (typically from a government entity) that are part of an existing exchange transaction between a recipient and an identified customer…In those instances, an entity shall apply the applicable guidance (for example, Topic 606 (ASU No. 2014-09) on revenue from contracts with customers)."

The FASB Accounting Standards Update (ASU) No. 2014-09, "*Revenue from Contracts with Customers*" -BC20, "*Basis For Recognizing Revenue*" states, "…revenue should be recognized only when an entity transfers a promised good or service to a customer, thereby satisfying a performance obligation in the contract. That transfer results in revenue recognition because upon satisfying a performance obligation an entity no longer has that obligation to provide the good or service."

The FASB ASU No. 2014-09, "*Revenue from Contracts with Customers*" -BC36, "*The Parties Have Approved the Contract and Are Committed to Perform Their Respective Obligations*" states, "the Boards decided that the parties should be committed to performing their respective obligations under the contract. However, the Boards decided that an entity and a customer would not always need to be committed to fulfilling all of their respective rights and obligations for a contract to meet the guidance…The Boards noted that requiring all of the rights and obligations to be fulfilled would have inappropriately resulted in no recognition of revenue for some contracts in which the parties are substantially committed to the contract."

The FASB ASU No. 2014-09, "*Revenue from Contracts with Customers*" -BC168, "*Input Methods*" states, "Input methods recognize revenue on the basis of an entity's efforts or inputs toward satisfying a performance obligation (for example, resources consumed, labor hours expended, costs incurred, time elapsed, or machine hours used) relative to the total expected inputs to satisfy the performance obligation.

The FASB ASU No. 2014-09, *"Revenue from Contracts with Customers*" -BC180, "*Reasonable Measures of Progress*" states, "The Boards also concluded that in cases in which an entity cannot reasonably measure its progress toward complete satisfaction of a performance obligation, but nevertheless expects eventually to recover the costs incurred in satisfying the performance obligation, the entity should recognize at least some amount of revenue to reflect the fact that it is making progress in satisfying the performance obligation. Consequently, the Boards decided that in those cases, an entity should recognize revenue for the satisfaction of the performance obligation only to the extent of the costs incurred. (That method is consistent with previous revenue recognition guidance in both IFRS and U.S. GAAP for measuring progress.)…"

The FASB ASU No. 2014-09 "*Revenue from Contracts with Customers*" -BC323, "*Relationship between Contract Assets and Receivables*" states, "In many cases, that contract asset is an unconditional right to consideration—a receivable—because only the passage of time is required before payment of that consideration is due…"

The FASB ASU No. 2014-09 "*Revenue from Contracts with Customers*" -BC326, "*Relationship between Contract Assets and Receivables*" states, "…an entity will have an unconditional right to consideration, even though the entity may be required to refund some or all of that consideration in the future. In those cases, the possible obligation to refund consideration in the future will not affect the entity's present right to be entitled to the gross amount of consideration…"

The Center contracts with the State Department of Developmental Services (DDS) to operate a regional center in accordance with the provisions of the Lanterman Developmental Disabilities Services Act of the Welfare and Institutions Code. The Center is substantially committed to the contract to provide services for the developmentally disabled (identified consumers) and their families in two Counties of the State. The DDS compensates the Center for the services provided to the identified consumers and their families, and also provides a general operating budget for the Center to run the regional center. Under the terms of the DDS contracts, the Center's expenses incurred in the performance of the contracts are compensable by the DDS. Such expenses are billable and reimbursable under the DDS contract when they are paid.

The receivable from the State of compensable costs incurred totaling $13,567,651 as of June 30, 2017 was an equal amount of the accumulated net post-retirement benefit costs incurred since the plan started in 1988. The projected net post-retirement benefit obligation is an actuarial valuation based from census data of eligible active and retired employees of the Center in which their services were already provided in accordance with the DDS contracts. The Center is not required to pay in full the plan obligation but could contribute to the plan in its sole discretion. Further, the RMR Plan has a provision that the plan ceases to exist once all the assets of the plan are fully spent. Hence, it is a self-liquidating plan. The Center did not contribute to the RMR Plan for the year ending June 30, 2017.

The Center has a promise to compensation or right to consideration from the DDS when services were provided according to the DDS contract. The Center's management is of the opinion that the promise to compensation or right to consideration becomes unconditional when the Center satisfies its performance obligation and compensable expenses are incurred under the terms of the DDS contracts. The Center's management is of the opinion that the payment provisions are not a condition required to realize a receivable to the extent of the incurred costs.

The payment provisions describe the required procedures for the Center to claim and get reimbursements after the Center has paid for the services in performance of the DDS contracts. The Center's management is of the opinion that these are administrative tasks unrelated for the Center to carry out the purpose of the DDS contract (performance of services) and has nothing to do in determining whether the Center has a promise to compensation or right to consideration for the Center to realize a receivable.

Current year status:
The prior year findings have been resolved. Management obtained an FASB valuation for the pension plan as of June 30, 2018. The Center has not recorded an asset or liability for the retiree medical reimbursement plan as of June 30, 2018.