

**HOFFMAN HOMES, INC.**  
**FINANCIAL STATEMENTS AND**  
**INDEPENDENT AUDITORS' REPORT**  
**JUNE 30, 2016**

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## INDEPENDENT AUDITORS' REPORT

The Board of Directors  
Hoffman Homes, Inc.

We have audited the accompanying statement of financial position of Hoffman Homes, Inc. (a nonprofit organization) as of June 30, 2016, and the related statements of activities, functional expenses and cash flows for the year then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

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

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 Hoffman Homes, Inc. as of June 30, 2016, and the changes in their net assets and their cash flows for the year then ended.

*Stambaugh Ness, PC*

York, Pennsylvania  
December 21, 2016

A Professional Corporation

**HOFFMAN HOMES, INC.**  
**STATEMENT OF FINANCIAL POSITION**  
**JUNE 30, 2016**

**ASSETS**

<b>CURRENT ASSETS</b>	
Cash	\$ 6,084
Accounts receivable	1,216,419
Prepaid expenses	5,818
Accounts receivable - other	<u>2,237</u>
Total current assets	1,230,558
<b>RESTRICTED CASH</b>	98,952
<b>INVESTMENTS</b>	4,254,503
<b>PROPERTY, PLANT AND EQUIPMENT</b>	
Property, plant and equipment - at cost	14,658,793
Less: accumulated depreciation	<u>(11,513,539)</u>
Net property, plant and equipment	3,145,254
<b>OTHER ASSETS</b>	
Beneficial interest in perpetual trusts	<u>2,528,761</u>
<b>TOTAL ASSETS</b>	<u><u>\$ 11,258,028</u></u>

**LIABILITIES AND NET ASSETS**

<b>CURRENT LIABILITIES</b>	
Line of credit	\$ 1,868,169
Cash overdraft	90,143
Accounts payable	192,738
Accrued payroll and related benefits	458,260
Accrued interest	1,462
Current portion of long-term debt	934,657
Interest rate swap liability	15,280
Escrow accounts payable	<u>882</u>
Total current liabilities	3,561,591
<b>LONG-TERM LIABILITIES</b>	
Long-term debt - net of current portion	1,240,102
Pension liability	<u>2,462,878</u>
Total long-term liabilities	<u>3,702,980</u>
<b>TOTAL LIABILITIES</b>	7,264,571
<b>NET ASSETS</b>	
Unrestricted:	
Undesignated	444,705
Temporarily restricted	185,099
Permanently restricted	<u>3,363,653</u>
<b>TOTAL NET ASSETS</b>	<u>3,993,457</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u><u>\$ 11,258,028</u></u>

See accompanying notes.

**HOFFMAN HOMES, INC.**  
**STATEMENT OF ACTIVITIES**  
**YEAR ENDED JUNE 30, 2016**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>REVENUES AND GAINS</b>				
Fees for services	\$ 8,304,894	\$ -	\$ -	\$ 8,304,894
Food reimbursement	159,016	-	-	159,016
Miscellaneous income	144,777	-	-	144,777
Contributions	251,794	25,000	-	276,794
Bequests	34,935	-	-	34,935
Irrevocable trust fund income	162,363	-	-	162,363
Investment gain (loss)	(209,547)	-	-	(209,547)
Education income	1,942,192	-	-	1,942,192
Changes in beneficial interest in perpetual trusts	-	-	(209,418)	(209,418)
Net assets released from restrictions:				
Restrictions satisfied by fulfilling purpose	39,182	(39,182)	-	-
<b>Total revenues and gains</b>	<b>10,829,606</b>	<b>(14,182)</b>	<b>(209,418)</b>	<b>10,606,006</b>
<b>EXPENSES AND LOSSES</b>				
Administration	1,620,963	-	-	1,620,963
Clinical services	6,045,484	-	-	6,045,484
Culinary	426,030	-	-	426,030
Development	183,377	-	-	183,377
Healthcare	1,233,295	-	-	1,233,295
Operations	990,096	-	-	990,096
Education (Academy)	951,476	-	-	951,476
<b>Total expenses and losses</b>	<b>11,450,721</b>	<b>-</b>	<b>-</b>	<b>11,450,721</b>
<b>OTHER CREDITS AND CHARGES</b>				
Defined benefit plan changes other than net periodic pension expense	(1,134,896)	-	-	(1,134,896)
Unrealized gain on interest rate swaps	12,128	-	-	12,128
<b>Total other credits and charges</b>	<b>(1,122,768)</b>	<b>-</b>	<b>-</b>	<b>(1,122,768)</b>
<b>DECREASE IN NET ASSETS</b>	<b>(1,743,883)</b>	<b>(14,182)</b>	<b>(209,418)</b>	<b>(1,967,483)</b>
<b>NET ASSETS</b>				
Beginning of year - originally stated	2,042,303	199,281	3,573,071	5,814,655
Prior period adjustment	146,285	-	-	146,285
Beginning of year - restated	2,188,588	199,281	3,573,071	5,960,940
End of year	<u>\$ 444,705</u>	<u>\$ 185,099</u>	<u>\$ 3,363,653</u>	<u>\$ 3,993,457</u>

See accompanying notes.

**HOFFMAN HOMES, INC.**  
**STATEMENT OF FUNCTIONAL EXPENSES**  
**YEAR ENDED JUNE 30, 2016**

	<u>Administration</u>	<u>Clinical Services</u>	<u>Culinary</u>	<u>Development</u>	<u>Healthcare</u>	<u>Operations</u>	<u>Education (Academy)</u>	<u>Total</u>
Salaries	\$ 653,887	\$ 4,484,850	\$ 84,008	\$ 102,829	\$ 569,831	\$ 235,470	\$ 740,637	\$ 6,871,512
Employee benefits*	175,089	1,241,128	26,688	7,988	139,082	59,085	116,581	1,765,641
Contracted services***	103,041	545	1,223	-	445,460	6,683	60,513	617,465
Depreciation expense	402,104	-	-	-	-	-	-	402,104
Utilities**	35,470	7,411	-	-	62	302,641	-	345,584
Food and food service supplies	-	-	312,739	-	-	-	-	312,739
Bad debt expense	-	223,060	-	-	-	-	-	223,060
Insurance - property and liability	-	-	-	-	-	188,566	-	188,566
Housekeeping & sanitation	1,369	3,410	-	65	2,071	89,855	1,040	97,810
Maintenance & repairs	355	110	1,372	1,046	-	87,858	1,847	92,588
Interest expense	91,642	-	-	-	-	-	-	91,642
Staff development/recruitment	24,096	47,897	-	2,116	256	113	1,784	76,262
Medical/dental supplies & expense	-	-	-	-	74,829	-	-	74,829
Development	13,299	-	-	42,792	17	-	301	56,409
Miscellaneous expense	45,420	7,323	-	9,735	-	-	543	60,016
Office supplies/equipment	9,837	18,762	-	1,682	1,687	2,486	16,269	50,723
Lease expense	36,090	-	-	-	-	-	-	36,090
Computer expenses	12,027	3,072	-	1,753	-	3,058	11,800	31,710
Travel/vehicle expense	175	1,839	-	325	-	14,281	161	16,781
Postage	17,062	-	-	-	-	-	-	17,062
Advertising	-	-	-	13,046	-	-	-	13,046
Behavior management	-	6,077	-	-	-	-	-	6,077
	<u>\$ 1,620,963</u>	<u>\$ 6,045,484</u>	<u>\$ 426,030</u>	<u>\$ 183,377</u>	<u>\$ 1,233,295</u>	<u>\$ 990,096</u>	<u>\$ 951,476</u>	<u>\$ 11,447,716</u>

\* Includes Social Security, Unemployment Tax, Workers Compensation, Medical, Life, Dental, Pension and Employee Assistance Program.

\*\* Includes telephone, electricity, fuel oil, water & sewer, cable TV and propane gas.

\*\*\* Includes legal, accounting, psychiatric and other professional services.

See accompanying notes.

**HOFFMAN HOMES, INC.**  
**STATEMENT OF CASH FLOWS**  
**YEAR ENDED JUNE 30, 2016**

<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>	
Change in net assets	\$ (1,967,483)
Adjustments to reconcile change in net assets to net cash from operating activities:	
Depreciation expense	402,104
Bad debt expense	223,060
Realized and unrealized loss on investments	405,493
Unrealized gain on interest rate swaps	(12,128)
Changes in beneficial interest in perpetual trusts	209,418
Defined benefit plan changes other than net periodic pension expense	1,135,356
(Increase) decrease in:	
Accounts receivable	(377,954)
Accounts receivable - other	10,092
Prepaid expenses	144,527
Restricted cash	31,548
Increase (decrease) in:	
Accounts payable	73,735
Accrued payroll and related benefits	(175,458)
Accrued interest	(493)
Escrow accounts payable	191
	<hr/>
Net cash provided by operating activities	102,008
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>	
Purchase of property, plant and equipment	(91,615)
Purchase of investments	(1,031,568)
Proceeds from sale of investments	1,091,098
	<hr/>
Net cash used in investing activities	(32,085)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>	
Net change in line of credit	(511,094)
Proceeds from long-term debt	700,000
Net change in cash overdraft	(55,442)
Payments on long-term debt	(225,278)
	<hr/>
Net cash used in financing activities	(91,814)
<b>NET CHANGE IN CASH</b>	<hr/> <b>(21,891)</b>
Cash at beginning of year	<hr/> 27,975
Cash at end of year	<hr/> <b>\$ 6,084</b> <hr/>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>	
Cash payments for interest	<hr/> <b>\$ 91,642</b> <hr/>

See accompanying notes.

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE A - SIGNIFICANT ACCOUNTING POLICIES**

Nature of Business

Hoffman Homes, Inc. ("Organization") is a private, not-for-profit, Pennsylvania Corporation related to the United Church of Christ.

The purpose of Hoffman Homes, Inc. is to provide comprehensive psychiatric care, treatment, and education to emotionally and behaviorally troubled children and their families. Hoffman Homes, Inc. is committed to providing services that are cost effective and responsive to the unique needs of each child, always in close cooperation with the parents/guardians, referring agencies, case management organizations, school systems, and funding sources. Hoffman Homes, Inc. grants credit to the agencies that place the youth in their facilities. The agencies that purchase services from Hoffman Homes, Inc. are located in Pennsylvania.

During fiscal year 2015-2016, Hoffman Homes, Inc. received approval from the Pennsylvania State Board of Academic Schools to establish and operate Hoffman Academy ("Academy"). The Academy provides differentiated instruction to meet the diverse needs of students with complex behavioral concerns. All programs are operated according to the guidelines established by PDE. Students have their needs assessed and then receive instruction designed specifically to their academic level.

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 that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Basis of Accounting

The financial statements of Hoffman Homes, Inc. have been prepared on the accrual basis of accounting and, accordingly, reflect all significant receivables, payables and other liabilities.

Basis of Presentation

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board in its Accounting Standards Codification 958, *Financial Statements of Not-for-Profit Organizations*. Under ASC 958, Hoffman Homes, Inc. is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets and permanently restricted net assets.



**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE A - SIGNIFICANT ACCOUNTING POLICIES** - continued

Cash and Cash Equivalents

For purposes of the statement of cash flows, Hoffman Homes, Inc. considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents. There were no cash equivalents as of June 30, 2016.

Restricted Cash

These amounts represent cash that has been restricted by donors, as well as by Board designation.

Accounts Receivable

Accounts receivable balances are reviewed by management monthly. Any account over sixty days past due based on contractual terms is analyzed. Based upon management's review and assessment an allowance for uncollectable accounts receivables in the amount of \$65,000 was recorded. Account balances generally are written off when management judges such balances uncollectible.

Donated Assets

Donated marketable securities and other non-cash donations are recorded as contributions at their estimated fair values at the date of donation.

Promises to Give

Unconditional promises to give are recognized as revenues or gains in the period the promise is made. The promise is an asset, decrease of a liability, or an expense depending on the form of the promise made. Conditional promises to give are recognized when the conditions on which they depend on are substantially met.

Restricted and Unrestricted Revenue and Support

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions. All donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when the 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.

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE A - SIGNIFICANT ACCOUNTING POLICIES** - continued

Beneficial Interest in Perpetual Trusts

Hoffman Homes, Inc. recognizes its interests in irrevocable perpetual trust agreements of which it has been named an income beneficiary. The assets reported in the Statement of Financial Position represent Hoffman Homes, Inc.'s beneficial interest in the fair market value of the irrevocable perpetual trusts. Upon Hoffman Homes, Inc. being named an income beneficiary of an irrevocable perpetual trust, the initial interest is recognized as permanently restricted bequest income. Hoffman Homes, Inc. also recognizes changes in the fair market value of its beneficial interests in perpetual trusts in the permanently restricted section of the Statement of Activities.

Income Tax Status

Hoffman Homes, Inc. is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. Section 501(c)(3) defines the exempt organization as being "organized and operated for religious, charitable, scientific, testing for public safety, literacy or educational purposes, or for the prevention of cruelty to children or animals." In addition, Hoffman Homes, Inc. qualifies for the charitable contribution deduction under Section 170(b)(1)(a) and has been classified as an organization that is not a private foundation under Section 509(a)(2). Accordingly, no provision for federal or state income taxes has been recorded in the financial statements. Adjustments, if any, for uncertain tax positions would be recorded as a liability. The Organization is no longer subject to tax examinations by tax authorities for years before 2012.

The Organization would also recognize accruals for interest and penalties related to uncertain tax positions in its interest expense.

Allocation of Functional Expenses

Expenses reported on Hoffman Homes, Inc.'s Statement of Functional Expenses are allocated directly to their functional categories.

Concentrations of Credit Risk

The financial instruments that potentially subject Hoffman Homes, Inc. to credit risk consist primarily of cash, investments and accounts receivable that represent amounts due for per diem fees from managed care organizations, government agencies, and private pay clients. Hoffman Homes, Inc. maintains its cash deposits and investments with various financial institutions where the account balances may at times exceed FDIC insured limits.

At June 30, 2016, accounts receivable from two managed care organizations and one school district accounted for 69% of total accounts receivable. These organizations provided 91% of total fee for service revenue during the year ended June 30, 2016.

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE A - SIGNIFICANT ACCOUNTING POLICIES** - continued

Advertising Costs

Advertising costs are expensed as incurred. Advertising costs totaled \$13,046 for the year ended June 30, 2016.

Fair Value of Financial Instruments

Accounting Standards Codification 820, *Fair Value Measurements*, provides a framework for measuring fair value under accounting principles generally accepted in the United States of America. Accounting Standards Codification 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Accounting Standards Codification 820 requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs.

Accounting Standards Codification 820 also establishes a fair value hierarchy, which prioritizes the valuation inputs into three broad levels. Financial assets and liabilities valued using Level 1 inputs are based on unadjusted quoted market prices within active markets. Financial assets and liabilities valued using Level 2 inputs are based primarily on quoted prices for similar assets or liabilities in active or inactive markets. Financial assets and liabilities using Level 3 inputs are primarily valued using management's assumptions about the assumptions market participants would utilize in pricing the asset or liability.

The estimated fair values of the Organization's financial instruments for the fiscal year ended June 30, 2016 are as follows:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Mutual funds	\$2,534,193	\$ -	\$ -	\$2,534,193
Mutual funds - fixed income	1,348,069	-	-	1,348,069
Common stock	207,697	-	-	207,697
Real estate investment trusts	-	-	164,544	164,544
Beneficial interests in perpetual trusts	-	-	2,528,761	2,528,761
Derivative instruments - swap	-	(15,280)	-	(15,280)
	<u>\$4,089,959</u>	<u>\$ (15,280)</u>	<u>\$2,693,305</u>	<u>\$6,767,984</u>

The change in Level 3 fair value inputs is as follows:

Beginning balance	\$2,995,259
Unrealized loss	<u>(301,954)</u>
Ending balance	<u>\$2,693,305</u>

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE A - SIGNIFICANT ACCOUNTING POLICIES** - continued

Property, Plant and Equipment

Hoffman Homes, Inc. capitalizes all expenditures for property and equipment with a useful life greater than one year and a cost in excess of \$1,000. Purchased property and equipment are carried at cost. Depreciation is computed using primarily the straight-line method over the estimated useful lives of the respective assets.

Equipment, new construction costs, furnishings, building improvements, land, and vehicles are stated at cost. Expenditures for renewals and improvements that significantly add to productive capacity or extend the useful life of the asset are capitalized. Maintenance and repairs are charged to expense as incurred. When depreciable property is retired or otherwise disposed of, the cost and related accumulated depreciation are eliminated from the accounts, and the resulting gain or loss is reflected in the statement of activities.

Donations of property and equipment are recorded as contributions at their estimated fair value on the date received. Hoffman Homes, Inc. does not imply time restrictions with respect to donated property and equipment.

Compensated Absences

Employees of Hoffman Homes, Inc. are entitled to paid time off and sick bank days. It is Hoffman Homes, Inc.'s policy to pay accrued paid time off when an employee resigns with proper notice. Sick bank days are only available for use during an extended illness and are not paid out upon separation of employment. The liability resulting from these policies has been recorded in the financial statements.

Revenue Recognition

Grant revenue which is determined to be an exchange transaction, is classified as unrestricted revenue or deferred revenue, as appropriate, when received or receivable. Such grant revenue is not deemed to be a contribution, since the proceeds thereof are used to pursue objectives of the grantor.

Grant revenue which is deemed to be a contribution, is classified as temporarily restricted revenue when received or receivable. Such grant revenue is not in respect of exchange transactions, since the proceeds are non-reciprocal, unconditional and voluntary.

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received which are restricted 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. However, if a restriction is fulfilled in the same time period in which the contribution is received, Hoffman Homes, Inc. reports the support as unrestricted.

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE B - OVERVIEW OF RESULTS OF OPERATIONS**

The Organization's financial statements have been presented on the basis that it is a going concern, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business.

The Organization incurred operating losses of approximately \$840,000 during fiscal year ending June 30, 2016 and approximately \$1,200,000 for the year ending June 30, 2015, thereby creating significant liquidity concerns.

Management continues to explore means to improve operational efficiency, explore new revenue streams and endowment development.

During fiscal 2015-16, the Organization was approved by the State Board of Private Academic Schools to begin offering classes with their private academic license and commenced the operation of Hoffman Academy. The Organization looks to this as an opportunity to enhance their overall program offerings and revenue streams. Although, due to existing state reimbursement procedures the Academy may not receive full reimbursement for certain students until fiscal year 2016-17.

**NOTE C - IRREVOCABLE TRUST FUND INCOME**

Hoffman Homes, Inc. receives income from several irrevocable trusts. The following provides income distributions from the listed trusts that are attributed to the year ended June 30, 2016:

<u>Trustee</u>	<u>Trust</u>	<u>Trust Income</u>
Fulton Financial Advisors	u/w John Gerber	\$ 64,512
BB&T Trust	u/w L. Crawford	21,893
Wilmington Trust	Ervin & Lottie Spangler	18,068
PNC Advisors	Katherine H. Glatfelter	13,247
Merrill Lynch	Frances Mowery	11,648
BB&T Trust	u/w F. Crawford	11,409
Wilmington Trust	Stewart & Florence Wolf Bortner	8,462
Trust Corp. America	Various	2,972
Fulton Bank	Ammon & Dorothy Patrick	2,782
PNC Advisors	Emma Duttera	2,128
Wilmington Trust	u/w Jacob Schnader	1,585
Wilmington Trust	u/w Mamie B. Bush	1,114
Wilmington Trust	Elmira Quickel	1,083
Trust Corp. America	u/w Estella M. Yingling	436
Merrill Lynch	Paul & Margie Smith	413
Wilmington Trust	u/w Howard W. Sheeler	384
Wilmington Trust	Jessie Omwake	<u>227</u>
		<u>\$162,363</u>

**HOFFMAN HOMES, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2016**

**NOTE D - PROPERTY, PLANT AND EQUIPMENT**

Below is a summary of the activity in the property, plant and equipment accounts as of June 30, 2016:

	<u>July 1, 2015</u>	<u>Additions (Deletions)</u>	<u>June 30, 2016</u>
Buildings	\$ 10,155,023	\$ 56,933	\$ 10,211,956
Furniture and fixtures	1,694,225	-	1,694,225
Equipment	1,223,690	34,682	1,258,372
Vehicles	238,507	-	238,507
Land improvements	907,840	-	907,840
Water tower	103,893	-	103,893
Sewage treatment plants	<u>244,000</u>	<u>-</u>	<u>244,000</u>
	14,567,178	91,615	14,658,793
Less: accumulated depreciation	<u>(11,111,435)</u>	<u>(402,104)</u>	<u>(11,513,539)</u>
Net property, plant and equipment	<u>\$ 3,455,743</u>	<u>\$ (310,489)</u>	<u>\$ 3,145,254</u>

**NOTE E - TEMPORARILY RESTRICTED NET ASSETS**

As of June 30, 2016, temporarily restricted net assets are available as follows:

Purpose restrictions:	
Housing construction or upgrades	\$ 100,728
Building/equipment repairs	59,067
Recreation center	5,000
Outpatient program development	<u>1,000</u>
Total purpose restrictions	165,795
Time restrictions:	
Bequest to be held in trust for 50 years	<u>19,304</u>
Total time restrictions	<u>19,304</u>
	<u>\$ 185,099</u>

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE F - PERMANENTLY RESTRICTED NET ASSETS**

Permanently restricted net assets consist of the beneficial interest in perpetual trusts and bequests received by Hoffman Homes, Inc. in which the donor has restricted the use of the principal portion of the gift.

As of June 30, 2016, permanently restricted net assets are restricted to investment in perpetuity, the income from which is expendable to support:

Scholarships	\$ 7,785
Unrestricted uses	<u>3,355,868</u>
	<u>\$ 3,363,653</u>

**NOTE G - OPERATING LEASES**

Hoffman Homes, Inc. leases equipment and vehicles under numerous operating leases with various expiration dates.

Minimum future rental payments under non-cancelable operating leases having remaining terms in excess of one year as of June 30, 2016, are as follows:

<u>June 30,</u>	
2017	\$ 29,844
2018	26,974
2019	26,400
2020	26,400
2021	<u>26,400</u>
	<u>\$136,018</u>

Rental expense amounted to \$36,090 in 2016.

**NOTE H - INVESTMENTS**

Investments consist of the following as of June 30, 2016:

Cash	\$ 95,354
Common stock	207,697
Mutual funds and alternative investments	2,438,839
Mutual funds - fixed income	1,348,069
Real estate investment trusts	<u>164,544</u>
	<u>\$ 4,254,503</u>

**HOFFMAN HOMES, INC.**  
**NOTES TO FINANCIAL STATEMENTS**  
**JUNE 30, 2016**

**NOTE H - INVESTMENTS - continued**

The following is a schedule of the components of investment gain as shown in the statement of activities for the year ended June 30, 2016:

Interest and dividends	\$ 220,852
Unrealized losses	(424,384)
Investment fees	(24,906)
Realized gains	<u>18,891</u>
	<u><u>\$ (209,547)</u></u>

**NOTE I - ESCROW ACCOUNTS PAYABLE**

The youths' individual account balances are maintained by the Hoffman Homes, Inc.'s business office. This money may be withdrawn for personal needs during a youth's stay. At the time of discharge, the total amount held in escrow for the youth is returned to the youth, along with interest accrued on the deposit. As of June 30, 2016, escrow accounts payable were \$882.

**NOTE J - LINE OF CREDIT**

Hoffman Homes, Inc. has a \$3,000,000 line of credit with PNC Bank, of which \$1,868,169 was used as of June 30, 2016; however, as of this date, they also had cash overdrafts in the amount of \$90,143, therefore, the outstanding amount on the line of credit at June 30, 2016 is \$1,958,312. The bank advances on the line of credit are due on demand and carry an interest rate of 30 Day LIBOR + 1.75%, which was 2.275% at June 30, 2016. The line of credit is secured by all assets of Hoffman Homes, Inc.

**NOTE K - LONG-TERM DEBT**

Long-term debt consisted of the following at June 30, 2016:

Term note payable to bank of \$1,464,154, payable in monthly principal installments of approximately \$18,500, plus interest at LIBOR plus 1.85% or 2.30% at June 30, 2016, due in March 2022, secured by all business assets.

Term note payable to bank of \$700,000, interest only through maturity of October 31, 2016, at 30 Day LIBOR + 1.75%.

Term note payable to bank in monthly principal and interest payments of \$330, due in March 2022, secured by Ford F-250.

Total term debt outstanding	\$ 2,174,759
Less current portion	<u>(934,657)</u>
Long-term portion	<u><u>\$ 1,240,102</u></u>



**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE K - LONG-TERM DEBT** - continued

Future maturities of long-term debt are as follows as of June 30, 2016:

2017	\$ 934,657
2018	244,029
2019	253,375
2020	260,525
2021	260,525
Thereafter	<u>221,648</u>
	<u>\$ 2,174,759</u>

Terms of the Organization's loan agreements provide for certain financial covenants. The Organization did not meet the Debt Service covenant for the year ending June 30, 2016. A waiver has been requested.

**NOTE L - CONTINGENT LIABILITIES**

Hoffman Homes, Inc. participates in several grant programs with funding from federal and state sources. These programs are subject to compliance audits by the grantors or their representatives. The audits of some of these programs for and including the year ended June 30, 2016, have not yet been conducted. Accordingly, Hoffman Homes, Inc.'s compliance with applicable grant requirements will be established at some future date. The amount, if any, of expenditures which may be disallowed by the grantor agencies cannot be determined at this time.

**NOTE M - RETIREMENT PLANS**

Tax Deferred Annuity Plan

Hoffman Homes, Inc. maintains a tax deferred annuity plan under Internal Revenue Code Section 403(b), covering eligible full-time employees.

Defined Benefit Plan

Hoffman Homes, Inc. has a defined benefit pension plan covering substantially all of its employees that were employed as of June 30, 2003. The benefits are based on years of service and the employee's compensation during the last year of employment. Hoffman Homes, Inc.'s funding policy is to contribute the minimum required deposit, as defined in Section 412 of the Internal Revenue Code, throughout the plan year which will keep the Plan from developing an accumulated funding deficiency.

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE M - RETIREMENT PLANS - continued**

Defined Benefit Plan - continued

Hoffman Homes, Inc. adopted a plan amendment which suspended all future benefit accruals in the defined benefit plan as of June 30, 2003. Hoffman Homes, Inc. established a defined contribution 403(b) plan for employee and employer contributions to be made after June 30, 2003.

Periodic benefit cost included in the Statement of Activities for 2016 include the following components:

Interest cost on the projected benefit obligation	\$297,028
Expected return on assets held in the plan	(385,050)
Recognized net actuarial loss	<u>88,482</u>
	<u>\$ 460</u>

Other disclosure information:

Measurement date	June 30, 2016
Projected benefit obligation	\$ 7,856,462
Accumulated benefit obligation	7,856,462
Fair value of plan assets	5,393,584
Funded status	(2,462,878)
Contributions	-
Benefits paid	271,306

Pension plan assets are carried at fair value based upon quoted market prices, a Level 1 fair value input and are made up of equity securities (\$1,672,012), mutual funds (\$3,667,637) and cash/money funds (\$53,935).

Contributions to the plan expected to be made during fiscal year ending June 30, 2017: \$ -

Components of expected net periodic pension cost for fiscal year ending June 30, 2017:

Interest cost	\$273,349
Return on assets	(366,597)
Amortization of net loss or (gain) from earlier periods	<u>166,387</u>
	<u>\$ 73,139</u>

Total expense for June 30, 2016 was \$77,547, comprised of \$460 of net periodic pension expense, \$50,013 for professional actuarial services and \$27,074 for Pension Benefit Guaranty Corporation (PBGC) premiums.

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE M - RETIREMENT PLANS** - continued

Defined Benefit Plan - continued

Items not recognized as a component of net periodic pension cost:

Net loss	\$ 1,134,896
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Assumptions:

Weighted average discount rate	3.55%
Weighted average compensation increase	0.00%
Expected long-term rate of return on assets	7.00%

Change in pension liability:

Net loss	\$ 1,223,378
Amortization of gain	<u>(88,482)</u>
	<u>\$ 1,134,896</u>

Estimated future fiscal year benefit payments:

2017	\$ 298,758
2018	304,495
2019	304,437
2020	327,859
2021	347,203
2022 - 2026	1,990,036

Allocation of plan assets at fair value:

Equity	31%
Mutual funds	68%
Other	1%

Investment policies and strategies:

The investment policy for plans sponsored by Hoffman Homes, Inc. is based on ERISA standards for prudent investing. This policy seeks to maximize return while limiting risk, which is achieved through a balanced portfolio of equity and fixed income investments, as well as alternative asset classes. Within each asset class, a diversified mix of individual securities and bonds is selected. Equity allocations are targeted between 50% and 75% of the portfolio, with the remainder in fixed income investments and a small portion in alternative asset classes such as real estate. Asset manager performance is reviewed at least once every six months and benchmarked against the peer universe for the given investment style.

**HOFFMAN HOMES, INC.**  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2016

**NOTE M - RETIREMENT PLANS** - continued

Defined Benefit Plan - continued

Determination of expected long-term rate of return on assets:

Hoffman Homes, Inc. has examined the historical benchmarks for returns in each asset class in its portfolio and, based on the target asset mix, has developed a weighted average expected return for the portfolio as a whole, taking into consideration forecasts of long-term expected inflation rates of 2.0% - 3.5%.

**NOTE N - DERIVATIVE INSTRUMENTS**

During the fiscal year ending June 30, 2012, Hoffman Homes, Inc. entered into a forward start interest rate swap to hedge the interest rate risk associated with a loan in the amount of \$2,350,000 at a fixed-rate. The loan was issued during the year ending June 30, 2012. The swap was effective on March 9, 2012, and terminates on March 9, 2022.

Hoffman Homes, Inc. is paying interest related to the swap agreement. The swap is issued at market terms so that it had no fair value at its inception. The carrying amount of the swap has been adjusted to the fair value at the end of the year. The swap agreement had a negative fair value of \$(15,280) at June 30, 2016. This amount is included in liabilities on the statement of financial position and the change in fair value shown as an unrealized gain on the statement of activities, affecting the changes in unrestricted net assets.

The fair market value of Hoffman Homes, Inc.'s financial assets and liabilities is determined using forecasted levels of LIBOR and the notional value noted above, and is considered a Level 2 input in accordance with Accounting Standards Codification 820, *Fair Value Measurements*. Level 2 inputs are based on quoted market prices for similar assets or liabilities within active markets. Management determined that the carrying value of the swap was materially consistent with the fair market value at June 30, 2016.

**NOTE O - PRIOR PERIOD ADJUSTMENT**

A prior period adjustment was required due to a change in how the organization was reconciling its bank account in regards to restricted cash and its cash overdraft. This resulted in a positive adjustment to the beginning net assets in the amount of \$146,285.

**NOTE P - SUBSEQUENT EVENTS**

Management has evaluated subsequent events through the date of the Independent Auditors' Report, the date the financial statements were available to be issued.