



STEPS, INC.

**Financial Statements
For the years ended
June 30, 2017 and 2016**

Not-for-Profit Corporation
501c(3)





STEPS, INC.

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Report of Independent Auditors

To the Board of Directors of
STEPS, Inc.
Farmville, Virginia

Report on the Financial Statements

We have audited the accompanying financial statements of STEPS, Inc. (the "Corporation"), which comprise the statements of financial position as of June 30, 2017 and 2016, and the related statements of activities, functional expenses, and cash flows for the years 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 audits. We conducted our audits 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 audits 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 the 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 STEPS, Inc. as of June 30, 2017 and 2016, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.





Other Matters

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards, as required by Title 2, U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 18, 2018, on our consideration of the Corporation'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 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 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 STEP Inc.'s internal control over financial reporting and compliance.

A handwritten signature in blue ink that reads "Davidson Doyle Hittner, LLP".

Lynchburg, Virginia
January 18, 2018





STEPS, INC.
Statements of Financial Position
June 30, 2017 and 2016

	Assets	
	2017	2016
Current assets		
Cash and equivalents	\$ 99,259	\$ 87,915
Accounts receivable	272,767	310,180
Prepaid expenses	53,546	38,826
Total current assets	<u>425,572</u>	<u>436,921</u>
Property and equipment		
Land	15,852	15,852
Building	2,696,294	2,518,184
Leasehold improvements	765,041	175,368
Furniture and equipment	291,437	263,099
Classroom furniture	91,325	-
Playground equipment	24,363	-
Transportation	907,264	662,823
	<u>4,791,576</u>	<u>3,635,326</u>
Less accumulated depreciation	<u>2,017,984</u>	<u>1,839,127</u>
Total property and equipment	<u>2,773,592</u>	<u>1,796,199</u>
Total assets	<u>\$ 3,199,164</u>	<u>\$ 2,233,120</u>
	Liabilities and Net Assets	
Current liabilities		
Accounts payable	\$ 227,332	\$ 306,620
Line of credit	-	386,236
Current maturities of notes payable	53,420	240,237
Accrued compensation expenses and other liabilities	133,126	91,216
Total current liabilities	<u>413,878</u>	<u>1,024,309</u>
Long-term liabilities		
Long-term debt, net of current maturities and unamortized debt issuance costs	<u>507,972</u>	<u>-</u>
Total long-term liabilities	<u>507,972</u>	<u>-</u>
Total liabilities	<u>921,850</u>	<u>1,024,309</u>
Net assets		
Unrestricted	1,266,629	117,525
Temporarily restricted	1,010,685	1,091,286
Total net assets	<u>2,277,314</u>	<u>1,208,811</u>
Total liabilities and net assets	<u>\$ 3,199,164</u>	<u>\$ 2,233,120</u>





STEPS, INC.
Statement of Activities
Year ended June 30, 2017

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	2017		
	Unrestricted	Temporarily Restricted	Total
Revenues, gains (losses), and other support			
Grant revenue	\$ 138,084	\$ 5,041,894	\$ 5,179,978
Business services	395,220	-	395,220
Production revenue	230,998	-	230,998
In-kind revenue	213,304	-	213,304
Contributions - direct	46,460	-	46,460
Rental income	27,585	-	27,585
Miscellaneous	2,217	-	2,217
Interest income	19	-	19
Special events, net of expense of \$12,847	(308)	-	(308)
Assets released from restrictions	5,122,495	(5,122,495)	-
Total revenues, gains (losses), and other support	<u>6,176,074</u>	<u>(80,601)</u>	<u>6,095,473</u>
Operating expenses			
Program services	4,489,613	-	4,489,613
Administrative and general	261,396	-	261,396
Fundraising	35,460	-	35,460
Total operating expenses	<u>4,786,469</u>	<u>-</u>	<u>4,786,469</u>
Increase (decrease) in net operating assets	1,389,605	(80,601)	1,309,004
Other expenses			
Depreciation	240,501	-	240,501
Total other expenses	<u>240,501</u>	<u>-</u>	<u>240,501</u>
Increase (decrease) in net assets	1,149,104	(80,601)	1,068,503
Net assets at beginning of year	<u>117,525</u>	<u>1,091,286</u>	<u>1,208,811</u>
Net assets at end of year	\$ <u>1,266,629</u>	\$ <u>1,010,685</u>	\$ <u>2,277,314</u>



See notes to financial statements.



STEPS, INC.
Statement of Activities
Year ended June 30, 2016

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	2016		
	Unrestricted	Temporarily Restricted	Total
Revenues, gains (losses), and other support			
Grant revenue	\$ 143,084	\$ 3,469,890	\$ 3,612,974
Business services	393,347	-	393,347
In-kind revenue	335,622	-	335,622
Production revenue	310,486	-	310,486
Debt forgiveness	130,000	-	130,000
Contributions - direct	94,361	-	94,361
Rental income	28,690	-	28,690
Special events, net of expense of \$6,348	7,972	-	7,972
Miscellaneous	5,190	-	5,190
Interest income	170	-	170
Assets released from restrictions	3,483,224	(3,483,224)	-
Total revenues, gains (losses), and other support	<u>4,932,146</u>	<u>(13,334)</u>	<u>4,918,812</u>
Operating expenses			
Program services	3,880,658	-	3,880,658
Administrative and general	216,170	-	216,170
Fundraising	37,696	-	37,696
Total operating expenses	<u>4,134,524</u>	<u>-</u>	<u>4,134,524</u>
Increase (decrease) in net operating assets	797,622	(13,334)	784,288
Other expenses			
Depreciation	192,183	-	192,183
Total other expenses	<u>192,183</u>	<u>-</u>	<u>192,183</u>
Increase (decrease) in net assets	605,439	(13,334)	592,105
Net assets at beginning of year	(487,914)	1,104,620	616,706
Net assets at end of year	\$ <u>117,525</u>	\$ <u>1,091,286</u>	\$ <u>1,208,811</u>





STEPS, INC.
Statement of Functional Expenses
Year ended June 30, 2017

	2017			
	<u>Program Services</u>	<u>Administrative and General</u>	<u>Fundraising</u>	<u>Total</u>
Salaries and wages	\$ 2,455,404	\$ 74,043	\$ 19,298	\$ 2,548,745
Client assistance	389,500	-	-	389,500
Payroll taxes	324,681	1,290	2,487	328,458
Repairs and maintenance	227,980	17,935	-	245,915
Utilities	189,224	35,268	-	224,492
Rent	180,604	31,871	-	212,475
Office supplies	150,490	15,442	-	165,932
Employee benefits	124,877	497	956	126,330
Auto expenses	107,256	7,044	-	114,300
Professional services	68,013	17,827	-	85,840
Insurance	77,893	4,901	-	82,794
Telephone	69,028	12,531	-	81,559
Conferences	65,682	7,358	-	73,040
Miscellaneous	19,219	10,508	-	29,727
Interest	17,682	9,667	-	27,349
Dues and membership fees	8,570	6,209	-	14,779
Marketing and seminars	-	-	12,719	12,719
Staff development	8,155	4,458	-	12,613
Printing	5,355	4,547	-	9,902
Total expenses	<u>\$ 4,489,613</u>	<u>\$ 261,396</u>	<u>\$ 35,460</u>	<u>\$ 4,786,469</u>





STEPS, INC.
Statement of Functional Expenses
Year ended June 30, 2016

	2016			
	<u>Program Services</u>	<u>Administrative and General</u>	<u>Fundraising</u>	<u>Total</u>
Salaries and wages	\$ 2,303,300	\$ 48,626	\$ 24,744	\$ 2,376,670
Client assistance	358,771	-	-	358,771
Payroll taxes	277,241	3,165	2,950	283,356
Repairs and maintenance	175,184	12,009	-	187,193
Rent	145,140	29,728	-	174,868
Utilities	118,235	24,434	-	142,669
Auto expenses	134,387	6,846	-	141,233
Employee benefits	100,774	1,150	1,072	102,996
Insurance	64,995	9,833	-	74,828
Professional services	59,706	14,931	-	74,637
Telephone	41,735	8,583	-	50,318
Office supplies	35,686	11,445	-	47,131
Interest	16,867	13,661	-	30,528
Miscellaneous	15,257	12,359	-	27,616
Conferences	14,319	5,445	-	19,764
Dues and membership fees	9,692	3,016	-	12,708
Staff development	6,969	5,644	-	12,613
Marketing and seminars	-	-	8,930	8,930
Printing	2,400	5,295	-	7,695
Total expenses	<u>\$ 3,880,658</u>	<u>\$ 216,170</u>	<u>\$ 37,696</u>	<u>\$ 4,134,524</u>





STEPS, INC.
Statements of Cash Flows
Years ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities		
Increase (decrease) in net assets	\$ 1,068,503	\$ 592,105
Adjustments to reconcile increase in net assets to net cash provided by operating activities		
Depreciation	240,501	192,183
Amortization, included in interest expense	1,635	-
Non-cash transfer of assets	-	(184,409)
Discount for prepayment of debt	-	(130,000)
(Increase) decrease in operating assets:		
Accounts receivable	37,413	(131,585)
Prepaid expenses	(14,720)	(17,158)
Increase (decrease) in operating liabilities:		
Accounts payable	(79,288)	60,150
Accrued payroll and taxes	41,910	36,791
Net cash provided by operating activities	<u>1,295,954</u>	<u>418,077</u>
Cash flows from investing activities		
Purchase of fixed assets	(<u>1,217,894</u>)	(<u>285,244</u>)
Net cash used in investing activities	(<u>1,217,894</u>)	(<u>285,244</u>)
Cash flows from financing activities		
Principal payments on line of credit	(386,236)	(18,700)
Proceeds on notes payable	625,000	-
Loan costs incurred	(9,813)	-
Principal payments on notes payable	(<u>295,667</u>)	(<u>114,451</u>)
Net cash used in financing activities	(<u>66,716</u>)	(<u>133,151</u>)
Net increase (decrease) in cash	11,344	(318)
Cash at beginning of year	<u>87,915</u>	<u>88,233</u>
Cash at end of year	\$ <u>99,259</u>	\$ <u>87,915</u>
Supplemental disclosure of cash flow information:		
Interest paid	\$ <u>27,349</u>	\$ <u>30,528</u>





STEPS, INC.
Notes to Financial Statements
June 30, 2017 and 2016

Note 1 – Nature of the corporation and summary of significant accounting policies

Nature of the Corporation

STEPS, Inc. (the "Corporation") is an extremely diversified Community Action Agency which delivers services to those in need. Services are delivered under Four Pillars of Service: **Workforce Development** – STEPS provides job training and employment opportunities to citizens living with disabilities, individuals who want to exit the welfare system and senior citizens living below the poverty level; **Economic Development** - STEPS is a major employer in our region and in addition operates three (3) commercial lines of business: secure document shredding, operation of a regional recycling center, and industrial sewing; **Housing** - STEPS provides services to alleviate and/or prevent homelessness and serves as a partner to Dominion Power in their EnergyShare program, meeting heating and cooling needs; **Education** - STEPS works with students with disabilities who are transitioning from the public education system and operates Head Start and Early Head Start services.

Basis of financial statement presentation

The Corporation's financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. The financial statements follow the recommendations of the Financial Accounting Standards Board in its Statement of Financial Accounting Standards, FASB ASC 958, *NPO Entities*. In this Statement, the Corporation 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.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. When a restriction expires (that is, when a 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.

Accordingly, net assets of the Corporation and changes therein are classified and reported as follows:

Unrestricted net assets - Net assets that are not subject to donor-imposed stipulations. Board designated restrictions are disclosed separately.

Temporarily restricted net assets - Net assets subject to donor-imposed stipulations that may or will be met, either by action of the Corporation and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Permanently restricted net assets - Net assets subject to donor-imposed restrictions that the assets be maintained permanently by the Corporation. Generally, the donors of these assets permit the Corporation to use all or part of the income earned on any related net assets for general purposes.

Contributions

In accordance with FASB ASC 958, *NPO Entities*, contributions are recognized when the donor makes an unconditional promise to give and are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor-imposed restrictions. Contributions that are restricted by the donor are reported as increases in unrestricted net assets if the restrictions expire during the fiscal year in which the contributions are recognized.

Promises to give

Unconditional promises to give are recognized as contribution revenue in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Promises to give are recorded at net realizable value if expected to be collected in one year and at fair value if expected to be collected in more than one year. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

Income recognition

Income is derived from several activities including job training and transportation, grants, contributions and sales of manufactured products. Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted net assets depending on the absence or existence and nature of any donor restrictions.





STEPS, INC.
Notes to Financial Statements
June 30, 2017 and 2016

Note 1 – Nature of the corporation and summary of significant accounting policies (continued)

Accounts receivable

Accounts receivable consist of trade accounts receivable and are stated at invoiced amount. Credit is extended to customers after an evaluation of the customer's financial condition and generally collateral is not required. It is the Organization's policy to charge off uncollectible accounts receivable when management determines the receivable will not be collected. The Organization's main customer is the Federal Government and therefore there has not been a need for an allowance for doubtful accounts.

Property and equipment

Property and equipment acquisitions are recorded at cost, or fair value if contributed. Depreciation is computed using the straight-line method over the estimated useful lives as follows:

<u>Classification</u>	<u>Estimated Useful Life</u>
Building	15-39 years
Leasehold improvements	15 years
Furniture and equipment	5-10 years

Expenses for maintenance and repairs are charged against revenues in the year the cost is incurred. Expenditures for additions and major improvements are capitalized and depreciated. The Organization capitalizes all property and equipment with a cost of \$500 or more. Cost and accumulated depreciation are removed from the accounts for property sold or retired, and any resulting gain or loss is included in the statement of activities.

Donated services

No amounts have been reflected in the financial statements for donated services. The Organization generally pays for services requiring specific expertise. However, many individuals volunteer their time and perform a variety of tasks that assist the Organization with specific assistance programs, campaign solicitations, and various committee assignments.

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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as 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.

Income taxes

No provision for income taxes has been made in the financial statements because the Corporation is a not-for-profit corporation as described in Section 501 (c)(3) of the Internal Revenue Code (IRC) and is exempt from federal income taxes on related income pursuant to Section 501(a) of the IRC. The Corporation has also been classified as an entity that is not a private foundation within the meaning of Section 509(a) of the IRC.

The Financial Accounting Standards Board ASC 740-10 prescribes a comprehensive model for how an organization should measure, recognize, present, and disclose in its financial statements uncertain tax positions that an organization has taken or expects to take on a tax return. The Corporation has analyzed tax positions taken for filing with the Internal Revenue Service and all state jurisdictions where it operates. The Corporation believes that income tax filing positions will be sustained upon examination and does not anticipate any adjustments that would result in a material adverse affect on the Corporation's financial condition, results of operations or cash flows. Accordingly, the Corporation has not recorded any reserves, or related accruals for interest and penalties for uncertain income tax positions at June 30, 2017. Fiscal years ending on or after June 30, 2014 remain subject to examination by federal and state tax authorities.





STEPS, INC.
Notes to Financial Statements
June 30, 2017 and 2016

Note 1 – Nature of the corporation and summary of significant accounting policies (continued)

Functional expenses

The costs of providing the Corporation’s various programs and supporting services have been summarized on a functional basis in the accompanying statement of functional expenses. The functional expenses of the various programs and supporting services include those costs directly attributable to the specific program as well as an allocation of supporting service expenditures, which, in the estimation of management, are indirectly attributable to the programs.

Advertising

The Corporation expenses advertising costs as incurred. Such expenses are shown in the statements of activities.

Shipping and handling revenue, fees and costs

The Corporation classifies amounts billed for shipping and handling as revenue in accordance with FASB ASC 605-45-50-2, *Shipping and Handling Fees and Costs*. Shipping and handling fees and costs are included in operating expenses.

New accounting pronouncements

In April 2015, the FASB issued ASU 2015-03, *Interest – Imputation of Interest (Subtopic 835-10), Simplifying the Presentation of Debt Issuance Costs*. The simplify the presentation of debt issuance costs, the amendment requires that debt issuance costs related to a recognized debt liability be presented on the balance sheet as a direct deduction from that debt liability, consistent with the presentation of a debt discount. The ASU is effective for financial statements issued for fiscal years beginning after December 15, 2015 and should be applied retrospectively. Management has adopted ASU 2015-03.

On August 18, 2016, FASB issued ASU No. 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities (Topic 958)*. The new standards are effective for annual financial statements issued for fiscal years beginning after December 15, 2017. Early application of the amendments in the ASU is permitted. The ASU, which is the first phase of a two-phase project, makes significant changes in seven areas: net asset classes, liquidity and availability of resources, classification and disclosure of underwater endowment funds, expense reporting, statement of cash flows, investment return, and release of restrictions on capital assets. The Organization has elected not to apply the amendments early.

Note 2 - Cash balances

The Corporation places its cash and cash equivalents on deposit with financial institutions in the United States. The Federal Deposit Insurance Corporation (FDIC) insured limit is currently \$250,000. During the year, the Corporation from time to time may have had amounts on deposit in excess of the federally insured limits. Management does not feel there is a risk of loss with these deposits.

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

Note 3 - Property and depreciation

A summary of depreciation expense for the year ended June 30, 2017 and accumulated depreciation at June 30, 2017 is as follows:

	Accumulated Depreciation 2017	Depreciation Expense 2017
Buildings	\$ 1,256,332	\$ 98,188
Furniture and equipment	259,656	24,012
Transportation	453,450	70,202
Classroom furniture and equipment	15,587	15,586
Playground equipment	4,060	4,060
Leasehold improvements	28,899	28,453
	<u>\$ 2,017,984</u>	<u>\$ 240,501</u>





STEPS, INC.
Notes to Financial Statements
June 30, 2017 and 2016

Note 3 – Property and depreciation (continued)

A summary of depreciation expense for the year ended June 30, 2016 and accumulated depreciation at June 30, 2016 is as follows:

	Accumulated Depreciation 2016	Depreciation Expense 2016
Buildings	\$ 1,158,282	\$ 92,464
Furniture and equipment	235,505	34,360
Transportation	444,893	64,912
Leasehold improvements	447	447
	<u>\$ 1,839,127</u>	<u>\$ 192,183</u>

Depreciation expense for the year ended June 30, 2017 and 2016, was \$240,501 and \$192,183, respectively.

Note 4 – Line of credit

In 2016, the Corporation renewed a line of credit agreement with a bank, which permits short-term borrowings up to \$413,000 with interest at 5.5% per year. The agreement is collateralized by real estate of the Corporation. The agreement matured January 10, 2017. The outstanding balance as of June 30, 2017 and 2016 was \$-0- and \$386,236, respectively.

Note 5 – Notes payable

The Corporation's notes payable at June 30, 2017 and 2016 were as follows:

	Maturity	2017	2016
Union First loan, payable \$6,497 monthly including interest at 4.5% with balance due upon maturity, secured by property	2021	\$ 569,570	\$ -
Navajo Air loan, payable \$2,388 monthly with no interest, interest imputed at AFR .95%, discount if prepaid	2023	-	205,375
Diversitex loan, payable \$2,615 monthly with no interest, interest imputed at AFR .95%, less unconditional future promise to give per Diversitex Settlement, discount if prepaid	2023	-	164,862
		569,570	370,237
Discounts for early payment		-	(130,000)
		569,570	240,237
Less portion due currently		53,420	240,237
Long-term debt		516,150	-
Unamortized debt issuance costs		(8,178)	-
Net Long-term debt		<u>\$ 507,972</u>	<u>\$ -</u>





STEPS, INC.
Notes to Financial Statements
June 30, 2017 and 2016

Note 5 – Notes payable (continued)

Aggregate principal payments on long-term debt are scheduled as follows:

Year Ending	Amount
2017	\$ 53,420
2018	55,875
2019	58,442
2020	61,127
2021	340,706
Thereafter	-
	\$ 569,570

Note 6 – Restricted use covenants

The county of Prince Edward has secured a \$400,000 deed of trust against the Craddock Terry building for twenty years which will remain unsatisfied as long as STEPS, Inc. does not sell the property. Should STEPS, Inc. sell the property within the twenty year period ending March 21, 2021, the full \$400,000 deed of trust will be due. At the end of the twenty year holding period, the deed of trust will be released without obligation if STEPS, Inc. still owns the building. The book value of this building is accounted for in the financial statements as temporarily restricted funds.

The county of Prince Edward secured grant money through the Department of Mines, Minerals, and Energy for STEPS, Inc. in the amount of \$1,009,002 to replace the roof and HVAC system in the Craddock Terry Building. Because the building is encumbered by the county until March 21, 2021, the book value of the assets used to improve the building are also accounted for in the financial statements as temporarily restricted funds. After 2021, the remaining book value of these assets will no longer be temporarily restricted.

Note 7 – Rental income

The Corporation received rental income of \$27,585 and \$28,690 from other agencies under non-cancellable operating lease arrangements for space in the Corporation's building for the year ended June 30, 2017 and 2016, respectively. The lease includes an annual rent escalation clause. The following is a schedule of future minimum rentals to be received under the lease as of June 30, 2017:

Year Ending	Amount
2018	\$ 8,579
Thereafter	-
	\$ 8,579

Note 8 – Operating leases

The Corporation leases equipment and real estate under operating lease agreements. The lease agreements expire at various dates. Rental expenses for these leases totaled \$212,475 and \$174,868 for the years ended June 30, 2017 and 2016. Future minimum lease payments under operating leases that have remaining terms in excess of one year as of June 30, 2017 are as follows:

Year Ending	Amount
2018	\$ 56,400
2019	56,400
2020	56,400
2021	47,400
2022	18,045
Thereafter	181,008
	\$ 415,653





STEPS, INC.
Notes to Financial Statements
June 30, 2017 and 2016

Note 9 – In-kind contributions

The Corporation received various donated goods and services during the year. In-kind contributions totaled \$213,304 and \$335,622 for the years ended June 30, 2017 and 2016. This included \$-0- and \$184,409 in donated vehicles and \$147,582 and \$151,213 in donated rent for various Head Start facilities.

Note 10 – Temporarily restricted net assets

The Corporation received grant revenue from several federal and state agencies. These programs are accounted for in the financial statements as temporarily restricted funds.

Temporarily restricted net assets of June 30, 2017 and 2016 consisted of the following:

	<u>2017</u>	<u>2016</u>
Temporarily Restricted		
Craddock Terry building deed of trust	\$ 400,000	\$ 400,000
Prince Edward building improvements grant	1,009,002	1,009,002
Less: Accumulated depreciation	<u>(398,317)</u>	<u>(317,716)</u>
Total temporarily restricted	<u>\$ 1,010,685</u>	<u>\$ 1,091,286</u>

Note 11 – Defined contribution retirement plan

The Corporation has a 403(b) plan covering substantially all full time employees. The Corporation made no contributions to the Plan during the years ended June 30, 2017 and 2016.

Note 12 - Major customers

The Corporation derived 64% and 46% of its revenue in 2017 and 2016 from the U.S. Department of Health and Human Services related to the Head Start grant.

Note 13 - Subsequent Events

The Corporation has evaluated subsequent events through January 18, 2018, the date the financial statements were available to be issued.





Supplemental Information





STEPS, INC.
Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2017

Federal Grantor/Pass-through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-through Entity Identifying Number	Federal Expenditures
U.S. Department of Health and Human Services			
Head Start Program	93.600	03CH010185	\$ 3,911,487
Pass-through from:			
Virginia Department of Social Services			
Community Services Block Grant	93.569	CVS-16-001-24	284,916
Temporary Assistance for Needy Families	93.558		<u>109,650</u>
Total U.S. Department of Health and Human Services			<u>4,306,053</u>
U.S. Department of Housing and Urban Development			
Pass-through from:			
Virginia Department of Housing and Community Development			
Virginia Housing Support Program	14.231		<u>21,100</u>
Total U.S. Department of Housing and Urban Development			<u>21,100</u>
U.S. Department of Agriculture			
Child and Adult Care Food Program	10.558		<u>167,212</u>
Total U.S. Department of Agriculture			<u>167,212</u>
U.S. Department of Labor			
Pass-through from:			
Virginia Department for Aging and Rehabilitative Services			
Senior Community Service Employment Program	17.235	16-055	<u>243,838</u>
Total U.S. Department of Labor			<u>243,838</u>
Total expenditures of federal awards			<u>\$ 4,738,203</u>

See accompanying notes to schedule of expenditures of federal awards.





STEPS, INC.
Notes to Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2017

Note 1 – Basis of Presentation

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of STEPS, Inc. under programs of the federal government for the year ended June 30, 2017. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Because the Schedule presents only a selected portion of the operations of STEPS, Inc., it is not intended to and does not present the financial position, changes in net assets or cash flows of STEPS, Inc.

Note 2 – Summary of Significant Accounting Policies

Expenditures

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in Uniform Guidance wherein certain types of expenditures are not allowable or are limited as to reimbursement.

Pass-through

Pass-through entity identifying numbers are presented where available.

Note 3 – Indirect Cost Rate

The Organization has elected not to use the ten percent de minimis indirect cost rate allowed under the Uniform Guidance.





**Independent Auditor's 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***

To the Board of Directors of
STEPS, Inc.
Farmville, Virginia

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of STEPS, Inc., which comprise the statement of financial position as of June 30, 2017 and the related statements of activities and cash flows and for the year ended, and the related notes to the financial statements, and have issued our report thereon dated January 18, 2018.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered STEPS, Inc.'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 STEPS, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of STEPS, Inc.'s internal control.

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether STEPS, 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 or other matters that are required to be reported under *Government Auditing Standards*.





Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the 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.

Davidson Doyle & Hittler, LLP

Lynchburg, Virginia
January 18, 2018





Independent Auditor's Report on Compliance for Each Major Program and on Internal Control over Compliance Required by the Uniform Guidance

To the Board of Directors of
STEPS, Inc.
Farmville, Virginia

Report on Compliance for Each Major Federal Program

We have audited STEPS, Inc.'s compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of STEPS, Inc.'s major federal programs for the year ended June 30, 2017. STEPS, Inc.'s major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of STEPS, Inc.'s major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about STEPS, Inc.'s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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

Basis for Qualified Opinion on Head Start Program

As described in the accompanying schedule of findings and questioned costs, STEPS did not comply with the requirements regarding CFDA 93.600 Head Start as described in finding number 2017-01 for Special Tests and Provisions. Compliance with such requirements is necessary, in our opinion, for STEPS to comply with the requirements applicable to that program.





Opinion on Each Major Federal Program

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, STEPS, Inc. complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2017.

Report on Internal Control over Compliance

Management of STEPS, Inc. is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered STEPS, Inc.'s internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of STEPS, Inc.'s internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the financial statements of STEPS, Inc. as of and for the year ended June 30, 2017, and have issued our report thereon dated January 18, 2018, which contained an unmodified opinion on those financial statements. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditure of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

A handwritten signature in blue ink that reads "Davidson Doyle & Hittor, LLP".

Lynchburg, Virginia
January 18, 2018





STEPS, INC.
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2017

Section I- Summary of Auditor’s Results

Financial Statements

- The auditor's report expresses an unmodified opinion on whether the financial statements of STEPS, Inc. were prepared in accordance with accounting principles generally accepted in the United States of America.
- During the audit of the financial statements, no significant deficiencies or material weaknesses are disclosed or reported.
- No instances of noncompliance material to the financial statements of STEPS, Inc., which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.

Federal Awards

- During the audit, no significant deficiencies or material weaknesses in internal control over major federal award programs are disclosed or reported.
- The auditor’s report on compliance for the major federal award programs for STEPS, Inc. expresses an unmodified opinion on all major federal programs.
- Audit findings that are required to be reported in accordance with the Uniform Guidance are reported in this Schedule.

Identification of Major Programs/Programs Tested

- The programs tested as major programs were:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
93.600	Head Start Program

- The threshold used for distinguishing between Type A and Type B programs was \$750,000.
- The auditee was not determined to be a low-risk auditee.

Section II- Financial Statement Findings

No reportable findings noted.





STEPS, INC.
Schedule of Findings and Questioned Costs
For the Year Ended June 30, 2017

Section III- Federal Award Findings and Questioned Costs

2017-001 Head Start Program – CFSA No. 93.600; Grant No. 03CH010185; Grant period: Year Ended July 31, 2016

Criteria and Condition: A Head Start Agency that uses Head Start funds to purchase real property or purchase, construct, or renovate a facility appurtenant to real property must record a Notice of Federal Interest. STEPS has not fully complied with this requirement.

Context: We requested documentation from STEPS for Notice of Federal Interest related to its Head Start facilities. We noted that legal counsel had been previously retained to file the necessary paperwork and amend lease agreements to reflect Notice of Federal Interest.

Cause: Although legal counsel was contacted earlier in the year about such notice, the decision was made to wait until multiple locations were open to file the necessary paperwork at one time. The lack of policy regarding the Notice of Federal Interest caused a delay in such filings as well as resulted in proper wording not being included in the related lease agreements for the Prince Edward facility, which was opened in August 2016.

Effect: Untimely filing of the Notice of Federal Interest resulted in STEPS not being in compliance with this special provision of the Head Start grant. There are no questioned costs as a result of failing to meet this requirement.

Recommendation: Appropriate written policies and procedures should be established to ensure proper filing and proper execution of wording in lease agreements. These procedures should provide for appropriate review and approvals by the Executive Director.

Views of Responsible Officials and Planned Corrective Actions: We agree with the finding and are working to establish written policies and procedures that will include Notice of Federal Interest and other compliance requirements. We have contacted legal counsel to file all necessary Notice of Federal Interest as well as to review all lease agreements for Head Start facilities and amend as necessary.

