



Head Start, Inc.

Independent Auditor's Report
and
Financial Statements
June 30, 2016 and 2015

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HEAD START, INC.

For the Years Ended June 30, 2016 and 2015

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Independent Auditor's Report

To the Board of Directors
Head Start, Inc.
Billings, Montana

Report on the Financial Statements

We have audited the accompanying financial statements of Head Start, Inc. (a non-profit organization) which comprise the statements of financial position as of June 30, 2016 and 2015 and the related statements of activities and changes in net assets, 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 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.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of Head Start, Inc., as of June 30, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The schedule of expenditures of federal awards is presented for purposes of additional analysis 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*, and is not a required part of the financial statements. Such information is the responsibility of management, and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued a report dated December 15, 2016 on our consideration of Head Start, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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 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 Head Start, Inc.'s internal control over financial reporting and compliance.



Billings, Montana
December 15, 2016

FINANCIAL STATEMENTS

STATEMENTS OF FINANCIAL POSITION

JUNE 30,

	<u>2016</u>	<u>2015</u>
Assets		
Cash	448,719	452,527
Investments	121,561	122,374
Grants and Other Receivables	102,013	203,050
Prepaid Expenses	19,897	23,936
Property and Equipment, Net of Depreciation	986,369	966,911
Total Assets	<u>1,678,559</u>	<u>1,768,798</u>
Liabilities and Net Assets		
Accounts Payable	164,680	182,492
Accrued Expenses and Other Liabilities	111,970	148,577
Total Liabilities	<u>276,650</u>	<u>331,069</u>
Net Assets		
<i>Unrestricted</i>		
Operating	342,874	378,456
Property and Equipment	986,369	966,911
Total Unrestricted Net Assets	<u>1,329,243</u>	<u>1,345,367</u>
<i>Temporarily Restricted</i>	<u>72,666</u>	<u>92,362</u>
Total Net Assets	<u>1,401,909</u>	<u>1,437,729</u>
Total Liabilities and Net Assets	<u>1,678,559</u>	<u>1,768,798</u>

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



FINANCIAL STATEMENTS

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS FOR THE YEAR ENDED JUNE 30, 2016

	Unrestricted	Temporarily Restricted	Total
Revenue and Support			
Grants	3,297,408		3,297,408
Contract			
United Way	19,000		19,000
Donated Goods and Services	425,982		425,982
Contributions	54,348	11,275	65,623
Net Investment Income	2,191		2,191
Net Assets Released from Restriction through Satisfaction of Program Restrictions	30,971	(30,971)	
Total Revenue and Support	3,829,900	(19,696)	3,810,204
Expenses			
Program Services	3,320,243		3,320,243
Support Services			
Management & General	510,728		510,728
Fundraising	15,053		15,053
Total Expenses	3,846,024		3,846,024
Change in Net Assets	(16,124)	(19,696)	(35,820)
Net Assets, Beginning of Year	1,345,367	92,362	1,437,729
Net Assets, End of Year	1,329,243	72,666	1,401,909

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



FINANCIAL STATEMENTS

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS FOR THE YEAR ENDED JUNE 30, 2015

	Unrestricted	Temporarily Restricted	Total
Revenue and Support			
Grants	3,278,006		3,278,006
Contract	31,524		31,524
United Way	19,000		19,000
Donated Goods and Services	511,795		511,795
Contributions	54,257	16,359	70,616
Net investment (Loss)	(4,784)		(4,784)
Net Assets Released from Restriction through Satisfaction of Program Restrictions	12,012	(12,012)	
Total Revenue and Support	3,901,810	4,347	3,906,157
Expenses			
Program Services	3,463,116		3,463,116
Support Services			
Management & General	444,680		444,680
Fundraising	11,518		11,518
Total Expenses	3,919,314		3,919,314
Change in Net Assets	(17,504)	4,347	(13,157)
Net Assets, Beginning of Year	1,362,871	88,015	1,450,886
Net Assets, End of Year	1,345,367	92,362	1,437,729

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



FINANCIAL STATEMENTS

SCHEDULE OF FUNCTIONAL EXPENSES

FOR THE YEAR ENDED JUNE 30, 2016

	Program Services	Support Services		Total
		Management & General	Fundraising	
Salaries and Wages	2,006,059	384,165		2,390,224
Payroll Taxes	211,725	45,982		257,707
Fringe Benefits	177,198	20,093		197,311
Contracted Services	48,472	456		48,928
Rent	34,333	1,506		35,839
Student Transportation	36,149			36,149
Travel	10,205	2,168	295	12,668
Supplies	254,930	5,130	313	260,373
Repair and Maintenance	123,028	173		123,201
Utilities	61,214	75	65	61,354
Professional Services	7,555	5,578	5,900	19,033
Advertising & Promotion	3,314	52	3,533	6,899
Insurance	27,929	8,891		36,820
Food	131,561			131,561
Training	29,947	16,147	399	46,493
Other	74,861	14,787	4,548	94,196
Total Expenses before Depreciation	3,238,500	505,203	15,053	3,758,756
Depreciation	81,743	5,525		87,268
Total Expenses	3,320,243	510,728	15,053	3,846,024

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



FINANCIAL STATEMENTS

SCHEDULE OF FUNCTIONAL EXPENSES

FOR THE YEAR ENDED JUNE 30, 2015

	Program Services	Support Services		Total
		Management & General	Fundraising	
Salaries and Wages	2,207,135	299,829		2,506,964
Payroll Taxes	254,013	36,878		290,891
Fringe Benefits	205,624	6,072		211,696
Contracted Services	14,375	33,077		47,452
Rent	34,772		656	35,428
Student Transportation	61,798			61,798
Travel	18,597	8,298	1,798	28,693
Supplies	287,475	15,526	1,535	304,536
Repair and Maintenance	86,553	7		86,560
Utilities	58,210	3,232	150	61,592
Professional Services	725	6,615	7,100	14,440
Advertising & Promotion	7,260	2,103	229	9,592
Insurance	10,963	24,077		35,040
Food	123,150			123,150
Training	24,466	6,857		31,323
Other	12,370	662	50	13,082
Total Expenses before Depreciation	3,407,486	443,233	11,518	3,862,237
Depreciation	55,630	1,447		57,077
Total Expenses	3,463,116	444,680	11,518	3,919,314

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



FINANCIAL STATEMENTS

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED JUNE 30,

	2016	2015
Cash Flows from Operating Activities		
Increase (Decrease) in Net Assets	(35,820)	(13,157)
Adjustments to Reconcile Increase (Decrease) in Net Assets to Net Cash Provided by Operating Activities:		
Depreciation	87,268	57,077
Unrealized (Gain) Loss on Investments	2,692	10,560
Realized (Gain) Loss on Investments	715	(1,301)
(Increase) Decrease in:		
Grants and Other Receivables	101,037	(203,050)
Prepaid Expenses	4,039	(19,758)
Increase (Decrease) in:		
Accounts Payable	(17,812)	69,477
Accrued Expenses and Other Liabilities	(36,607)	51,046
	105,512	(49,104)
Cash Flows from Investing Activities		
Purchases of Investments	(15,042)	(41,199)
Proceeds from Sales of Investments	12,448	39,838
Purchases of Property and Equipment	(106,726)	(9,700)
	(109,320)	(11,061)
Cash Flows from Financing Activities		
None		
	(3,808)	(60,165)
Net Increase (Decrease) in Cash		
	(3,808)	(60,165)
Cash, Beginning of Year	452,527	512,692
Cash, End of Year	448,719	452,527
Supplemental Disclosure of Non-cash Investing and Financing Activity		
Accounts Payable for Property and Equipment		110,610

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



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

Note A Organization

Head Start, Inc. (the Organization) operates a federally funded Head Start program in Billings, Joliet, Laurel, Lockwood, and Red Lodge, Montana. The mission of the Organization is to provide comprehensive services for young children and their families to achieve school readiness and lifelong success.

Note B Summary of Significant Accounting Policies

Cash - For purposes of the statement of cash flow, the Organization considers all highly liquid investments available for current use with an initial maturity of three months or less to be cash equivalents.

Contribution Revenue - 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 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 and change in net assets as a net assets released from restrictions. If a restriction is fulfilled in the same period in which the contribution is received, the support is reported as temporarily restricted and then released from restriction in the same period.

Investments - The Organization records investment purchases at cost, or if donated, at fair value on the date of donation. Thereafter, investments are reported at their fair values in the statements of financial position. Net investment return/(loss) is reported in the statements of activities and consists of interest and dividend income, and realized and unrealized capital gains and losses.

Grants and Other Receivables - Past history has indicated that all receivables are collectible. The Organization has elected to record bad debts using the direct write-off method. Generally accepted accounting principles require that the allowance method be used to recognized bad debts; however, the effect of using the direct write-off method is not materially different from the results that would have been obtained under the allowance method.

Property and Equipment - Purchased property and equipment is recorded at cost while contributed property and equipment is recorded at fair value at the time of donation. The Organization capitalizes all property and equipment in excess of \$5,000 and minor replacements, maintenance, and repairs are charged to expense as incurred. When property and equipment are retired or otherwise disposed of, the cost and accumulated depreciation are removed from the accounts and any resulting gain or loss is included in the statement of activities and change in net assets for the respective period. Depreciation is provided over the estimated useful lives of the related assets using the straight-line method.



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS CONTINUED FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

The United States Department of Health and Human Services retains a reversionary interest in any equipment acquired with Federal funds. Disposition of such equipment is subject to rules and regulations of the United States Government. Assets acquired with other funds of the Organization are not subject to reversionary interests.

The estimated useful lives for significant property and equipment categories are as follows:

Vehicles	5 years
Equipment	5 - 10 years
Buildings and Improvements	5 - 40 years

Accrued Leave - Accrued leave represents the Organization's liability for the cost of unused employee annual leave in the event of employee terminations.

Functional Allocation of Expenses - The costs of providing the Organization's various programs and supporting services have been summarized on a functional basis. Accordingly, certain costs have been allocated among the programs and supporting services benefitted.

Income Taxes - The Organization is organized as a Montana nonprofit corporation and has been recognized as exempt from federal income taxes under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3), qualifies for the charitable contribution deduction under Sections 170(b)(1)(A)(vi), and has been determined not to be a private foundation under Section (509)(a)(1). The Organization is annually required to file a Return of Organization Exempt from Income Tax (Form 990) with the IRS. In addition, the Organization is subject to income tax on net income that is derived from business activities that are unrelated to its exempt purposes. The Organization has no unrelated business income and has not filed and Exempt Organization Business Income Tax Return (Form 990-T) with the IRS.

Advertising - Advertising costs are expensed as incurred. Advertising expense was \$6,899 and \$4,404 for the years ended June 30, 2016 and 2015, respectively.

Functional Allocation of Expenses - The costs of program and supporting services have been summarized on a functional basis in the statements of activities. The statements of functional expenses represent the natural classification detail of expenses by function. Accordingly, certain costs have been allocated among the programs and supporting services benefitted.

Use of Estimates - Preparing the Organization's financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect 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 these estimates.



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS CONTINUED FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

Cash in Excess of FDIC Insured Limits - The Organization maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. Accounts are guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. At June 30, 2016 and 2015, the Organization had approximately \$0 and \$0, respectively, in excess of FDIC limits. The Organization has not experienced any losses in such accounts.

Net Assets – Net assets, revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

- Unrestricted Net Assets – Net assets available for use in general operations.
- Temporarily Restricted Net Assets – Net assets subject to donor restrictions that may or will be met by expenditures or our actions and/or passage of time.

Recent Accounting Guidance – In May 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-09, *Revenue from Contracts with Customers* which requires all companies to adopt a five step analysis to determine the point in that goods or services have been exchanged with customers in exchange for consideration. The implementation of this update is effective for annual reporting periods beginning after January 1, 2018. Based on its initial review of the requirements under the new pronouncement, management does not believe there will be any material impact on the recognition of revenues as reported under its contracts.

In August 2016, the FASB issued ASU 2016-14 (the ASU) *Presentation of Financial Statements for Not-for-Profit Entities*. The ASU seeks to improve Not-for-Profit financial reporting by simplifying net asset classifications and enhancing presentation and disclosure requirements regarding liquidity, financial performance, and cash flows. The ASU is effective for fiscal years beginning after December 15, 2017. Management has not assessed the impact of implementing this new guidance.

Note C Net Investment Return

Net investment return consists of the following for the years ended June 30, 2016 and 2015:

	2016	2015
Interest and Dividends	5,598	4,475
Net Realized and Unrealized Gain (Loss)	(3,407)	(9,259)
	<u>2,191</u>	<u>(4,784)</u>



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS CONTINUED FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

Note D Property and Equipment

Property and Equipment consists of the following at June 30, 2016 and 2015:

	2016	2015
Vehicles	488,996	437,875
Equipment	151,540	151,540
Buildings and Improvements	1,416,190	1,240,276
Improvements in Process		120,310
Total capital assets at cost	2,056,726	1,950,001
Less Accumulated Depreciation	(1,070,357)	(983,090)
	<u>986,369</u>	<u>966,911</u>

Note E Fair Value Measurements

The Organization reports certain assets at fair value in the financial statements. Fair value is the price that would be received to sell an asset in an orderly transaction in the principal, or most advantageous, market at the measurement date under current market conditions regardless of whether that price is directly observable or estimated using another valuation technique. Inputs used to determine fair value refer broadly to the assumptions that market participants would use in pricing the asset, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset based on the best information available. A three-tier hierarchy categorizes the inputs as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets that the Organization can access at the measurement date.
- Level 2 - Inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly. These include quoted prices for similar assets in active markets, quoted prices for identical or similar assets in markets that are not active, inputs other than quoted prices that are observable for the asset, and market-corroborated inputs.
- Level 3 – Unobservable inputs for the asset. In these situations, we develop inputs using the best information available in the circumstances.



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS CONTINUED FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

The Organization classifies assets and liabilities within the fair value hierarchy based on the lowest level of input that is significant to the fair value measurement of each individual asset and liability taken as a whole. The table below sets forth by level within the fair value hierarchy the gross components of the assets and liabilities measured at fair value on a recurring basis.

June 30, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Net Fair Value
Marketable Securities	55,413			55,413
Mutual Funds	66,148			66,148
	<u>121,561</u>			<u>121,561</u>
June 30, 2015				
Marketable Securities	54,703			54,703
Mutual Funds	67,671			67,671
	<u>122,374</u>			<u>122,374</u>

Note F Donated Goods and Services

Donated goods and services for the years ended June 30, 2016 and 2015 are as follows:

	June 30,	
	2016	2015
Salaries and fringe benefits (Professional Services)	348,523	442,741
Rent of office and classroom space	14,800	19,000
Supplies	60,102	49,206
Travel	1,773	
Other	784	848
	<u>425,982</u>	<u>511,795</u>

Contributions of services are recognized in the Organization's financial statements only if (1) the services enhance or create non-financial assets or require specialized skills, (2) are provided by individuals possessing those skills and (3) would typically need to be purchased if not provided by donation. During the years ended June 30, 2016 and 2015, services donated by non-professionals and parents totaled \$170,423 and \$165,514, respectively. These amounts have not been included in the financial statements.



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS CONTINUED FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

All donated goods and services were for regular program services. Their value has been calculated using the estimated cost of similar goods and services.

Note G Temporarily Restricted Net Assets

Temporarily restricted net assets at June 30, 2016 and 2015 consisted of the following:

	<u>June 30, 2016</u>	<u>June 30, 2015</u>
Children and Family Needs at Red Lodge site		5,591
Classrooms	2,073	2,155
Clothing	21	60
Families	17,573	18,420
Freezer		250
Friday Food Pack Program		4,306
Garden		596
Health Education for Parents	4,945	5,865
Healthy Habits	2,296	2,296
Heros Hunt	109	109
Language and Literacy	9,880	9,907
Milk	374	2,007
Miscellaneous	3,137	14,724
Montana Healthy Kids	22,726	22,726
Move with Me, Mommy	248	807
North Park Children's Center	500	500
Playground	182	300
Read to Me, Daddy	526	1,546
Trauma Informed Care	8,076	197
Totals	<u>72,666</u>	<u>92,362</u>



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS CONTINUED FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

Note H Net Assets Released from Restrictions

Net assets were released from restrictions during the years ended Jun 30, 2016 and 2015 by incurring expenses satisfying the restricted purposes as follows:

	<u>June 30, 2016</u>	<u>June 30, 2015</u>
Children and Family Needs at Red Lodge site	5,591	
Classrooms	1,031	1,168
Clothing	39	
Families	923	522
Freezer	250	
Friday Food Pack Program	5,056	694
Garden	596	1,677
Graduation		300
Health Education for Parents	920	85
Language and Literacy	28	90
Milk	1,633	
Miscellaneous	11,587	63
Move with Me, Mommy	1,059	173
Playground	118	5,000
Read to Me, Daddy	1,019	437
Trauma Informed Care	1,121	1,803
Totals	<u>30,971</u>	<u>12,012</u>

Note I Lease Commitments

On July 1, 2008, the Organization entered into a lease agreement with Joliet Community Center, Inc. to lease classroom, playground, and office space in the Joliet Community Center in Joliet, Montana. The lease term was for six years and was to expire June 30, 2018. The Organization was required to pay rent of \$6,700 annually and its proportionate share of utilities, repairs, and maintenance. The Organization was required to maintain a general public liability insurance and personal property insurance as deemed necessary for their functions. The Joliet site was closed as of June 30, 2016. The Joliet Community Center, Inc. agreed to terminate the lease as of October 31, 2016. A final lease payment of \$2,232 was paid on December 7, 2016.

On August 1, 2012, the Organization entered into a lease agreement with the Red Lodge Community United Church of Christ to lease certain parts of the Church building and grounds. The lease term was for three years and expired July 31, 2015. The Organization was required to pay \$6,500 annually plus the expense for its own telephone line and any necessary repairs and maintenance. The Organization was required to



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS CONTINUED FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

maintain general public liability insurance as deemed necessary for their functions. The Red Lodge site was closed as of June 30, 2016. No further lease payments are due.

The Organization entered into a shared services agreement with the Laurel Public Schools for classroom and office space. The lease is on an annual basis and requires rental payment of \$1,000. The Organization is required to provide any furnishings necessary in the classrooms.

The Organization entered into a shared services agreement with the Lockwood Public Schools for classroom and office space. The lease is on an annual basis and requires rental payment of \$2,000. The Organization is required to provide any furnishings necessary in the classrooms.

The lease portion of rent expense for the years ended June 30, 2016 and 2015 was \$13,200 and \$13,200, respectively. No future minimum lease payments are required.

Note J Economic Dependency

The Organization recognized \$3,106,216 and \$3,100,841 in fiscal years 2016 and 2015, respectively, in Head Start funds provided by the Department of Health and Human Services. This represents 94% and 95%, respectively, of total grant funding for the years audited. These funds are essential for the Organization to continue to meet its contractual obligations. A decrease would impair the Organization's operations.

Note K Defined Contribution Plan

Certain employees are covered by a 401(k) defined contribution plan. To be eligible to participate, an employee must have attained the age of 18 and completed one year of service. The Organization may make discretionary or matching contributions, and in 2016 and 2015 elected to contribute \$25,000 each year on behalf of eligible employees who had participated in the plan. Plan administrative expenses incurred by the Organization were \$0 and \$0 for the years ended June 30, 2016 and June 30, 2015, respectively.

Note L Contingency

The Organization participates in a number of federally assisted grant programs that are subject to audit and adjustment by the grantors. The grantor audits of these programs, if any, for or including the year ended June 30, 2016, have not yet been conducted. Accordingly, the Organization'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 granting agencies cannot be determined at this time although the Organization expects such amounts, if any, to be immaterial.



FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS CONTINUED FOR THE YEARS ENDED JUNE 30, 2016 AND 2015

Note M Subsequent Events

On June 30, 2016, the Red Lodge site was vacated and closed. The Joliet site was vacated on June 30, 2016, with the lease ending on October 31, 2016. A final lease payment of \$2,232 was paid to the Joliet Community Center on December 7, 2016.

Management has evaluated the activities and transactions subsequent to June 30, 2016, to determine the need for any adjustments to and/or disclosure within the audited financial statements for the year ended June 30, 2016. Management has performed this evaluation through December 15, 2016, the date the financials were available to be issued.





Head Start, Inc.

Supplemental Information
for the Years Ended
June 30, 2016 and 2015



SUPPLEMENTAL INFORMATION

SCHEDULE OF EXPENDITURE OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2016

<u>Federal Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Grant or Contract Number</u>	<u>Program or Award Amount</u>	<u>Total Expenditures</u>
<u>U.S. Department of Health and Human Services</u>				
Head Start CAN 4122	93.600	08CH1030/02	3,073,112	3,073,112
Head Start CAN 4120	93.600	08CH1030/02	33,104	<u>33,104</u>
Total U.S. Department of Health and Human Services				<u>3,106,216</u>
<u>U.S. Department of Agriculture</u>				
Passed through:				
Montana Department of Public Health and Human Services				
Child and Adult Care Food Program	10.558	1202CACFP129		<u>153,812</u>
Total U.S. Department of Agriculture				<u>153,812</u>
Total Expenditures of Federal Awards				<u><u>3,260,028</u></u>

See Notes to Schedule of Expenditures of Federal Awards



SUPPLEMENTAL INFORMATION

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2016

Note A **Basis of Presentation**

The accompanying schedule of expenditures of federal awards includes the federal award activity of Head Start, Inc. under programs of the federal government for the year ended June 30, 2016, in accordance with the requirements of Uniform Guidance. Because the schedule presents only a selected portion of the operations of Head Start, Inc., it is not intended to and does not present the financial position, changes in net assets, or cash flows of Head Start, Inc.

Note B **Significant Accounting Policies**

Expenditures reported on the schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in Subpart E – Cost Principles of the Uniform Guidance, wherein certain types of expenditures are not allowed or are limited as to reimbursement. Head Start, Inc.'s summary of significant accounting policies is presented in Note B in Head Start, Inc.'s basic financial statements.

Head Start, Inc. has not elected to use the 10% de minimus indirect cost rate as allowed under 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
Head Start, Inc.
Billings, Montana

We have audited, 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, the financial statements of Head Start, Inc. (a nonprofit organization), which comprise the statement of financial position as of June 30, 2016, and the related statements of activities and changes in net assets, 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 December 15, 2016.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered Head Start, 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 Head Start, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of Head Start, 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 a 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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as finding 2016-A, that we consider to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Head Start, Inc.'s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of 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*.

Head Start, Inc.'s Response to Findings

Head Start, Inc.'s response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. Head Start, Inc.'s response 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

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.

A handwritten signature in cursive script that reads "Eide Sully LLP".

Billings, Montana
December 15, 2016



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

To the Board of Directors of
Head Start, Inc.
Billings, Montana

Report on Compliance for Each Major Federal Program

We have audited Head Start, Inc.'s compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on Head Start, Inc.'s major federal program for the year ended June 30, 2016. Head Start, Inc.'s major federal program is 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 terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on the compliance for Head Start, Inc.'s major federal program 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 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 Head Start, 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 its major federal program. However, our audit does not provide a legal determination of Head Start, Inc.'s compliance.

Opinion on Each Major Federal Program

In our opinion, Head Start, Inc. complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major Federal program for the year ended June 30, 2016.

Report on Internal Control over Compliance

Management of Head Start, Inc. is responsible for establishing and maintaining effective internal control over compliance with the compliance requirements referred to above. In planning and performing our audit of compliance, we considered Head Start, Inc.'s internal control over compliance with the types of requirements that could have a direct and material effect on its major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for its 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 of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Head Start, 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 compliance requirement will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal 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 that might be material weaknesses or significant deficiencies and therefore, material weaknesses and significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we identified certain deficiencies in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as item 2016-001 that we consider to be a significant deficiency.

Head Start, Inc.'s response to the internal control over compliance finding identified in our audit is described in the accompanying corrective action plan. Head Start, Inc.'s response was not subjected to auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

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.



Billings, Montana
December 15, 2016

Section I – Summary of Auditor’s Results

FINANCIAL STATEMENTS

Type of auditor's report issued	Unmodified
Internal control over financial reporting:	
Material weaknesses identified	Yes
Significant deficiencies identified not considered to be material weaknesses	None reported
Noncompliance material to financial statements noted?	No

FEDERAL AWARDS

Internal control over major program:	
Material weaknesses identified	No
Significant deficiencies identified not considered to be material weaknesses	Yes
Type of auditor's report issued on compliance for major programs:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with Uniform Guidance 2 CFR 200.516:	Yes

Identification of major programs:

<u>Name of Federal Program</u>	<u>CFDA Number</u>
Head Start	93.600
Dollar threshold used to distinguish between type A and type B programs:	\$750,000
Auditee qualified as low-risk auditee?	No

Section II – Financial Statement Findings

2016-A Segregation of Duties

Criteria: A good system of internal control contemplates an adequate segregation of duties so that no one handles a transaction from its inception to completion.

Condition: Head Start, Inc. has a limited number of office personnel and, accordingly, does not have adequate internal accounting controls in certain areas because of a lack of segregation of duties.

Cause: Head Start, Inc.’s size and budget constraints limit the number of personnel and do not facilitate the segregation of duties necessary to adequately separate procedures.

Effect: The design of the internal control over financial reporting could adversely affect the ability to record, process, summarize, and report financial data consistent with assertions of management in the financial statements. This deficiency may cause misstatements of the financial statements, which would not be prevented or detected, and reported by Head Start, Inc.’s internal control.

Recommendation: We recommend that Head Start, Inc. periodically assess the accounting staffing and duties and that the Board continue to be actively involved and knowledgeable about the operations of the organization.

*Views of
Responsible Officials:* There is no disagreement with the finding.

Section III – Federal Award Findings and Questioned Costs

**2016-001 U.S. Department of Health and Human Services
CFDA#93.600 Head Start**

**Matching
Significant Deficiency in Internal Control over Compliance**

Criteria: The Head Start Program Performance Standard 45 CFR 1304 requires that all matching in-kind contributions must be verifiable from the grantee's records. Time sheets must be used to document hours contributed to the program. These time sheets must include the volunteer's name, dates of volunteer time, duration, and description of the services provided and a signature of the volunteer and a supervisor.

Condition: For 2 out of 60 in-kind donations tested, the hours of volunteer time recorded did not recalculate to the hours of volunteer time listed on the time sheets.

Cause: Head Start, Inc.'s established system of controls did not effectively ensure all in-kind activity time sheets are completely and accurately prepared and recorded as designed.

Effect: The recorded amount on in-kind transactions could be overstated.

Questioned Costs: None reported.

Context/Sampling: Nonstatistical sampling was used. Sample size was 60 out of 4500 transactions and included \$3,901 of \$596,406 of in-kind contributions.

Repeat Finding from Prior Year(s): No.

Recommendation: We recommend that Head Start, Inc. maintain proper oversight and review of in-kind compliance with regard to time sheets and recordkeeping.

Views of Responsible Officials: There is no disagreement with the finding.

**2015-A Financial Statement Finding
 Entity Level Controls over Journal Entries**

*Initial Fiscal Year
Finding Occurred:* Year ended June 30, 2015.

Finding Summary: Head Start, Inc. does not have an internal control process for the review and approval of journal entries.

Status: Partially Implemented. Head Start, Inc. has implemented procedures for controls over journal entries within the limitations of office size, as noted in the current year finding 2016-A.

**2015-B Financial Statement Finding
 Segregation of Duties**

*Initial Fiscal Year
Finding Occurred:* Year ended June 30, 2015.

Finding Summary: Head Start, Inc. has a limited number of office personnel and, accordingly, does not have adequate internal accounting controls in certain areas because of a lack of segregation of duties.

Status: Not implemented; restated as current year finding 2016-A. Management is still evaluating the limited office size of Head Start, Inc. and how it will respond to this financial statement finding. Refer to management's corrective action plan for the current year finding 2016-A.



HEAD START, INC.



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Corrective Action Plans Year Ended June 30, 2016

2016-A Segregation of Duties Material Weakness

Contact Person Responsible for Corrective Action – Kristin Van Luchene, Finance Director

Corrective Actions Planned – Head Start, Inc. will continue to periodically assess the accounting staffing and duties and the Board will continue to be actively involved and knowledgeable about the operations of the organization.

The Accounting & Financial Policies and Procedures Manual will be updated to include Control Grids showing segregation of duties. This manual will be reviewed at least annually by the Finance Committee, Board of Directors, and Policy Council.

Anticipated Completion Date of Corrective Action Plan – Ongoing.

2016-001 Matching Significant Deficiency in Internal Control over Compliance

Contact Person Responsible for Corrective Action – Kristin Van Luchene, Finance Director

Corrective Actions Planned – Entry of in-kind match will be done on a timely basis, with periodic checks by the Finance Director to make sure review procedures are followed. Matching amounts will be included in the monthly financial reports to the Board and Policy Council for their review. An internal controls review has been scheduled with an accounting firm that specializes in non-profits and Financial Edge, the accounting system used by Head Start, Inc.

Anticipated Completion Date of Corrective Action Plan – Ongoing with the internal controls review to be done in January 2017.