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ABILITYWORKS, INC.

MADISON, MISSISSIPPI

FINANCIAL REPORT

JUNE 30, 2015



HARPER, RAINS, KNIGHT
& COMPANY

*Certified Public Accountants
A Professional Association*

ABILITYWORKS, INC.
MADISON, MISSISSIPPI
FINANCIAL REPORT
JUNE 30, 2015

HARPER, RAINS, KNIGHT & COMPANY, P.A.
CERTIFIED PUBLIC ACCOUNTANTS
RIDGELAND, MISSISSIPPI

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The Board of Directors
AbilityWorks, Inc.
Madison, Mississippi

Independent Auditors' Report

Report on the Financial Statements

We have audited the accompanying financial statements of AbilityWorks, Inc., a component unit of the State of Mississippi, as of and for the years ended June 30, 2015 and 2014, and the related notes to the financial statements, which collectively comprise the basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express opinions 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 auditors' 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 auditors consider 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.

Auditors' Responsibility - continued

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of AbilityWorks, Inc., a component unit of the State of Mississippi, as of June 30, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5-11 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were conducted for the purpose of forming opinions on the financial statements that collectively comprise AbilityWorks, Inc.'s, a component unit of the State of Mississippi, basic financial statements. The supplementary information included in the accompanying schedules of cost of production, general and administrative expenses, and statistical analysis of operations are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The schedules of cost of production, general and administrative expenses, and statistical analysis of operations are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audits 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 basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the accompanying supplementary information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The Board of Directors
AbilityWorks, Inc. - Continued

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 23, 2015 on our consideration of AbilityWorks, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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* and should be considered in assessing the results of our audits.

Harper, Rainie, Knight & Company, P.A.

November 23, 2015

ABILITYWORKS, INC.
FINANCIAL REPORT
MANAGEMENT'S DISCUSSION AND ANALYSIS

The following is a discussion and analysis of the AbilityWorks, Inc. ("AbilityWorks") financial performance, providing an overview of the activities for the fiscal year ended June 30, 2015.

Since the Management's Discussion and Analysis is designed to focus on the current year's activities, resulting changes and currently known facts, please read it in conjunction with AbilityWorks, Inc.'s basic financial statements.

Financial Highlights

- Total net position for AbilityWorks at year end was reported at \$22,482,665, which was an increase of \$775,806, or 3.6%, from the prior fiscal year.
- Revenues for fiscal year 2015 decreased \$1,718,379, or 15.5%, from fiscal year 2014. The change in Revenue included the following: "production revenue" decreased \$1,114,960, "other operating revenue" decreased \$601,707, and "nonoperating revenue" decreased \$1,712.
- Total expenses decreased 2.6%, or \$441,435, from 2014 to 2015. "Cost of production" decreased \$287,972, "general and administrative expenses" decreased \$86,021, and "capital asset purchases" decreased \$67,442.
- Operating Transfers-in increased \$1,913,979, or 32.7%.

Overview of the Financial Statements

Under GASB 34, the applicable accounting standards for governmental financial statements, there are three components to the basic financial statements: 1) the government-wide financial statements, 2) the fund financial statements and 3) the notes to the financial statements.

Government-Wide Statements

AbilityWorks is classified as an enterprise fund and therefore utilizes the accrual method as its basis of accounting, which is the same as a private sector business. By utilizing the accrual method of accounting, the presentation of financial information in the government-wide statements and the fund financial statements would contain no differences. However, due to the fact that AbilityWorks is a component unit of the State of Mississippi, government-wide statements are not included herein but will instead be included in the State of Mississippi's basic financial statements. AbilityWorks' financial statements will be presented in the State of Mississippi's government-wide statements under the "business type activities".

ABILITYWORKS, INC.
FINANCIAL REPORT
MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Fund Financial Statements

The financial statements for AbilityWorks report the financial activity for all seventeen locations making up AbilityWorks. As an enterprise fund, these facilities charge customers for services provided, whether to outside customers or to other agencies within the State. The method of accounting used by AbilityWorks is the accrual method of accounting, which is the same used by private sector businesses, in that revenues are recognized when earned and expenses are recognized when incurred. Included in the fund financial statements are the statements of net position, the statements of revenues, expenses and changes in net position, and the statements of cash flows using the direct method. No other "required supplementary information" is presented. In addition, supplementary information is presented regarding cost of production, general and administrative expenses and certain statistical information.

Financial Analysis

AbilityWorks' increase in net position increased \$775,806 over the course of this fiscal year's operations.

Table 1
Statements of Net Position
June 30, 2015 and 2014

	<u>Governmental Activities</u>	
	<u>2015</u>	<u>2014</u>
Current and other assets	\$ 25,888,165	\$ 24,799,502
Current and other liabilities	<u>3,405,500</u>	<u>3,092,643</u>
Net position:		
Unrestricted	<u>\$ 22,482,665</u>	<u>\$ 21,706,859</u>

ABILITYWORKS, INC.
FINANCIAL REPORT
MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

- "Current and other assets" increased \$1,088,663 or 4%. Of this amount:
 - "Cash" increased \$4,760,569. The majority of this increase is attributed to the Medicaid Waiver, as wages were invoiced and paid by the parent agency for ten months of the current fiscal year (as opposed to only nine months in FY 2014).
 - "Investments" increased \$490.
 - The "Accounts receivables, net" account increased \$73,061. Due to the current economic climate, there has been a shift at facilities from entering into manufacturing contracts to entering into service/janitorial contracts. The majority of the Accounts Receivable balance at June 30, 2015, pertains to service contracts with the General Services Administration. Historically, payments for services on those contracts are not made as timely as with other contracts. Therefore, an increase in this account occurred.
 - The "Unbilled receivables" account, which involved the Medicaid Waiver for payroll processing services, increased \$146,803. The amount represents the payroll generated for those hours earned by personal care attendants prior to June 30th; however, the services were not invoiced to the parent agency by the June 30th cutoff. The increase in this account is the reflection of the growth that continues to be experienced in this program as well as our strengthening of review procedures regarding the invoicing process.
 - The "Interfund receivables" account decreased by \$3,908,303. The majority of the Interfund receivables account relates to the Medicaid Waiver, which represents payroll items which have been generated for hourly wages earned by personal care attendants and subsequently invoiced by the parent agency before June 30th but were not paid by the parent agency by June 30th. The FY 2014 interfund receivable amount includes wages invoiced for the months of April, May, and June. Due to the strengthening of our review procedures regarding this invoicing process, the current year interfund receivable amount includes wages invoiced for May and June only. Therefore, a decrease in the account occurred.
 - The "Inventories" account increased \$22,460. Due to the nature of some of the contracts obtained (i.e., janitorial, production of wood pallets, etc.), facilities will purchase raw materials (e.g., janitorial supplies, wood) to fulfill future production needs when a fair price is obtained for the raw materials.
 - The "Prepaid expenses" account did not significantly change from 2014 to 2015; no explanation is needed.

ABILITYWORKS, INC.
FINANCIAL REPORT
MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

- "Current liabilities" increased \$312,857. Of this amount:
 - The "accounts payable" account increased \$89,729. Under our centralized system, all invoices are submitted to the centralized office for processing. Due to the timing for which invoices were received and subsequently processed at the close of the fiscal year, AbilityWorks noted a 41% increase in this account.
 - The "accrued expenses" account increased \$223,128. The balance in this account represents the hours earned by the personal care attendants from the period June 16–30, 2015 and subsequently paid in July 2015. The increase in this account is the reflection of the growth that continues to be experienced in this program.

Table 2
Statement of Revenue,
Expenses and Changes in Net Position
For the Years Ended June 30, 2015 and 2014

	<u>Governmental Activities</u>	
	<u>2015</u>	<u>2014</u>
Revenues		
Operating revenues		
Revenue from production, net	\$ 9,047,551	\$ 10,162,511
Other operating income, net	307,634	909,341
Nonoperating revenues		
Investment income	<u>10,339</u>	<u>12,051</u>
Total revenues	9,365,524	11,083,903
Expenses		
Cost of production	8,499,718	8,787,690
General and administrative	7,776,579	7,862,600
Capital asset purchases	<u>90,000</u>	<u>157,442</u>
Total expenditures	16,366,297	16,807,732
Transfers		
Transfers-in	<u>7,776,579</u>	<u>5,862,600</u>
Total transfers (net)	7,776,579	5,862,600
Increase in net position	775,806	138,771
Net assets – beginning of year	<u>21,706,859</u>	<u>21,568,088</u>
Net assets – ending	<u>\$ 22,482,665</u>	<u>\$ 21,706,859</u>

ABILITYWORKS, INC.
FINANCIAL REPORT
MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

- AbilityWorks consists of community rehabilitation programs in seventeen separate locations which provide a fee for service to production and manufacturing industries within each workshop's area. Eight of the seventeen locations represented over 87% of the production revenue recorded in 2015. These facilities are as follows: Monroe County, Oxford, Washington County, Greenwood, Starkville, Jackson, Harrison County, and Meridian. The decrease in production revenue was due to the loss of contracts experienced by some of the facilities throughout the state.
- The decrease in the "cost of production" correlates to the decrease in the "revenue from production". Loss of contracts at several locations attributes to this decrease. As production revenue decreases, the cost of production decreases.
- The majority of the "other operating income" account is reported by our Medicaid Waiver payroll processing services. The decrease reported in this revenue account was \$601,707, which is mainly due to the implementation of the Affordable Care Act. Beginning January 1, 2015, AbilityWorks Inc. was required to offer health insurance to all nonclients working 30+ hours per week. Approximately \$1.5 million was the Medicaid Waiver's portion of the health insurance premiums offered.
- The "general and administrative expenses" represent those costs associated with office personnel of the AbilityWorks system, including facility managers, office managers, production managers, evaluators, instructors and administrative assistants as well as reimbursements to the facilities for client transportation and community based services. In fiscal year 2015, we noted an approximate 1% decrease in this category. The majority of general and administrative expenses represent salaries and wages (over 70%). Although only an immaterial decrease was noted, the majority of fluctuation in this category is attributable to salaries and related expenses.
- "Capital asset purchases" account in 2015 was \$90,000, which decreased \$67,442. The reason for the decrease was due to purchases made in 2014 that were not required in 2015. For FY2015, purchases included two 12.5 ton air conditioner units at Starkville (\$27,750), a forklift in Tupelo (\$21,667), a forklift in Jackson (\$11,500), a condensing unit in Washington County (\$4,795), an ice machine for Jackson (\$2,438), and a carpet cleaner for Meridian (\$2,434).
- The increase in the "transfers-in" account is mainly attributable to the timely payment of invoices by the parent agency for the Medicaid Waiver payroll. Closer scrutiny over review procedures has allowed for billing of the payroll in a more timely manner.

ABILITYWORKS, INC.
FINANCIAL REPORT
MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Economic Factors

Mississippi has experienced a steady decrease in the number of jobs in the manufacturing sector over the last decade. While some manufacturing job gains have occurred, statewide manufacturing jobs continues to be stagnant. The loss of manufacturing jobs is a direct reflection of the number of manufacturing businesses that closed down their operations in Mississippi. The production income generated by each AbilityWorks' facility is tied to the availability of subcontract work obtained from manufacturing businesses in the local community. Since manufacturing contracts have been declining in recent years, the AbilityWorks' system has been intentionally expanding production income from service sector contracts. These service contracts include janitorial, housekeeping, and ground maintenance.

Additionally, OVR leadership has incorporated a community based program within the AbilityWorks system. This program, LINC'S (Linking Innovative Networks of Community Services), provides vocational evaluation and job readiness opportunities outside the boundaries of the facility and places clients directly in local businesses. Once the clients' vocational interests are obtained, the facility staff seeks businesses that offer those specific skill opportunities and contracts with them directly to help train our clients. This is a winning scenario for businesses, clients and AbilityWorks.

The AbilityWorks, Inc. system anticipates additional capital asset purchases in fiscal year 2016 in the following area:

- To ensure the viability of the AbilityWorks, Inc. system, we continue to work with local businesses to develop additional contract work. In order to add new contracts throughout the state, we anticipate purchases of new or additional production related equipment, such as fork-lifts, delivery trucks, planer/molder woodworking machinery, etc.
- The purchase of ten passenger vans and one mini-van for client transportation is anticipated for nine AbilityWorks locations.

ABILITYWORKS, INC.
FINANCIAL REPORT
MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued

Lastly, on August 21, 2015, a three-judge panel of the District of Columbia Circuit Court of Appeals issued a unanimous decision upholding the FLSA Home Care Rule. This rule requires third party employers to pay at least the federal minimum wage and overtime pay to any direct care worker jointly employed. Direct care workers are workers who provide home care services, such as certified nursing assistants, home health aides, personal care aides, caregivers, and companions. Workers who are covered under federal overtime pay protections must be paid at a rate of not less than one and one-half times their regular rate of pay after 40 hours of work in a workweek.

Financial Contact

AbilityWorks' financial statements are designed to present users with a general overview of AbilityWorks' finances and to demonstrate its accountability. If you have any questions about the report or need additional information, contact the Director of Finance at the Mississippi Department of Rehabilitation Services, 1281 Highway 51 North, Madison, Mississippi 39110.

ABILITYWORKS, INC.

STATEMENTS OF NET POSITION

June 30, 2015 and 2014

ASSETS

	2015	2014
Current assets		
Cash	\$ 14,070,299	\$ 9,309,730
Investments	166,460	165,970
Accounts receivable, net	1,216,798	1,143,737
Unbilled receivables	2,469,696	2,322,893
Interfund receivable	7,494,067	11,402,370
Inventories	195,012	172,552
Prepaid expenses and other	275,833	282,250
	<u>25,888,165</u>	<u>24,799,502</u>
Total assets	<u>\$ 25,888,165</u>	<u>\$ 24,799,502</u>

LIABILITIES AND NET POSITION

Current liabilities		
Accounts payable	\$ 308,306	\$ 218,577
Accrued expenses	3,097,194	2,874,066
Total current liabilities	3,405,500	3,092,643
Net position - unrestricted	<u>22,482,665</u>	<u>21,706,859</u>
Total liabilities and net position	<u>\$ 25,888,165</u>	<u>\$ 24,799,502</u>

The Notes to Financial Statements are an integral part of these statements.

ABILITYWORKS, INC.

STATEMENTS OF REVENUES, EXPENSES
AND CHANGES IN NET POSITION
Years Ended June 30, 2015 and 2014

	2015	2014
Revenue		
Revenue from production, net	\$ 9,047,551	\$ 10,162,511
Cost of production	8,499,718	8,787,690
Gross profit	547,833	1,374,821
Other operating income	307,634	909,341
General and administrative expenses	7,776,579	7,862,600
Operating loss	(6,921,112)	(5,578,438)
Nonoperating revenue (expenses)		
Investment income	10,339	12,051
Capital asset purchases	(90,000)	(157,442)
Total nonoperating expenses	(79,661)	(145,391)
Loss before transfers	(7,000,773)	(5,723,829)
Transfers-in	7,776,579	5,862,600
Increase in net position	775,806	138,771
Net position, beginning of year	21,706,859	21,568,088
Net position, end of year	\$ 22,482,665	\$ 21,706,859

The Notes to Financial Statements are an integral part of these statements.

ABILITYWORKS, INC.

STATEMENTS OF CASH FLOWS
Years Ended June 30, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Cash flows from operating activities:		
Receipts from customers	\$ 9,002,485	\$ 10,331,024
Receipts from DRS for payroll processing	62,451,722	53,606,004
Other receipts	278,136	174,341
Payments to suppliers	(4,235,502)	(4,484,789)
Payments to employees	(11,774,055)	(12,022,195)
Payments for payroll processing	<u>(58,658,645)</u>	<u>(53,160,376)</u>
Net cash used by operating activities	<u>(2,935,859)</u>	<u>(5,555,991)</u>
Cash flows from noncapital financing activities:		
Transfers-in	<u>7,776,579</u>	<u>5,862,600</u>
Net cash provided by noncapital financing activities	<u>7,776,579</u>	<u>5,862,600</u>
Cash flows from investing activities:		
Investment income	10,339	12,051
Sale and maturity of investments	165,970	165,538
Investment purchases	(166,460)	(165,970)
Capital asset purchases	<u>(90,000)</u>	<u>(157,442)</u>
Net cash used in investing activities	<u>(80,151)</u>	<u>(145,823)</u>
Net increase in cash	4,760,569	160,786
Cash at beginning of year	<u>9,309,730</u>	<u>9,148,944</u>
Cash at end of year	<u>\$ 14,070,299</u>	<u>\$ 9,309,730</u>

The Notes to Financial Statements are an integral part of these statements.

ABILITYWORKS, INC.

STATEMENTS OF CASH FLOWS - Continued
Years Ended June 30, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	\$ (6,921,112)	\$ (5,578,438)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Net effect of changes in assets and liabilities:		
Accounts receivable	(73,061)	190,661
Unbilled receivables	(146,803)	(82,411)
Interfund receivables	3,908,303	(195,903)
Inventories	(22,460)	(5,711)
Prepaid expenses and other	6,417	106,117
Accounts payable	89,729	(14,780)
Accrued expenses	<u>223,128</u>	<u>24,474</u>
Net cash used by operating activities	<u>\$ (2,935,859)</u>	<u>\$ (5,555,991)</u>

The Notes to Financial Statements are an integral part of these statements.

NOTES TO FINANCIAL STATEMENTS

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of AbilityWorks, Inc., (hereafter referred to as "AbilityWorks"), a component unit of the State of Mississippi, have been prepared in conformity with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board ("GASB"). The more significant of AbilityWorks' accounting policies follow.

Organization and Nature of Operations

AbilityWorks is a non-profit corporation owned and operated by the State of Mississippi, Department of Rehabilitation Services, Office of Vocational Rehabilitation (the "Division"). AbilityWorks was incorporated on July 18, 1969 with the granting of a charter by the State of Mississippi. Legal authority for AbilityWorks is granted under Section 37-33-101 of the Mississippi Code of 1972. AbilityWorks' purpose is to operate a statewide system of community rehabilitation programs through which citizens with disabilities receive work experience to prepare them for employment outside the workshop setting.

Currently, seventeen (17) AbilityWorks facilities are located in communities throughout Mississippi. These facilities provide work settings with realistic job stations where vocational evaluation, work adjustment, counseling, guidance and other services are provided. The Division funds some of the general and administrative expenses, such as staff payroll, rent, utilities, etc. The Division also provides all management necessary to administer AbilityWorks at no cost. Also, the Division transfers funds to the facilities on a monthly basis for additional expenses incurred as a result of expanded client services, such as maintenance to clients and incentive allowances.

Basis of Presentation

Basic financial statements include government wide financial statements, fund financial statements and notes to the financial statements. Since AbilityWorks is a component unit of the State of Mississippi, it only presents fund financial statements. AbilityWorks continues to report as a business-type enterprise fund.

Basis of Accounting

The accounts of AbilityWorks are reported using the accrual basis of accounting and the economic resources measurement focus. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred. Revenue from production and payroll processing income are stated net of provision for bad debt (benefit) expense of \$2,981 in 2015 and \$(2,136) in 2014.

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Inventories

Finished goods inventories are stated at the lower of manufacturing cost (first-in, first-out) or market (net realizable value). Purchased raw materials and supplies are stated at the lower of cost (first-in, first-out) or replacement market.

Revenue Recognition

Production revenue is recognized when the goods are shipped or the services performed.

Operating/Nonoperating Income

AbilityWorks has classified its revenue as either operating or nonoperating revenues according to the following criteria:

Operating revenues - Operating revenues generally result from community rehabilitation programs in seventeen separate locations which provide a fee for service to production and manufacturing industries within each workshop's area. Other operating income consists of net payroll income for processing payroll under the Medicaid Waiver program.

Nonoperating revenues - Nonoperating revenues are those revenues that do not meet the definition of operating revenues. Nonoperating revenues include investment income.

Interfund/Intrafund Transactions

Interfund represents transactions with a fund outside of AbilityWorks, while intrafund represents transactions within AbilityWorks. Interfund/intrafund transactions are reflected as either loans, services provided, reimbursements or transfers. Loans are reported as receivables and payables as appropriate and are subject to elimination upon combination. Services provided are treated as revenues and expenditures/expenses.

Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund and reduces its related expense as a reimbursement. All other interfund/intrafund transactions are treated as transfers. Intrafund balances have been eliminated and are not reflected in the basic financial statements.

Capital Asset Purchases

Property and equipment purchased directly by the facilities are the property of the State of Mississippi. These acquisition costs are classified as a nonoperating expense.

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Use of Estimates in the Preparation of Financial Statements

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 amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from those estimates.

Income Taxes

AbilityWorks is exempt from federal and state income taxes.

Investments

Investments consist of certificates of deposit which are carried at cost which approximates fair value.

Other

AbilityWorks provides transportation and maintenance funds to clients of the Department of Rehabilitation Services based on the orders of client counselors. The clients are not necessarily those employed by AbilityWorks. The amounts provided, \$91,733 in 2015 and \$69,448 in 2014, have been fully reimbursed by the State of Mississippi. The funds provided do not represent income or expenses of AbilityWorks and have not been recorded in the financial statements.

Cash and Cash Equivalents

For purposes of the statements of cash flows, cash includes all checking and savings accounts. AbilityWorks has no cash equivalents.

Employee Benefits

Employees of AbilityWorks, who are eligible for employee benefits, are considered employees of and are provided employee benefits through the State of Mississippi. The employees are covered by the State of Mississippi Public Employee Retirement System ("PERS"), a cost-sharing multiple-employer defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by state law and may be amended only by the Mississippi State Legislature. PERS issues a publicly available financial report that includes financial statements and required supplementary information. Disclosures regarding employee benefits are maintained and communicated within the State of Mississippi financial reports.

(1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Employee Benefits - continued

Employee benefit expenses are allocated to AbilityWorks through state paid expenditure transactions and are reported within the general and administrative expenses and cost of production schedules.

Subsequent Events

Subsequent events were evaluated by AbilityWorks through November 23, 2015, which is the date the financial statements were available to be issued.

(2) CONCENTRATIONS OF CREDIT AND OTHER RISKS

Financial instruments that potentially subject AbilityWorks to concentrations of credit risk consist of cash and cash equivalents, accounts receivable and loss of financial assistance from the State of Mississippi. AbilityWorks receives substantial support in the form of financial assistance from the State of Mississippi, the loss of which could have a material effect on the continuation of operations. Accounts receivable are due from customers in numerous industries within the State of Mississippi. Each facility monitors the credit worthiness of its customers to limit credit risk.

AbilityWorks maintains cash balances at various financial institutions. Accounts at each institution are insured up to \$250,000 by the Federal Deposit Insurance Corporation ("FDIC"). Amounts in excess of \$250,000 are collateralized by certain assets pledged by the financial institution's trust department in AbilityWorks' name. In addition, AbilityWorks has minimized credit risk by depositing cash and cash equivalents in banks with a high credit standing. AbilityWorks has not experienced any losses of such funds and management believes exposure to significant credit risk on cash and cash equivalents is minimal.

(3) INVESTMENTS

Investments at June 30, 2015, consist of a certificate of deposit totaling \$166,460 which matures in February 2016. Investments at June 30, 2014, consist of a certificate of deposit totaling \$165,970 which matured in February 2015. Interest earned on investments and cash balances for the years ended June 30, 2015 and 2014 was \$10,339 and \$12,051, respectively.

(4) ACCOUNTS RECEIVABLE

A summary of accounts receivable follows:

	<u>2015</u>	<u>2014</u>
Trade receivable	\$ 1,219,779	\$ 1,143,737
Less allowance for doubtful accounts	<u>(2,981)</u>	<u>-</u>
Accounts receivable, net	<u>\$ 1,216,798</u>	<u>\$ 1,143,737</u>

(5) UNBILLED RECEIVABLES

Unbilled receivables are the total amount for payroll processing services rendered but not yet invoiced, related to the Medicaid Waiver program. Unbilled receivables totaled \$2,469,696 in 2015 and \$2,322,893 in 2014.

(6) INTERFUND RECEIVABLES

Interfund receivables/payables related to payroll processing and other services provided to the agencies of the State of Mississippi consist of the following:

	<u>2015</u>	<u>2014</u>
Interfund receivables		
Office of Special Disability Programs	\$ 5,178,116	\$ 7,835,818
Spinal Cord Trauma Brain Injury	2,190,316	3,406,618
Office of Vocational Rehabilitation	121,642	142,673
Office of Employment Security	-	101
Office of Vocational Rehabilitation for the Blind	-	8,619
University of Southern Mississippi	-	8,541
Mississippi Department of Transportation	1,485	-
University of Mississippi Medical Center	<u>2,508</u>	<u>-</u>
	<u>\$ 7,494,067</u>	<u>\$11,402,370</u>

(7) INVENTORIES

A summary of inventories follows:

	<u>2015</u>	<u>2014</u>
Finished goods	\$ 71,077	\$ 73,558
Raw materials and supplies	<u>123,935</u>	<u>98,994</u>
Total inventories	<u>\$ 195,012</u>	<u>\$ 172,552</u>

(8) OTHER OPERATING INCOME, NET

A summary of other operating income, net follows:

	<u>2015</u>	<u>2014</u>
Payroll processing income, net	\$ 58,718,218	\$ 53,862,169
Payroll processing expense	(58,688,720)	(53,127,169)
Other income	<u>278,136</u>	<u>174,341</u>
Other operating income, net	<u>\$ 307,634</u>	<u>\$ 909,341</u>

(9) RELATED PARTY TRANSACTIONS

Net transfers-in of \$7,776,579 in 2015 and \$5,862,600 in 2014 represent general and administrative expenses paid on behalf of the AbilityWorks' facilities by the State of Mississippi Department of Rehabilitation Services. Transfers-in are from sources as follows:

	<u>2015</u>	<u>2014</u>
MDRS - general and administrative expenses	\$ 7,776,579	\$ 7,862,600
MDRS - payroll processing	<u>-</u>	<u>(2,000,000)</u>
Total operating transfers	<u>\$ 7,776,579</u>	<u>\$ 5,862,600</u>

(10) FACILITIES

Production facilities utilized by seven AbilityWorks locations are provided without rent by the counties in which the facilities are located. The other eleven facilities reported rent expense of \$402,663 in 2015 and \$415,263 in 2014 under cancellable operating leases. During fiscal years 2015 and 2014, AbilityWorks offset a portion of the rent expense by charging state agencies which occupied space in the facilities an allocated portion of the related rent expense. The amount charged and offset against rent expense was \$209,514 for 2015 and 2014.

ABILITYWORKS, INC.

SCHEDULES OF COST OF PRODUCTION

Years Ended June 30, 2015 and 2014

	2015	2014
Bank charges	\$ 17,854	\$ 16,690
Commissions	159,351	165,433
Employee benefits	1,120,799	947,148
Equipment rent and maintenance	253,073	266,251
Facility repairs and maintenance	109,689	128,635
General shop and tools	69,936	77,374
Marketing	62,574	58,389
Miscellaneous	80,959	55,301
Opportunity wages production	1,958,096	2,228,433
Other administrative expenses	25,132	44,325
Professional fees	247,220	247,454
Rent	193,149	205,749
Salaries, non-client employees	2,675,088	2,786,540
Supplies	1,342,322	1,336,592
Uniforms	30,884	39,263
Vehicle expense	153,592	184,113
	<u> </u>	<u> </u>
Total cost of production	\$ 8,499,718	\$ 8,787,690

See Independent Auditors' Report.

ABILITYWORKS, INC.

SCHEDULES OF GENERAL AND ADMINISTRATIVE EXPENSES

Years Ended June 30, 2015 and 2014

	2015	2014
Client transportation	\$ 628,355	\$ 628,382
Commodities	14,157	51,288
Community based	805,210	884,246
Contractual services	419,802	534,404
Equipment	916	8,199
Salaries and related expenses	5,789,497	5,648,064
Subsidy - opportunity wages	118,227	107,420
Travel	415	597
	<u> </u>	<u> </u>
Total general and administrative expenses	\$ <u>7,776,579</u>	\$ <u>7,862,600</u>

See Independent Auditors' Report.

ABILITYWORKS, INC.

SCHEDULE OF STATISTICAL ANALYSIS OF OPERATIONS
Year Ended June 30, 2015
(Unaudited)

	Total per the Statement of Revenues, Expenses and Changes in Net Assets	Total Cost of Operations for Year in Relation to		
		Clients Served	Client Days	Clients Closed/ Rehabilitated
Cost of production	\$ 8,499,718	\$ 3,438	\$ 87	\$ 10,035
General and administrative expenses	<u>7,776,579</u>	<u>3,146</u>	<u>80</u>	<u>9,181</u>
Total operating cost	16,276,297	6,584	167	19,216
Less revenue and other operating income	<u>9,325,687</u>	<u>3,773</u>	<u>95</u>	<u>11,010</u>
Total operating cost, net of revenue and other operating revenue	6,950,610	2,811	72	8,206
Nonoperating (revenue) expense	<u>79,661</u>	<u>32</u>	<u>1</u>	<u>94</u>
Total operating cost after nonoperating (revenue) expense	<u>\$ 7,030,271</u>	<u>\$ 2,843</u>	<u>\$ 73</u>	<u>\$ 8,300</u>
Totals for the year ended June 30, 2015:				
Clients served	2,472			
Client days	97,706			
Clients closed/rehabilitated	847			
Average daily attendance	404			
Average length of stay	Client days	40		
per client in days	Clients served			

* Total operating cost after nonoperating expense does not include payroll processing income and payroll processing expenses. These items are not related to clients served and employed data and are appropriately not included in the above analysis.

See Independent Auditors' Report.



The Board of Directors
AbilityWorks, Inc.
Madison, Mississippi

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*

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the basic financial statements of AbilityWorks, Inc., a component unit of the State of Mississippi, as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise AbilityWorks, Inc.'s, a component unit of the State of Mississippi, basic financial statements, and have issued our report thereon dated November 23, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered AbilityWorks, Inc.'s, a component unit of the State of Mississippi, internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the internal control. Accordingly, we do not express an opinion on the effectiveness of AbilityWorks, Inc.'s, a component unit of the State of Mississippi, 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.

Internal Control Over Financial Reporting - continued

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 AbilityWorks, Inc.'s, a component unit of the State of Mississippi, basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

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 result of that testing, and is not to provide an opinion on the effectiveness of internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering AbilityWorks, Inc.'s, a component unit of the State of Mississippi, internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Harper, Raines, Knight & Company, P.A.

November 23, 2015