SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC. AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES FOUNDATION

COMBINED FINANCIAL STATEMENTS
JUNE 30, 2010

WINDES & MCCLAUGHRY
ACCOUNTANCY CORPORATION
Certified Public Accountants & Consultants
EXCEEDING EXPECTATIONS SINCE 1926

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
San Diego – Imperial Counties
Developmental Services, Inc. and
San Diego – Imperial Counties
Developmental Services Foundation

We have audited the accompanying combined statement of financial position of San Diego – Imperial Counties Developmental Services, Inc. and San Diego – Imperial Counties Developmental Services Foundation (California nonprofit corporations) as of June 30, 2010, and the related combined statements of activities, functional expenses, and cash flows for the year then ended. These combined financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these combined financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. The financial statements of San Diego – Imperial Counties Developmental Services Foundation were not audited in accordance with *Government Auditing Standards*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of San Diego – Imperial Counties Developmental Services, Inc. and San Diego – Imperial Counties Developmental Services Foundation as of June 30, 2010, and the changes in their net assets and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 28, 2011, on our consideration of the San Diego – Imperial Counties Developmental Services, 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 audit.

Our audit was conducted for the purpose of forming an opinion on the basic combined financial statements of San Diego – Imperial Counties Developmental Services, Inc. and San Diego - Imperial Counties Developmental Services Foundation taken as a whole. The schedules of combined statements of financial position and of activities are presented for purposes of additional analysis and are not a required part of the basic combined financial statements of the Organization. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations,* and is also not a required part of the basic combined financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic combined financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic combined financial statements taken as a whole.

Windes & McClaughry

Long Beach, California
February 28, 2011

SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC. AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES FOUNDATION

COMBINED STATEMENT OF FINANCIAL POSITION
JUNE 30, 2010

ASSETS

ASSETS	
Cash and cash equivalents	$ 22,976,412
Cash – client trust funds	1,814,825
Restricted cash	2,592,988
Contracts receivable from state and federal agencies	18,324,297
Investments	622,461
Sundry receivables, prepaids, and other assets	696,282
Due from state-accrued leave and retirement benefits	11,232,177
Property and equipment	9,026,061
TOTAL ASSETS	$ 67,285,503

LIABILITIES AND NET DEFICIT

LIABILITIES	
Accounts payable	$ 20,899,040
Accrued payroll	952,599
Line of credit	19,245,000
Amounts payable under retirement plan	34,919,064
Accrued leave benefits	1,644,069
Amounts held for clients	1,762,032
Bonds payable	9,000,000
	88,421,804
COMMITMENTS AND CONTINGENCIES (Notes 8, 9 and 10)	
NET DEFICIT	
Unrestricted	(21,136,301)
TOTAL LIABILITIES AND NET DEFICIT	$ 67,285,503

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

**SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC.
AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL
SERVICES FOUNDATION**

**COMBINED STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2010**

CHANGE IN UNRESTRICTED NET ASSETS	
SUPPORT AND REVENUE	
Contracts – state and federal agencies	$ 242,363,956
Interest and dividend income	284,126
Unrealized gain on investments, net	26,098
Donations	149,342
Rental related and other income	577,712
	243,401,234
EXPENSES	
Program Services	
Client services	32,839,165
Residential care	55,572,515
Day care and training	77,214,327
Medical programs	2,623,194
Camps and respite service	22,647,182
Independent living costs	16,991,674
Transportation services	12,495,736
Prevention services	3,078,708
Other purchased services	14,382,055
	237,844,556
Supporting Services	
General and administrative	4,955,467
Total Expenses	242,800,023
CHANGE IN NET DEFICIT BEFORE PENSION-RELATED CHANGES OTHER THAN NET PERIODIC PENSION COST	601,211
PENSION-RELATED CHANGES OTHER THAN NET PERIODIC POST-RETIREMENT BENEFIT COST	(773,344)
CHANGE IN NET DEFICIT	(172,133)
NET DEFICIT AT BEGINNING OF YEAR	
As previously reported	(22,500,811)
Adjustment (Note 12)	1,536,643
As restated	(20,964,168)
NET DEFICIT AT END OF YEAR	($ 21,136,301)

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

**SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC.
AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL
SERVICES FOUNDATION**

**COMBINED STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2010**

	Program Services				
	Client Services	Residential Care	Day Care and Training	Medical Programs	Camps and Respite Service
Salaries	$ 19,562,872				
Employee health and retirement benefits	7,494,480				
Payroll taxes	287,366				
Total salaries and related expenses	27,344,718				
Purchase of services		$ 55,572,515	$ 77,214,327	$ 2,623,194	$ 22,647,182
Facility maintenance	359,876				
Postage	130,837				
General expenses	762,929				
ARCA dues	58,050				
Accounting fees	70,327				
Printing	30,409				
Insurance	245,169				
Board expenses	15,762				
Legal fees	407,687				
Utilities	225,875				
Public information and education	444,127				
Staff training	9,455				
Outside services	219,043				
Depreciation and amortization	169,031				
Telephone	231,290				
Building rent	1,018,556				
Equipment purchases, rental, and maintenance	281,490				
Interest expense	430,296				
Travel	384,238				
	$ 32,839,165	$ 55,572,515	$ 77,214,327	$ 2,623,194	$ 22,647,182

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

Independent Living Costs	Transportation Services	Prevention Services	Other Purchased Services	Total	Supporting Services General and Administrative	Total Expenses
				$ 19,562,872	$ 3,117,137	$ 22,680,009
				7,494,480	962,415	8,456,895
				287,366	45,789	333,155
				27,344,718	4,125,341	31,470,059
$ 16,991,674	$ 12,495,736	$ 3,078,708	$ 14,382,055	205,005,391		205,005,391
				359,876	57,342	417,218
				130,837	20,848	151,685
				762,929	113,441	876,370
				58,050	9,250	67,300
				70,327	11,206	81,533
				30,409	4,845	35,254
				245,169	39,065	284,234
				15,762	2,511	18,273
				407,687	64,961	472,648
				225,875	35,991	261,866
				444,127	70,767	514,894
				9,455	1,506	10,961
				219,043	34,902	253,945
				169,031	26,933	195,964
				231,290	36,854	268,144
				1,018,556	162,296	1,180,852
				281,490	44,853	326,343
				430,296	68,563	498,859
				384,238	23,992	408,230
$ 16,991,674	$ 12,495,736	$ 3,078,708	$ 14,382,055	$ 237,844,556	$ 4,955,467	$ 242,800,023

SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC.
AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL
SERVICES FOUNDATION

COMBINED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2010

CASH FLOWS FROM OPERATING ACTIVITIES	
Change in net deficit	($ 172,133)
Adjustments to reconcile change in net deficit to net cash from operating activities:	
Depreciation	175,846
Amortization of bond issuance costs	20,118
Unrealized gain on investments	(26,098)
(Increase) decrease in:	
Cash – client trust funds	(15,011)
Restricted cash	(225,955)
Contracts receivable from state and federal agencies	(8,798,535)
Sundry receivables, prepaids, and other assets	25,367
Due from state-accrued leave and retirement benefits	(1,825,669)
Increase (decrease) in:	
Accounts payable	649,201
Accrued payroll	(39,887)
Amounts payable under retirement plan	2,648,556
Accrued leave benefits	(49,543)
Amounts held for clients	13,406
Net Cash Used In Operating Activities	(7,620,337)
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of investments	(53,813)
Proceeds from sale of investments	52,303
Purchase of property and equipment	(103,815)
Net Cash Used In Investing Activities	(105,325)
CASH FLOWS FROM FINANCING ACTIVITIES	
Net proceeds from line of credit	19,117,059
Repayment of bonds payable	(250,000)
Net Cash Provided By Financing Activities	18,867,059
NET CHANGE IN CASH AND CASH EQUIVALENTS	11,141,397
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	11,835,015
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 22,976,412

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

NOTE 1 – Summary of Significant Accounting Policies

Basis of Presentation

San Diego – Imperial Counties Developmental Services, Inc. (SDICDSI) is a nonprofit public benefit corporation, the primary purpose of which is to contract with the State of California Department of Developmental Services (DDS) and other governmental agencies to operate a regional center for persons with developmental disabilities and their families. The regional center was organized in accordance with the provisions of the Lanterman Developmental Disabilities Services Act (the Act) of the Welfare and Institutions Code of the State of California. Contracts with the state and other agencies are generally renewed on an annual basis and provide a limit on expenditures and the respective contract funding. The period of expenditure reimbursement may, in some cases, extend beyond one year. Required services provided include outreach, diagnosis, assessment, counseling, prevention services, public information and education, and advocacy to persons with developmental disabilities and their families residing in San Diego and Imperial Counties.

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

The regional center contract between SDICDSI and the DDS stipulates that funded expenditures are not to exceed $242,069,641 for the 2009-2010 contract year. Actual net expenditures under the regional center contract for the 2009-2010 contract was $241,034,416 as of June 30, 2010.

NOTE 1 – Summary of Significant Accounting Policies (Continued)

Basis of Presentation (Continued)

As discussed above, SDICDSI operates under contracts with the DDS. Contract revenue is funded on a cost reimbursement basis. The net deficit reported as of June 30, 2010 on the statement of financial position is primarily the result of the implementation of an accounting standard regarding the reporting of SDICDSI's defined benefit pension plan. As further discussed in Note 9, the accounting standard required SDICDSI to recognize as a charge to net assets the actuarial losses and prior service cost which had not yet been recognized as components of periodic benefit costs. For purposes of reporting periodic benefit costs, the unrecognized actuarial losses and prior service costs will continue to be amortized into plan expenses over future years. Periodic benefit costs under the defined benefit pension plan are reimbursed under the DDS contract as SDICDSI funds the plan.

Combination

The accompanying combined financial statements include the financial statements of SDICDSI and the San Diego – Imperial Counties Developmental Services Foundation (the Foundation) hereafter referred to as, collectively, the Organization. Intercompany transactions and accounts are eliminated in the accompanying combined financial statements.

The Foundation is a separately incorporated, nonprofit organization in which SDICDSI is the sole member and exercises significant influence. The Foundation was organized to provide fund-raising and other services to benefit children and adults with developmental disabilities residing in San Diego and Imperial Counties.

Financial Statement Presentation

The Organization is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted, and permanently restricted. As of June 30, 2010, the Organization had no temporarily or permanently restricted net assets.

Contributions

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor-imposed restrictions.

NOTE 1 – Summary of Significant Accounting Policies (Continued)

Use of Estimates and Assumptions

Management uses estimates and assumptions in preparing combined financial statements in accordance with accounting principles generally accepted in the United States of America. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported support, revenues, and expenses. Actual results could vary from the estimates that were assumed in preparing the combined financial statements.

Cash and Cash Equivalents and Concentration of Credit Risk

For purposes of the combined statement of cash flows, the Organization considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

At June 30, 2010 and throughout the year, the Organization has maintained cash balances with one of its financial institutions in excess of federally insured limits. Given the current economic environment and risks in the banking industry, there is risk that these deposits may not be readily available or covered by insurance.

Contracts Receivable from State and Federal Agencies

Contracts receivable from state and federal agencies and contract support are recorded on the accrual method as related expenses are incurred.

Investments

Investments are recorded at fair market value. Unrealized gains and losses are included in the change in net assets (deficit).

Property and Equipment

Pursuant to the terms of the DDS contract, SDICDSI equipment purchases become the property of DDS and, accordingly, are charged as expense when incurred. Property and equipment pertaining to the Foundation and corporate funds are stated at cost and depreciated using the straight-line method over their estimated useful lives.

NOTE 1 – Summary of Significant Accounting Policies (Continued)

Long-Lived Assets

The Organization reviews long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Organization records impairment losses on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amounts. Any long-lived assets held for disposal are reported at the lower of their carrying amounts or fair value less costs to sell.

Leave and Retirement Benefits

SDICDSI has accrued a liability for leave benefits earned and retirement obligations discussed in Note 9. However, such benefits are reimbursed under the DDS contract only when actually paid. SDICDSI has also recorded a receivable from the DDS for the accrued benefits to reflect the future reimbursement of such benefits.

Defined Benefit Pension Plan

The Organization recognizes the funded status of a benefit plan, measured as the difference between plan assets at fair value and the benefit obligation, in the statement of financial position, with an offsetting charge or credit to net assets. Gains or losses and prior service costs or credits that arise during the period but are not recognized as components of net period benefit cost will be recognized each year as a separate charge or credit to net assets (deficit).

Allocation of Expenses

The combined statement of functional expenses allocates expenses to the program and supporting service categories based on a direct-cost basis for purchase of services expenses, including salaries and related expenses. Operating expenses are allocated based on a percentage of salaries per category to total salaries, except for travel, which is allocated on a direct-cost basis.

NOTE 1 – Summary of Significant Accounting Policies (Continued)

Income Tax Status

The Organization has received tax-exempt status from the Internal Revenue Service and California Franchise Tax Board under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the Revenue and Taxation Code. Tax-exempt status is generally granted to nonprofit entities organized for charitable or mutual benefit purposes.

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

Subsequent Events

The Organization has evaluated subsequent events from the combined statement of financial position date through February 28, 2011, the date at which the combined financial statements were available to be issued for the year ended June 30, 2010, and determined there are no other items to disclose.

NOTE 2 – Cash-Client Trust Funds

SDICDSI functions as custodian for receipt of certain governmental payments and resulting disbursements made on behalf of regional center clients. The cash balances are segregated from the operating cash accounts of SDICDSI and are restricted for client support. The following is a summary of operating cash activity for the fiscal year ended June 30, 2010:

Social Security and other client support received	$25,283,989
Residential care and other disbursements	25,267,576
Support over disbursements	16,413
Changes to reconcile support over disbursements to net cash for support and care activities:	
Increase (decrease) in amounts due to SDICDSI	31,379
(Increase) decrease in receivable from state and federal agencies	(32,781)
Increase in cash	15,011
Cash at beginning of year	1,799,814
Cash at end of year	$ 1,814,825

NOTE 3 – Restricted Cash

Pursuant to the terms of a Bond agreement, various funds have been established. (See Note 8.) Reserved cash has been set aside as follows as of June 30, 2010:

Reserve fund	$ 943,317
Debt services	555,475
Capital improvements	1,094,196
	$ 2,592,988

NOTE 4 – Contract Advances from State

As of June 30, 2010, the DDS had advanced SDICDSI $38,692,537 under the regional center contracts. For financial statement presentation, to the extent there are claims receivable, these advances have been offset against the claims receivable from the DDS.

Contracts receivable	$ 57,016,834
Contract advances	(38,692,537)
Net contracts receivable	$ 18,324,297

NOTE 5 – Investments

The Organization accounts for investments at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A recent accounting standard has established a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Organization has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for the asset or liability.

The level in the fair value hierarchy within which a fair measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety.

NOTE 5 – Investments (Continued)

The following table sets forth by level, within the fair value hierarchy, investment assets at fair value:

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Fixed Income				
Certificate of Deposit	$ 275,875		$ 275,875	
U.S. Treasury	29,216	$ 29,216		
Mutual Funds				
Equity based	317,370	317,370		
Total assets at fair value	$ 622,461	$ 346,586	$ 275,875	None

Investment income is summarized as follows as of June 30, 2010:

Interest and dividends	$ 16,378
Unrealized and realized gain, net	26,098
	$ 42,476

NOTE 6 – Property and Equipment

Property and equipment consists of the following as of June 30, 2010:

		Estimated Useful Lives
Building and improvements	$ 5,096,813	10-40 years
Equipment	33,824	5 years
	5,130,637	
Less accumulated depreciation	(1,104,576)	
	4,026,061	
Land	5,000,000	
	$ 9,026,061	

NOTE 7 – Line of Credit

The Organization has a revolving line of credit agreement with a bank. Subsequent to year-end, the agreement was amended to allow the Organization to borrow up to $39,848,000 through July 30, 2010. Borrowings are secured by substantially all assets of the Organization with interest payable monthly at an interest rate of 3.25% at June 30, 2010. The amount outstanding at June 30, 2010 was $19,245,000.

NOTE 8 – Bonds Payable

In September 2002, the Foundation issued $10,750,000 Certificates of Participation Series 2002 bonds (the Certificates) through the County of San Diego. The bonds are secured by a deed of trust with assignment of rents and fixture filing. The proceeds received from the sale of the Certificates were used by the Foundation to purchase the main office building and related capital improvements, to fund a reserve and project fund for the Certificates, and to pay certain delivery costs of the Certificates. The Foundation incurred bond issuance costs in the amount of $492,898, included in sundry receivables, prepaids and other assets, which are amortized under the interest method over the life of the related bonds payable. Total accumulated amortization as of June 30, 2010 was $157,593.

NOTE 8 – Bonds Payable (Continued)

The Certificates' interest rates and maturity dates are:

Term Certificates, 4.5%, due September 1, 2012	$ 750,000
Term Certificates, 5.5%, due September 1, 2017	2,250,000
Term Certificates, 5.5%, due September 1, 2027	6,000,000
	$ 9,000,000

Future principal payments on the bonds are as follows:

Year Ending June 30,	
2011	$ 250,000
2012	250,000
2013	250,000
2014	250,000
2015	500,000
Thereafter	7,500,000
	$ 9,000,000

Future amortization on bond issuance costs are as follows:

Year Ending June 30,	
2011	$ 20,118
2012	20,118
2013	20,118
2014	20,118
2015	20,118
Thereafter	234,715
	$ 335,305

SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC.
AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL
SERVICES FOUNDATION

NOTES TO THE COMBINED FINANCIAL STATEMENTS
JUNE 30, 2010

NOTE 9 – Defined Benefit Pension Plan

Effective July 1, 2004, SDICDSI adopted a defined benefit pension plan to provide retirement benefits for all employees. The benefits under the plan are funded in accordance with the insurance company contracts. SDICDSI is required to contribute an amount to the plan, after employee contributions to the retirement plan, of 6.2%, which is necessary to purchase the contracts that will fund the retirement benefits.

The following table sets forth the plan's funded status as determined at June 30, 2010:

RECONCILIATION OF BENEFIT OBLIGATION

Change in benefit obligation	
Obligation at beginning of year	$ 49,661,932
Service cost	2,521,246
Interest cost	2,875,723
Actuarial loss	3,344,092
Benefit paid	(693,656)
Benefit obligation at end of year	57,709,337
Change in plan assets	
Fair value of plan assets at beginning of year	17,391,424
Actual return on plan assets	1,704,917
Employer contribution	4,387,588
Benefit paid	(693,656)
Fair value of plan assets at end of year	22,790,273
Funded status	(34,919,064)
Net amount recognized in the combined statement of financial position	($ 34,919,064)

NOTE 9 – Defined Benefit Pension Plan (Continued)

Net periodic postretirement benefit cost consists of the following components:

Service cost	$ 2,521,246
Interest cost	2,875,723
Expected return on plan assets	(1,404,971)
Amortization of transition obligation	2,021,844
Amortization of net loss	248,958
Net periodic benefit cost	$ 6,262,800

All previously unrecognized actuarial gains or losses are reflected in the combined statement of financial position. The plan items not yet recognized as a component of periodic plan expenses, but included as a separate charge to net assets, are:

Unamortized net transition obligation	$ 14,152,910
Unamortized net loss	11,178,046
	$ 25,330,956

The above net amounts recognized as a separate charge to net assets (deficit) do not have an offsetting accrual from the DDS to reflect the future reimbursement of such benefits. The Organization has accrued a receivable from the DDS for the balance of the accrued benefit obligation of $9,588,108 as of June 30, 2010, representing the portion of the accrued benefit obligation which has been recognized as plan expense.

The accumulated benefit obligation was $47,342,318 at June 30, 2010. The unamortized net transition obligation as of June 30, 2010 is $14,152,910, with remaining amortization of seven years. Annual amortization is $2,021,844.

Assumptions

Weighted-average assumptions used to determine benefit obligations were as follows as of June 30, 2010:

Discount rate	5.50%
Rate of compensation increase	3.00%

NOTE 9 – Defined Benefit Pension Plan (Continued)

Assumptions (Continued)

Weighted-average assumptions used to determine net periodic benefit cost were as follows as of June 30, 2010:

Discount rate	5.50%
Expected long-term return on plan assets	7.50%
Rate of compensation increase	3.00%

Weighted-average asset allocations at year-end were as follows:

Asset Category		Target Allocation
Equity securities	57%	55%
Debt securities	43%	45%
	100%	100%

The investment objective of the plan is to provide a rate of return commensurate with a moderate degree of risk of loss of principal and return volatility. The pension plan assets are invested in a Group Annuity Contract through Minnesota Life Insurance Company. Investment responsibility for the assets is assigned to an Investment Policy Committee of the board of directors of SDICDSI. The assets of the plan are periodically rebalanced to remain within the desired target allocations.

Historical rates of return for individual asset classes and future estimated returns are used to develop expected rates of return. These rates of return are applied to the plan's investment policy to determine a range of expected returns.

NOTE 9 – Defined Benefit Pension Plan (Continued)

Assumptions (Continued)

The following table sets forth by level, within the fair value hierarchy, the plan's assets at fair value as of June 30, 2010:

	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Money market funds	$ 1,698,255		$ 1,698,255	
Mutual funds				
Fixed income	8,080,669	$ 8,080,669		
Equities	13,011,349	13,011,349		
Total	$ 22,790,273	$ 21,092,018	$ 1,698,255	None

Estimated Future Benefit Payments

The following estimated benefit payments, which reflect expected future service, as appropriate, are expected to be paid on a fiscal year basis:

Year Ending June 30,	
2011	$ 728,672
2012	$ 1,025,690
2013	$ 1,124,550
2014	$ 1,269,192
2015	$ 1,325,988
2016-2020	$12,401,238

Contributions

The Organization expects to contribute at least the minimum funding requirement to this plan in the fiscal year ending in 2010. In addition, it may contribute additional amounts not yet determined.

NOTE 10 – Commitments and Contingencies

Leases – As Lessee

SDICDSI leases facilities and certain equipment under operating leases expiring in various years through 2027. These leases, which may be renewed for periods up to five years, generally require the lessee to pay all maintenance, insurance, and property taxes and contain a termination clause in the event the annual contract between the DDS and SDICDSI is not renewed. Several leases are subject to periodic adjustment based on price indices or cost increases.

Rental expense for facilities and equipment for the year ended June 30, 2010 was $3,005,166. SDICDSI is leasing its main office from the Foundation. The Foundation received approximately $1,652,000 of rental income and common area and utility expense reimbursements from SDICDSI, which was eliminated upon combination against the total building rental expense of SDICDSI of approximately $2,832,000 for the year ended June 30, 2010.

Future minimum lease payments by SDICDSI for operating leases are as follows:

Year Ending June 30,	Related Party-Foundation	Other	Total
2011	$ 1,434,752	$ 1,044,026	$ 2,478,778
2012	1,477,794	987,329	2,465,123
2013	1,522,128	925,391	2,447,519
2014	1,567,792	637,309	2,205,101
2015	1,614,825	633,066	2,247,891
Thereafter	23,605,181	1,185,113	24,790,294
	$ 31,222,472	$ 5,412,234	$ 36,634,706

NOTE 10 – Commitments and Contingencies (Continued)

Leases – As Lessor

The following is a schedule by years of the Foundation's future minimum rents receivable under noncancellable operating leases that have initial or remaining lease terms in excess of one year as of June 30, 2010:

Year Ending June 30,	Related Party- SDICDSI	Other	Total
2011	$ 1,434,752	$ 91,197	$ 1,525,949
2012	1,477,794	66,587	1,544,381
2013	1,522,128	41,089	1,563,217
2014	1,567,792	31,447	1,599,239
2015	1,614,825		1,614,825
Thereafter	23,605,181		23,605,181
	$ 31,222,472	$ 230,320	$ 31,452,792

The following schedule provides an analysis of the Foundation's investment in property and equipment held for lease by major classes as of June 30, 2010:

Land and buildings	$ 9,400,000
Building improvements	696,813
	10,096,813
Less accumulated depreciation	(1,070,752)
	$ 9,026,061

Agreement with Insurance Company

SDICDSI had entered into an agreement with an insurance company that requires an irrevocable standby letter of credit for workers' compensation insurance. SDICDSI will pay or reimburse the insurance company for all premiums, administrative expenses, and claims incurred through March 1, 2006 up to a retained limit of $250,000 per incident. This agreement required SDICDSI to establish, in favor of the insurance company, an irrevocable standby letter of credit for $200,000 as security for the agreement. Effective March 1, 2006, SDICDSI changed its workers' compensation carrier and acquired non-participating coverage. The standby letter of credit of $200,000 related to the prior policy is being maintained as security for any potential prior policy claims.

NOTE 10 – Commitments and Contingencies (Continued)

Contingencies

In accordance with the terms of the DDS contract, an audit may be performed by an authorized state representative. Should such audit disclose any unallowable costs, SDICDSI may be liable to the state for reimbursement of such costs. In the opinion of the SDICDSI's management, the effect of any disallowed costs would be immaterial to the combined financial statements at June 30, 2010, and for the year then ended.

SDICDSI is dependent on continued funding provided by the DDS to operate and provide services for its clients. SDICDSI's contract with DDS provides funding for services under the Lanterman Act. In the event that the operations of SDICDSI result in a deficit position at the end of any contract year, DDS may reallocate surplus funds within the State of California system to supplement SDICDSI's funding. Should a system-wide deficit occur, DDS is required to report to the Governor of California and the appropriate fiscal committee of the State Legislature and recommend actions to secure additional funds or reduce expenditures. DDS's recommendations are subsequently reviewed by the Governor and the Legislature and a decision is made with regard to specific actions, including the possible suspension of the entitlement.

The State of California is experiencing an unprecedented budget shortfall due to the severe national and state economic crisis. The DDS has undertaken numerous efforts to control costs throughout the system and is committed to preserving the entitlement services and supports. Reductions in regional center operations and purchase of services are expected for the 2010/2011 fiscal year as a result of cost control efforts and legislation enacted.

SDICDSI has elected to self-insure its unemployment insurance. SDICDSI is required to reimburse the state of California for benefits paid to its former employees. In addition, SDICDSI has elected to self-insure a portion of its employee benefits based on actual costs of dental services performed. At June 30, 2010, SDICDSI had $202,009 held by an outside agency trust to pay for any potential claims.

SDICDSI is in the process of negotiating a union agreement with SEIU Local 221 and its labor force.

SDICDSI is involved in various claims and lawsuits arising in the normal conduct of its operations. SDICDSI management believes it has adequate defenses and insurance coverage for these actions and, thus, has made no provision in the combined financial statements for any costs relating to the settlement of such claims.

NOTE 11 – Supplemental Disclosure of Cash Flow Information

Interest expense paid during the year ended June 30, 2010 was $493,455.

NOTE 12 – Adjustment

Net assets at June 30, 2009 has been restated to reflect an additional amount due from the state for the accrued net periodic postretirement benefit cost recognized for the year ended June 30, 2009. Net assets was increased by $1,536,643 to reflect the support that should have been reported as a result of the additional employee benefit expense accrued for the retirement plan of $1,536,643 for the year ended June 30, 2009.

SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC. AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES FOUNDATION

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2010

Federal Grantor/ Pass-Through Grantor/ Grant Title	Federal CFDA Number	Grant Identification Number	Grant Expenditures
U.S. Department of Education			
Passed through State of California Department of Developmental Services			
Early Intervention Services (IDEA) Cluster:			
Special Education – Grants for Infants and Families	84.181	H181A090037	$ 2,347,833
ARRA – Special Education – Grants for Infants and Families, Recovery Act	84.393	H393A090037A	2,503,691
			$ 4,851,524

Basis of Presentation

The Schedule of Expenditures of Federal Awards includes the federal award activity of San Diego – Imperial Counties Developmental Services, Inc. and is prepared based on state contract budget allocations. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic consolidated financial statements.

**SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC.
AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL
SERVICES FOUNDATION**

**SUPPLEMENTARY INFORMATION
SCHEDULE OF COMBINED STATEMENT OF FINANCIAL POSITION
JUNE 30, 2010**

	SDICDSI	Foundation	Elimination Entries	Combined Balance
ASSETS				
Cash and cash equivalents	$ 22,566,029	$ 410,383		$ 22,976,412
Cash – client trust funds	1,814,825			1,814,825
Restricted cash		2,592,988		2,592,988
Contracts receivable from state and federal agencies	18,324,297			18,324,297
Investments		622,461		622,461
Sundry receivables, prepaids, and other assets	338,530	357,752		696,282
Due from state-accrued leave and retirement benefits	11,232,177			11,232,177
Property and equipment		9,026,061		9,026,061
TOTAL ASSETS	$ 54,275,858	$ 13,009,645		$ 67,285,503
LIABILITIES				
Accounts payable	$ 20,613,035	$ 286,005		$ 20,899,040
Accrued payroll	952,599			952,599
Line of credit	19,245,000			19,245,000
Amounts payable under retirement plan	34,919,064			34,919,064
Accrued leave benefits	1,644,069			1,644,069
Amounts held for clients	1,762,032			1,762,032
Bonds payable		9,000,000		9,000,000
	79,135,799	9,286,005		88,421,804
NET ASSETS (DEFICIT)				
Unrestricted	(24,859,941)	3,723,640		(21,136,301)
TOTAL LIABILITIES AND NET ASSETS	$ 54,275,858	$ 13,009,645		$ 67,285,503

SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC.
AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES FOUNDATION

SUPPLEMENTARY INFORMATION
SCHEDULE OF COMBINED STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2010

	SDICDSI	Foundation	Elimination Entries	Combined Balance
SUPPORT AND REVENUE				
Contracts – state and federal agencies	$ 242,363,956			$ 242,363,956
Interest and dividend income	266,952	$ 17,174		284,126
Unrealized gain on investments		26,098		26,098
Donations		149,342		149,342
Rental related and other income	482,462	1,747,225	($ 1,651,975)	577,712
	243,113,370	1,939,839	(1,651,975)	243,401,234
EXPENSES				
Program Services				
Client services	32,788,179	50,986		32,839,165
Residential care	55,572,515			55,572,515
Day care and training	77,214,327			77,214,327
Medical programs	2,623,194			2,623,194
Camps and respite service	22,647,182			22,647,182
Independent living costs	16,991,674			16,991,674
Transportation services	12,495,736			12,495,736
Prevention services	3,078,708			3,078,708
Other purchased services	14,382,055			14,382,055
	237,793,570	50,986		237,844,556
Supporting Services				
General and administrative	5,315,617	1,291,825	(1,651,975)	4,955,467
Total Expenses	243,109,187	1,342,811	(1,651,975)	242,800,023
CHANGE IN NET ASSETS BEFORE PENSION-RELATED CHANGES OTHER THAN NET PERIODIC PENSION COST	4,183	597,028		601,211
PENSION-RELATED CHANGES OTHER THAN NET PERIODIC PENSION COST	(773,344)			(773,344)
CHANGE IN NET ASSETS	(769,161)	597,028		(172,133)
NET ASSETS (DEFICIT) AT BEGINNING OF YEAR	(24,090,780)	3,126,612		(20,964,168)
NET ASSETS (DEFICIT) AT END OF YEAR	($ 24,859,941)	$ 3,723,640	None	($ 21,136,301)

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

To the Board of Directors of
San Diego – Imperial Counties
Developmental Services, Inc. and
San Diego – Imperial Counties
Developmental Services Foundation

We have audited the combined financial statements of San Diego – Imperial Counties Developmental Services, Inc. and San Diego – Imperial Counties Developmental Services Foundation as of and for the year ended June 30, 2010, and have issued our report thereon dated February 28, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. The financial statements of San Diego – Imperial Counties Developmental Services Foundation were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered San Diego – Imperial Counties Developmental Services, Inc.'s and San Diego – Imperial Counties Developmental Services Foundation's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the combined financial statements, but not for the purpose of expressing an opinion on the effectiveness of San Diego – Imperial Counties Developmental Services, Inc. and San Diego – Imperial Counties Developmental Services Foundation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control over financial reporting.

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.

Our consideration of internal control over financial reporting 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 financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether San Diego – Imperial Counties Developmental Services, Inc's. and San Diego – Imperial Counties Developmental Services Foundation's combined 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 combined 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*.

We noted certain other matters that we reported to management of San Diego – Imperial Counties Developmental Services, Inc's. and San Diego – Imperial Counties Developmental Services Foundation in a separate letter dated February 28, 2011.

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

Windes & McClaughry

Long Beach, California
February 28, 2011

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INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Directors of
San Diego – Imperial Counties
Developmental Services, Inc. and
San Diego – Imperial Counties
Developmental Services Foundation

Compliance

We have audited San Diego – Imperial Counties Developmental Services, Inc.'s compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct material effect on each of San Diego – Imperial Counties Developmental Services, Inc.'s major federal programs for the year ended June 30, 2010. San Diego – Imperial Counties Developmental Services, Inc.'s major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of San Diego – Imperial Counties Developmental Services, Inc.'s management. Our responsibility is to express an opinion on San Diego – Imperial Counties Developmental Services, Inc.'s compliance based on our audit.

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 OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 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 San Diego – Imperial Counties Developmental Services, 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. Our audit does not provide a legal determination of San Diego – Imperial Counties Developmental Services, Inc.'s compliance with those requirements.

In our opinion, San Diego – Imperial Counties Developmental Services, Inc. complied, in all material respects, with the 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, 2010.

Internal Control Over Compliance

Management of San Diego – Imperial Counties Developmental Services, Inc. is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered San Diego – Imperial Counties Developmental Services, Inc.'s internal control over compliance with requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance, and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 San Diego – Imperial Counties Developmental Services, 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.

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 deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

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

Windes & McClaughry

Long Beach, California
February 28, 2011

SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES, INC. AND SAN DIEGO – IMPERIAL COUNTIES DEVELOPMENTAL SERVICES FOUNDATION

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED JUNE 30, 2010

SECTION I - SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued – Unqualified

Internal control over financial reporting

1. Material weakness(es) identified? – No
2. Significant deficiencies identified that are not considered to be material weaknesses? – None reported
3. Noncompliance material to combined financial statements noted? – No

Federal Awards

Internal control over major programs

1. Material weakness(es) identified? – No
2. Significant deficiencies identified that are not considered to be material weakness(es)? – None reported
3. Type of auditors' report issued on compliance for major programs? – Unqualified
4. Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? – No
5. Identification of major programs: Early Intervention Services (IDEA) Cluster – Special Education – Grants for Infants and Families, CFDA #84.181, and ARRA – Special Education – Grants for Infants and Families, Recovery Act, CFDA #84.393
6. Dollar threshold used to distinguish between Type A and Type B programs was $300,000.
7. Auditee qualified as low-risk auditee? – Yes

SECTION II - FINANCIAL STATEMENTS FINDINGS

None

SECTION III – MAJOR FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

None