

**GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA
AND AFFILIATES**

CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA
AND AFFILIATES

CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

CONTENTS

INDEPENDENT AUDITOR'S REPORT	1
FINANCIAL STATEMENTS:	
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION	3
CONSOLIDATED STATEMENTS OF ACTIVITIES	4
CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES	6
CONSOLIDATED STATEMENTS OF CASH FLOWS	8
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.....	9
SUPPLEMENTARY INFORMATION:	
SUPPLEMENTAL SCHEDULE – CLASSIFIED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION.....	29

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Goodwill Industries of Southern California and Affiliates
Los Angeles, California

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Goodwill Industries of Southern California and Affiliates (collectively, the "Organization"), which comprise the consolidated statements of financial position as of December 31, 2018 and 2017, and the related consolidated statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated 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 consolidated financial statements.

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

(Continued)

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Goodwill Industries of Southern California and Affiliates as of December 31, 2018 and 2017, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters*Supplementary Information*

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

Emphasis of Matter

As discussed in Note 2 to the financial statements, the Organization has adopted ASU 2016-14 - *Not-For-Profit Entities (Topic 958): Presentation of Financial Statements of Not-For-Profit Entities*. Our opinion is not modified with respect to this matter.



Crowe LLP

Los Angeles, California
May 9, 2019

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
ASSETS		
Cash and cash equivalents	\$ 14,290,386	\$ 13,193,618
Cash and cash equivalents designated for improvements	331,690	533,350
Investments (Note 5)	19,890,051	21,091,188
Accounts receivable, net	4,363,474	4,166,541
Inventory	8,731,781	7,630,764
Prepaid expenses and deposits	2,249,575	2,716,146
Other receivables (Note 6)	2,386,600	1,495,182
Property, plant and equipment, net (Note 7)	<u>28,957,183</u>	<u>30,209,970</u>
Total assets	<u>\$ 81,200,740</u>	<u>\$ 81,036,759</u>
LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable and accrued liabilities	\$ 10,719,638	\$ 10,360,991
Accrued compensation and related expenses	6,113,988	5,741,081
Accrued insurance claims (Note 12)	16,378,596	15,835,995
Deferred rent	4,036,979	4,080,806
Deferred gain on sale-leaseback (Note 7)	3,454,974	3,836,464
Deferred rent - construction allowance (Note 7)	2,697,727	3,005,416
Capitalized lease obligation (Note 8)	386,368	446,495
Note payable (Note 8)	<u>8,805,148</u>	<u>9,126,620</u>
Total liabilities	<u>52,593,418</u>	<u>52,433,868</u>
Net assets (Note 9)		
Net assets without donor restrictions	20,973,294	21,144,157
Net assets with donor restrictions	<u>7,634,028</u>	<u>7,458,734</u>
Total net assets	<u>28,607,322</u>	<u>28,602,891</u>
Total liabilities and net assets	<u>\$ 81,200,740</u>	<u>\$ 81,036,759</u>

See accompanying notes to consolidated financial statements.

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
CONSOLIDATED STATEMENT OF ACTIVITIES
For the year ended December 31, 2018

	<u>Net Assets Without Donor Restrictions</u>	<u>Net Assets With Donor Restrictions</u>	<u>Total</u>
Revenues			
Operating revenues			
Retail sales	\$ 124,981,322	\$ -	\$ 124,981,322
Commodities sales	583,872	-	583,872
Contract services	7,233,080	-	7,233,080
Workforce development revenues	7,953,141	-	7,953,141
Workforce development – government grants	5,079,657	-	5,079,657
Other	<u>922,047</u>	<u>-</u>	<u>922,047</u>
	146,753,119	-	146,753,119
Other revenues and support			
Contributions	4,264,474	3,494,790	7,759,264
Contributions to capital campaign	-	381	381
Interest and dividends	508,996	-	508,996
Contributed goods	83,068,092	-	83,068,092
Gain on sale of property	97,990	-	97,990
Net assets released from restriction	<u>2,835,904</u>	<u>(2,835,904)</u>	<u>-</u>
Total revenues and support	237,528,575	659,267	238,187,842
Expenses			
Program services	224,953,217	-	224,953,217
Fundraising	2,440,690	-	2,440,690
General and administrative	<u>9,733,559</u>	<u>-</u>	<u>9,733,559</u>
Total operating expense	237,127,466	-	237,127,466
Changes in net assets from operations	401,109	659,267	1,060,376
Other changes in net assets			
Realized and unrealized (loss) on investments, net	<u>(571,972)</u>	<u>(483,973)</u>	<u>(1,055,945)</u>
Changes in net assets	(170,863)	175,294	4,431
Net assets, beginning of the year	<u>21,144,157</u>	<u>7,458,734</u>	<u>28,602,891</u>
Net assets, end of year	<u>\$ 20,973,294</u>	<u>\$ 7,634,028</u>	<u>\$ 28,607,322</u>

See accompanying notes to consolidated financial statements.

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
CONSOLIDATED STATEMENT OF ACTIVITIES
For the Year Ended December 31, 2017

	<u>Net Assets Without Donor Restrictions</u>	<u>Net Assets With Donor Restrictions</u>	<u>Total</u>
Revenues			
Operating revenues			
Retail sales	\$ 117,020,125	\$ -	\$ 117,020,125
Commodities sales	1,082,833	-	1,082,833
Contract services	8,400,513	-	8,400,513
Workforce development revenues	7,243,314	-	7,243,314
Workforce development - government grants	6,683,395	-	6,683,395
Other	<u>852,336</u>	<u>-</u>	<u>852,336</u>
	141,282,516	-	141,282,516
Other revenues and support			
Contributions	2,383,935	3,084,960	5,468,895
Contributions to capital campaign	-	19,544	19,544
Interest and dividends	467,952	-	467,952
Contributed goods	78,835,939	-	78,835,939
Gain on sale of property	1,490	-	1,490
Net assets released from restriction	<u>1,936,503</u>	<u>(1,936,503)</u>	<u>-</u>
Total revenues and support	224,908,335	1,168,001	226,076,336
Expenses			
Program services	214,708,012	-	214,708,012
Fundraising	1,985,544	-	1,985,544
General and administrative	<u>10,577,468</u>	<u>-</u>	<u>10,577,468</u>
Total operating expense	227,271,024	-	227,271,024
Changes in net assets from operations	(2,362,689)	1,168,001	(1,194,688)
Other changes in net assets			
Realized and unrealized gain on investments, net	<u>1,653,333</u>	<u>465,530</u>	<u>2,118,863</u>
Changes in net assets	(709,356)	1,633,531	924,175
Net assets, beginning of the year	<u>21,853,513</u>	<u>5,825,203</u>	<u>27,678,716</u>
Net assets, end of year	<u>\$ 21,144,157</u>	<u>\$ 7,458,734</u>	<u>\$ 28,602,891</u>

See accompanying notes to consolidated financial statements.

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
For the Year Ended December 31, 2018

	Program Services					Support Services		Total Expenses
	Material Handling	Stores	Contract Services	Workforce Development	Total	Fundraising	General Administrative	
Salaries and wages	\$ 20,761,327	\$ 25,554,600	\$ 4,542,560	\$ 10,418,376	\$ 61,276,863	\$ 1,337,184	\$ 4,618,834	\$ 67,232,881
Payroll taxes	1,528,254	1,927,270	337,308	779,014	4,571,846	94,279	256,858	4,922,983
Employee benefits	3,178,546	4,024,521	686,807	1,502,730	9,392,604	191,871	612,476	10,196,951
Total salaries and related expenses	25,468,127	31,506,391	5,566,675	12,700,120	75,241,313	1,623,334	5,488,168	82,352,815
Contributed goods - cost of goods sold	-	81,617,577	-	-	81,617,577	-	-	81,617,577
Rents	7,118,865	20,411,893	6,500	438,762	27,976,020	-	-	27,976,020
Occupancy	3,480,550	4,558,417	466,865	1,942,414	10,448,246	209,383	706,851	11,364,480
Professional services and temporary labor	1,771,526	1,783,435	260,174	415,487	4,230,622	180,013	733,713	5,144,348
Participant training and support	-	-	-	2,793,443	2,793,443	-	-	2,793,443
Technology and communication	424,876	1,518,187	144,533	368,020	2,455,616	85,777	1,188,262	3,729,655
Utilities	163,517	2,440,599	-	7,736	2,611,852	-	-	2,611,852
Supplies	225,770	1,552,409	570,395	257,785	2,606,359	10,056	37,414	2,653,829
Trash disposal	2,849,709	6,118	-	697	2,856,524	-	-	2,856,524
Transportation	2,445,578	103,321	98,743	11,685	2,659,327	1,224	8,730	2,669,281
Banking and finance fees	43,579	1,304,547	7,373	3,353	1,358,852	-	(34,885)	1,323,967
Insurance	359,931	752,314	110,048	142,809	1,365,102	15,785	531,010	1,911,897
Postage and shipping	6,642	1,192,516	1,701	2,334	1,203,193	135,199	23,946	1,362,338
Repairs and maintenance	161,958	718,729	20,664	20,687	922,038	3,818	10,258	936,114
Travel, conference and meetings	11,012	71,047	54,995	312,513	449,567	73,876	46,308	569,751
Printing, publications and media	412	148,500	134	33,921	182,967	90,958	1,674	275,599
Other (taxes, licenses and dues)	4,492	7,018	11,590	17,995	41,095	2,237	244,854	288,186
Interest	20,138	-	-	-	20,138	-	333,190	353,328
Depreciation	934,708	2,235,494	346,968	396,196	3,913,366	9,030	414,066	4,336,462
	<u>\$ 45,491,390</u>	<u>\$ 151,928,512</u>	<u>\$ 7,667,358</u>	<u>\$ 19,865,957</u>	<u>\$ 224,953,217</u>	<u>\$ 2,440,690</u>	<u>\$ 9,733,559</u>	<u>\$ 237,127,466</u>

See accompanying notes to consolidated financial statements.

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
For the Year Ended December 31, 2017

	Program Services					Support Services		Total Expenses
	Material Handling	Stores	Contract Services	Workforce Development	Total	Fundraising	General Administrative	
Salaries and wages	\$ 20,427,768	\$ 23,791,916	\$ 5,002,640	\$ 10,586,964	\$ 59,809,288	\$ 1,007,590	\$ 5,088,389	\$ 65,905,267
Payroll taxes	1,507,855	1,777,273	373,752	713,597	4,372,477	59,998	307,223	4,739,698
Employee benefits	<u>3,036,613</u>	<u>3,854,213</u>	<u>719,015</u>	<u>1,582,567</u>	<u>9,192,408</u>	<u>149,691</u>	<u>705,462</u>	<u>10,047,561</u>
Total salaries and related expenses	24,972,236	29,423,402	6,095,407	12,883,128	73,374,173	1,217,279	6,101,074	80,692,526
Contributed goods - cost of goods sold	-	77,928,194	-	-	77,928,194	-	-	77,928,194
Rents	6,775,013	18,778,400	5,500	330,097	25,889,010	-	-	25,889,010
Occupancy	2,599,518	4,507,744	1,313,830	1,692,153	10,113,245	138,612	585,894	10,837,751
Professional services and temporary labor	1,506,228	1,481,897	236,982	569,080	3,794,187	232,703	1,463,450	5,490,340
Participant training and support	-	-	-	2,964,542	2,964,542	-	-	2,964,542
Technology and communication	241,728	1,135,997	89,018	294,518	1,761,261	19,378	1,056,200	2,836,839
Utilities	160,728	2,496,878	-	76,283	2,733,889	-	-	2,733,889
Supplies	391,914	1,338,407	472,547	268,669	2,471,537	5,076	84,340	2,560,953
Trash disposal	2,240,029	31,935	-	-	2,271,964	-	-	2,271,964
Transportation	1,926,530	135,686	106,614	60,022	2,228,852	898	21,649	2,251,399
Banking and finance fees	79,288	1,281,094	107,930	5,269	1,473,581	187	(56,571)	1,417,197
Insurance	329,876	622,321	69,366	107,652	1,129,215	10,392	253,550	1,393,157
Postage and shipping	4,887	884,464	703	2,942	892,996	277,689	27,510	1,198,195
Repairs and maintenance	170,228	690,627	15,310	102,401	978,566	-	2,978	981,544
Travel, conference and meetings	9,571	98,002	70,706	242,445	420,724	16,453	116,372	553,549
Printing, publications and media	6,355	317,488	1,332	2,323	327,498	56,844	-	384,342
Other (taxes, licenses and dues)	4,209	6,330	1,178	9,221	20,938	1,003	212,891	234,832
Interest	16,027	-	-	-	16,027	-	311,995	328,022
Depreciation	<u>935,720</u>	<u>2,237,924</u>	<u>347,344</u>	<u>396,625</u>	<u>3,917,613</u>	<u>9,030</u>	<u>396,136</u>	<u>4,322,779</u>
	<u>\$ 42,370,085</u>	<u>\$ 143,396,790</u>	<u>\$ 8,933,767</u>	<u>\$ 20,007,370</u>	<u>\$ 214,708,012</u>	<u>\$ 1,985,544</u>	<u>\$ 10,577,468</u>	<u>\$ 227,271,024</u>

See accompanying notes to consolidated financial statements.

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the years ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities		
Change in net assets	\$ 4,431	\$ 924,175
Adjustments to reconcile changes in net assets to net cash provided by operating activities:		
Depreciation	4,336,462	4,322,779
Recognize deferred gain with sale-leaseback	(381,490)	(344,002)
Loss on sale of property, plant and equipment	(97,990)	1,490
Net realized and unrealized loss (gain) on investments	1,055,945	(2,118,863)
Contributions for capital expenditures	(381)	(19,544)
Changes in assets and liabilities:		
Accounts receivable, net	(1,033,943)	(371,972)
Inventory	(1,101,017)	(1,838,267)
Prepaid expenses and deposits	428,664	1,152,694
Accounts payable and accrued liabilities	358,647	2,339,444
Accrued compensation and related expense	372,907	360,294
Accrued insurance claims	542,601	939,936
Deferred rent	(43,827)	(144,511)
Deferred rent from construction allowance	<u>(307,689)</u>	<u>342,561</u>
Net cash provided by operating activities	4,133,320	5,546,214
Cash flows from investing activities		
Proceeds from sale of property, plant and equipment	97,990	370,110
Purchases of property, plant and equipment	(3,083,675)	(5,371,529)
Proceeds from sale of investments	2,467,929	3,917,640
Purchases of investments	<u>(2,339,238)</u>	<u>(4,321,871)</u>
Net cash used in investing activities	(2,856,994)	(5,405,650)
Cash flows from financing activities		
Contributions restricted for capital expenditures	381	19,544
Borrowing of capitalized lease	-	272,376
Repayment of capitalized lease	(60,127)	(43,096)
Repayment of Term Loan	<u>(321,472)</u>	<u>(375,852)</u>
Net cash used in financing activities	<u>(381,218)</u>	<u>(127,028)</u>
Net increase in cash and cash equivalents	895,108	13,536
Cash and cash equivalents at beginning of year	<u>13,726,968</u>	<u>13,713,432</u>
Cash and cash equivalents at end of year	<u>\$ 14,622,076</u>	<u>\$ 13,726,968</u>
Supplemental cash flow information:		
Cash paid for interest	<u>\$ 353,328</u>	<u>\$ 328,022</u>

See accompanying notes to consolidated financial statements.

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 1 – ORGANIZATION

General: Goodwill Industries of Southern California (“Goodwill” or the “Organization”) was incorporated in 1919. Goodwill is a tax-exempt 501(c)(3) public charity, incorporated under the laws of the State of California as a non-profit public benefit corporation. The mission of Goodwill is to transform lives through the power of work. Goodwill serves people with disabilities or other vocational challenges, as well as businesses, by providing education, training, work experience and job placement services. Goodwill operates a network of retail stores and attended donation centers and provides contractual services such as assembly and fulfillment, secure document management, e-recycling, printing, custodial and building services, and workforce development programs in Los Angeles, San Bernardino, and Riverside counties.

Formation of Goodwill Retail Services: In March 2011, Goodwill’s Board of Directors authorized the creation of Goodwill Retail Services (“GRS”) as a supporting organization under Section 509(a)(3) of the Internal Revenue Code. GRS’s purpose is to support, benefit and carry out the purposes of Goodwill. Its specific purpose is to provide staffing services in the retail stores operated by Goodwill. GRS was incorporated on April 4, 2011, and received its tax-exempt status determination letter as a 501(c)(3) supporting organization from the Internal Revenue Service on April 20, 2012. As the supported organization, Goodwill controls GRS, and the financial statements of the two entities are consolidated.

Program Services:

Material Handling – These services include the collection, transportation, sorting, and processing of contributed goods, most of which are made available for sale through Goodwill’s network of stores, clearance centers and e-commerce operations. Material handling creates employment for persons with disabilities and other barriers to employment.

Stores – Goodwill operates 82 stores where contributed goods and a limited selection of new goods are available to the public. Persons with disabilities or other vocational challenges work alongside traditional employees to provide the consumer with a positive shopping experience. The proceeds from store sales are used to support unfunded or partially funded program services in addition to capital and administrative expenses for the Organization.

Contract Services – Persons with disabilities and other vocational challenges work in closely supervised teams to provide electronics recycling, shredding, document imaging, printing, custodial services, and assembly and fulfillment services to the local business community.

Workforce Development – There are over 50 program activities to provide education, training, placement and other vocational support for target populations including persons with disabilities, at-risk youth, the working poor, ex-offenders, veterans, and the homeless. These programs are funded through reimbursement, fee for service arrangements, and private support. Workforce development also includes the operation of a cafeteria for vocational training and several career centers that provide job listings, resume assistance, telephone and computer services for all job seekers.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting and Reporting: The accompanying consolidated financial statements of the Organization have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (“GAAP”). All significant intercompany transactions have been eliminated.

The Organization reports its consolidated financial position and activities into two net asset categories according to the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Organization and changes therein, are classified and reported as follows (see Note 9):

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

- *Net assets without donor restrictions* – Net assets that are not subject to donor-imposed stipulations. Net assets without donor restrictions may be designated by the Board either for specific purposes or for investment.
- *Net assets with donor restrictions* – Net assets subject to donor-imposed stipulations that may, or will be, met by either actions of the Organization, and/or, the passage of time.

Revenue Recognition: Goodwill recognizes revenue from sales from stores and commodities sales at the time goods are sold. Contract sales are recognized when services have been provided. Workforce development fees are earned based on agreed rates for services provided or, in the case of government grants, reimbursed based on allowable costs expended for program services.

Contributions, including unconditional promises to give, are recognized when received. Donated goods revenue and donated goods inventory are recorded at fair value based on the estimated value of the inventory at selling price. The fair value is derived from sales value less the cost to bring the product to market.

Cash and Cash Equivalents: Cash and cash equivalents include short-term, highly liquid investments and certificates of deposit with an original maturity of three months or less at the time of purchase. Cash and cash equivalents representing assets held as endowment and as charitable gift annuities are included within investments. Cash equivalents are reported at cost, which approximates fair value.

Concentrations of Credit Risk: The Organization has cash balances that exceed the Federal Deposit Insurance Corporation (“FDIC”) insurance coverage. The Organization has not experienced and does not anticipate any losses related to cash held in these accounts.

Investments: The Organization’s investment policy is to adhere to high standards of quality in the selection of all types of investments, with reasonable diversification to be maintained at all times. Marketable securities are held by one independent custodian. The Organization has not experienced and does not anticipate any adverse impact to the investments as a result of this concentration. The fair value of investments in securities traded on national securities exchanges are valued at the closing price on the last business day of the fiscal year; securities traded on the over-the-counter market are valued at the last reported bid price.

Securities transactions are recorded on a trade-date basis. Dividend income is recorded as of the ex-dividend date, and interest income is recorded as earned using the accrual basis. Net realized and unrealized gains and losses on investments include realized and unrealized gains and losses on investments held or sold during the year. Investment income is recognized as a component of net assets without donor restrictions, unless its use is temporarily or permanently restricted by donors for a specified purpose or future period.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accounts Receivable: Accounts receivable are comprised of grants and contracts receivable from the federal, state and local government and customer obligations due under normal trade terms requiring payment within 30 – 90 days from the invoice date. Management analyzes the collectability of these receivables and establishes an allowance for doubtful accounts that reflects its best estimate of the amounts that will not be collected. The allowance for doubtful accounts is determined by a monthly and annual review of account balances, including the age of the balance and historical collection experience. Uncollectible receivables are charged to the allowance. An expense is recorded at the time the allowance is adjusted. Management has determined substantially all government receivables are fully collectible, but has provided an allowance for approximately \$275,000 and \$229,000 for customer obligations at December 31, 2018 and 2017, respectively.

Contributions Receivable: The Organization records contributions receivable, net of allowances for estimated uncollectible amounts, when there is sufficient evidence in the form of verifiable documentation that an unconditional promise to give was received. No allowance was recorded for estimated uncollectible contributions receivable at December 31, 2018 or 2017. Multi-year contributions are recorded at fair value at the date of the contribution. Conditional promises to give are recognized only when the conditions on which they depend are substantially met. Contributions receivable is reported within other receivables on the consolidated statements of financial position (see Note 6).

Inventory: Inventory is comprised of donated goods inventory and new product inventory. Donated goods inventory is recorded at fair value as noted in the revenue accounting policy above. New product inventory is valued at the lower of cost or net realizable value, using the weighed-average cost method.

Property, Plant and Equipment: Property, plant and equipment used in the operations of the Organization are stated at cost or, if donated, at the fair value at the date of contribution. Property, plant and equipment with a cost of at least \$5,000 and a useful life of three years or more is capitalized. Depreciation and amortization on both purchased and donated items are recorded using the straight-line method over the shorter of the estimated useful life of the related asset or the term of the lease for leasehold improvements as follows:

Buildings and improvements	5 – 30 years
Fixtures and equipment	5 – 30 years
Transportation equipment	3 – 7 years

Normal repairs and maintenance are expensed as incurred, whereas significant charges that increase the fixed asset values or extend useful lives are capitalized and depreciated over the estimated useful lives of the related assets.

Expenditures for fixed assets that are purchased with government funds are expensed when acquired because the grantor retains title to such assets.

Gains and losses are recognized in the consolidated statements of activities upon disposal of property and equipment. During the year ended December 31, 2012, the Organization entered into sale-leaseback transactions on three properties, for which specific analysis has been performed and gains deferred (see Note 7).

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accounting for the Impairment of Long-Lived Assets and for the Disposal of Long-Lived Assets: The Organization reviews property and equipment for impairment whenever events or changes in circumstances indicate that the carrying value of the property and equipment may not be recoverable. Recoverability is measured by a comparison of the carrying amount of the asset to future net cash flows, undiscounted and without interest, expected to be generated by the asset. If assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds the fair value of the asset. During the years ended December 31, 2018 and 2017, there were no events or changes in circumstances indicating that the carrying amount of the property, plant and equipment may not be recoverable.

Split-Interest Agreements: The Organization is a beneficiary of irrevocable split-interest agreements, including charitable remainder trusts, perpetual trusts and gift annuities.

The charitable remainder trust agreements generally require the Organization to make annual payments to the trust beneficiaries based on stipulated payment rates, applied to the fair value of the trust assets as determined annually. The Organization uses an interest rate commensurate with the risks involved to discount the future payments and calculate the present value of the liability. A receivable, net of the present value of the liability, is recorded in other receivables (Note 6) at the estimated fair value of the asset. A receivable is recorded in other receivables for the perpetual trusts at the estimated fair value of the amount held by the trustee that is due to the Organization.

The Organization invests funds contributed by individuals in exchange for a lifetime annuity paid by the Organization. These investments are reported at fair value and reported with investments (Note 5). The liability associated with these annuities is reported with accounts payable and accrued liabilities on the consolidated statements of financial position.

Donor-Restricted Contributions: Unconditional promises to give (contributions receivable) are recognized as contributions when received at their estimated fair value. Contributions are considered available for unrestricted use unless specifically restricted by the donor. Amounts received that are restricted for future period or by the donor for specific purposes are reported as donor-restricted support that increases those net asset classes.

When a donor-imposed time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the accompanying consolidated statements of activities as net assets released from restrictions. Capital campaign contributions are considered to be net assets with donor restrictions until the asset is placed into service.

Government and Other Grants: The Organization receives numerous grants from governmental agencies and certain foundations. The Organization recognizes income from these grants as revenue and support only to the extent that expenditures have been made for the purposes specified by the grant agreement.

Advertising Expenses: Advertising costs are expensed as incurred. During 2018 and 2017, advertising costs were approximately \$247,000 and \$376,000, respectively, and are reported with printing, publication and media on the consolidated statements of functional expenses.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Functional Expenses: The Organization allocates its expenses on a functional basis among its various programs and support services. Expenses that are identified with a specific program or support service are charged directly according to their natural expenditure classification. Expenses that are common to specific programs or support services are allocated to those services based on estimated level of effort or level of use. Certain shared costs are allocated. Services related to information technology are allocated based on the number of computers for each program or support service. Occupancy and related costs for the Los Angeles, San Fernando Valley, San Bernardino and Ontario campuses are allocated based on the number of square feet used by program and support service departments.

Use of Estimates: The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and related disclosures at the date of the financial statements and the reported amounts of revenues, expenses and changes in net assets during the reporting period. While management believes that these estimates are adequate as of December 31, 2018 and 2017, it is possible that actual results could differ from those estimates, and the difference could be material to the consolidated financial statements.

Income Tax Status: The Organization was organized pursuant to the General Nonprofit Corporation Law of the State of California. The Organization has been recognized by the Internal Revenue Service as an organization that is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. The Organization has also been recognized by the California Franchise Tax Board as an organization that is exempt from California franchise and income taxes under Section 23701d of the California Revenue and Taxation Code and has qualified for the welfare exemption from certain general county real and personal property taxes. However, the Organization is subject to income taxes on any net income that is derived from a trade or business, regularly carried on, and not in furtherance of the purposes for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the consolidated financial statements taken as a whole.

Tax positions taken related to the Organization's tax exempt status, unrelated business activities taxable income and deductibility of expenses and other miscellaneous tax positions have been reviewed, and management is of the opinion that material positions taken by the Organization would more likely than not be sustained by examination. Accordingly, the Organization has not recorded an income tax liability for uncertain tax benefits as of December 31, 2018 and 2017, nor does it expect there will be a material change in the twelve months following the year ended December 31, 2018.

Contributed Services: A substantial number of volunteers have donated significant amounts of time and services to the Organization's program operations and to its fundraising campaigns. Contributed services are recognized by the Organization if the services received (a) create or enhance long-lived assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. The services donated are not reflected in the accompanying consolidated financial statements as an expense or as income from donations; such services do not meet the above criteria for recording under GAAP.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Adoption of New Accounting Standard: In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities*, which revises the not-for profit financial reporting model. ASU 2016-14 provides for additional disclosure requirements and modifies net asset reporting. The standard requires the Organization to reclassify its net assets (i.e., unrestricted, temporarily restricted, and permanently restricted) into two categories: net assets without donor-imposed restrictions and net assets with donor-imposed restrictions, among other requirements. The Organization adopted ASU 2016-14 for its fiscal year ending December 31, 2018 and has adjusted the presentation of these financial statements accordingly. The ASU has been applied retrospectively to all periods presented, except for the liquidity disclosure, as permitted. The implementation of this ASU did not have a material effect on amounts previously presented.

Recent Accounting Guidance: In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-02, *Leases (Topic 842)*, to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the statement of financial position and disclosing key information about leasing arrangements for lessees and lessors. The new standard applies a right-of-use model that requires, for all leases with a lease term of more than 12 months, an asset representing its right to use the underlying asset for the lease term and a corresponding liability. The ASU is effective for fiscal years beginning after December 15, 2019. The Organization has not yet implemented this ASU and is in the process of assessing the effect on the financial statements.

Reclassifications: Certain amounts in the prior year financial statements have been reclassified to conform to the current year presentation. Such reclassifications did not have an effect on net assets or change in net assets.

NOTE 3 – LIQUIDITY AND AVAILABILITY

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the balance sheet date, comprise the following:

Cash and cash equivalents	\$ 14,622,076
Accounts receivable	4,363,474
Endowment spending-rate distributions and appropriations	393,266
Investments	<u>16,553,054</u>
Total	<u>\$ 35,931,870</u>

The Organization's endowment funds consist of donor-restricted endowments and funds designated by the board as endowments. Income from donor-restricted endowments is restricted for specific purposes, with the exception of the amounts available for general use, which on an annual basis is calculated as 7% of the average balance of the prior twelve quarters. Otherwise, donor-restricted endowment funds are not available for general expenditure.

The Organization's investments of \$16,553,054 are accessible upon board approval, and are not subject to an annual spending maximum. Although the Organization does not intend to spend from these board-designated amounts, these amounts could be made available by the board if necessary. In addition, the Organization has available a revolving line of credit totaling \$5,000,000, as further described in Note 8.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 4 – FAIR VALUE

For those assets and liabilities reported at fair value, the Organization has determined their placement in the fair value hierarchy based on the nature of inputs to determine the fair value and management's assessment of risk characteristics associated with these inputs. The Organization categorizes the financial assets and liabilities, based on the priority of inputs to the valuation technique, into three-tiered hierarchy as described below.

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities as of the reporting date. Level 1 investments include listed equities, listed fixed income securities, and certain mutual funds.

Level 2 – Observable inputs, other than Level 1 quoted prices, such as quoted prices for similar assets and liabilities, quoted prices in markets that are not active, or other inputs that are observable for the asset or liability either directly or indirectly. Investments in this category include corporate and government bonds, and certain money market funds. A significant adjustment to a Level 2 input could result in the Level 2 measurement becoming a Level 3 measurement.

Level 3 – Unobservable inputs that are supportable by little or no market activity, which requires the Organization to develop its own assumptions. Investments that are included in this category include hedge funds and certain mutual funds. Contributions receivable from split-interest agreements are also included in this category.

The following methods and assumptions are used to estimate fair value:

Mutual funds - Mutual funds held by the Organization are publicly traded and are valued at the closing price on the last business day of the fiscal year.

Beneficial interests in trusts - Beneficial interests in trusts (Note 6) include charitable remainder trusts and perpetual trusts administered by other trustees, which are valued based on estimates associated with life expectancy, investment return, future inflation, and cash flows associated with real estate and untraded securities.

The following tables summarize the valuation of the Organization's investments and contributions receivable under split-interest agreements by fair value hierarchy levels as of December 31, 2018 and 2017. Investments include CDs in the amount of \$1,517,186 and \$1,931,050, as of December 31, 2018 and 2017, respectively, which is not included in the fair value hierarchy table below.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 4 – FAIR VALUE (Continued)

2018	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Investments				
Money market funds	\$ -	\$ 1,023,224	\$ -	\$ 1,023,224
Mutual funds - equity				
Emerging Markets - Index	539,726	-	-	539,726
Small Cap - Index	210,053	-	-	210,053
Stock - Index	6,399,972	-	-	6,399,972
Global Stock - Index	1,280,818	-	-	1,280,818
Growth	1,244,108	-	-	1,244,108
Mutual funds - fixed income				
Global Bonds Index	1,385,918	-	-	1,385,918
Intermediate Bonds	4,550,352	-	-	4,550,352
Intermediate Bonds - Index	518,390	-	-	518,390
Bond Index	<u>1,220,304</u>	<u>-</u>	<u>-</u>	<u>1,220,304</u>
Total investments	17,349,641	1,023,224	-	18,372,865
Beneficial interests in trusts				
Perpetual trusts	-	-	271,688	271,688
Charitable remainder trusts	<u>-</u>	<u>-</u>	<u>683,964</u>	<u>683,964</u>
Total beneficial interests in trusts	<u>-</u>	<u>-</u>	<u>955,652</u>	<u>955,652</u>
Assets reported at fair value	<u>\$ 17,349,641</u>	<u>\$ 1,023,224</u>	<u>\$ 955,652</u>	<u>\$ 19,328,517</u>

2017	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Investments				
Money market funds	\$ -	\$ 416,009	\$ -	\$ 416,009
Mutual funds - equity				
Emerging Markets - Index	631,823	-	-	631,823
Small Cap - Index	257,123	-	-	257,123
Stock - Index	6,830,643	-	-	6,830,643
Global Stock - Index	1,523,453	-	-	1,523,453
Growth	1,274,528	-	-	1,274,528
Mutual funds - fixed income				
Global Bonds Index	1,401,228	-	-	1,401,228
Intermediate Bonds	4,769,964	-	-	4,769,964
Intermediate Bonds - Index	700,788	-	-	700,788
Bond Index	<u>1,354,579</u>	<u>-</u>	<u>-</u>	<u>1,354,579</u>
Total investments	18,744,129	416,009	-	19,160,138
Beneficial interests in trusts				
Perpetual trusts	-	-	312,477	312,477
Charitable remainder trusts	<u>-</u>	<u>-</u>	<u>626,674</u>	<u>626,674</u>
Total beneficial interests in trusts	<u>-</u>	<u>-</u>	<u>939,151</u>	<u>939,151</u>
Assets reported at fair value	<u>\$ 18,744,129</u>	<u>\$ 416,009</u>	<u>\$ 939,151</u>	<u>\$ 20,099,289</u>

The Organization's policy is to recognize transfers in and out of Levels 1, 2, and 3 as of the end of the year. There were no transfers between levels during 2018 or 2017. The changes in value of Level 3 assets are reported within realized and unrealized gains and losses in the consolidated statements of activities.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 4 – FAIR VALUE (Continued)

The following table summarizes the Organization's Level 3 reconciliation as of December 31, 2018 and 2017:

	<u>Charitable</u>	<u>Perpetual</u>	<u>Total</u>
Balance January 1, 2017	\$ 555,831	\$ 293,692	\$ 849,523
Increase in fair value	<u>70,843</u>	<u>18,785</u>	<u>89,628</u>
Balance December 31, 2017	626,674	312,477	939,151
Increase (decrease) in fair value	<u>57,290</u>	<u>(40,789)</u>	<u>16,501</u>
Balance December 31, 2018	<u>\$ 683,964</u>	<u>\$ 271,688</u>	<u>\$ 955,652</u>

For the beneficial interest in the charitable remainder trusts and perpetual trusts, upon the death of the donors or other termination of the trusts as may be defined in the individual agreements, the remaining trust assets will be distributed by the Organization to itself and to other beneficiaries, as stipulated in the trust agreements.

NOTE 5 – INVESTMENTS

Investments consist of the following as of December 31:

	<u>2018</u>	<u>2017</u>
Cash and cash equivalents	\$ 1,023,224	\$ 416,009
Certificates of deposit	1,517,186	1,931,050
Mutual funds - bond funds	7,674,964	8,226,559
Mutual funds - stock funds	<u>9,674,677</u>	<u>10,517,570</u>
	<u>\$ 19,890,051</u>	<u>\$ 21,091,188</u>

The uses of the investments as of December 31, are as follows:

	<u>2018</u>	<u>2017</u>
Charitable gift annuities	\$ 518,390	\$ 716,106
Board designated reserve	1,207,627	507,302
Other investments	15,345,427	16,548,698
Endowment	<u>2,818,607</u>	<u>3,319,082</u>
	<u>\$ 19,890,051</u>	<u>\$ 21,091,188</u>

The investments include the assets of the charitable gift annuities account, whose funds are contributed by individuals in exchange for a lifetime annuity paid by Goodwill. Investments in this account are regulated under the California Insurance Code and by the Department of Insurance. The liability associated with these annuities of approximately \$10,000 and \$16,000 as of December 31, 2018 and 2017, respectively, is reported within accounts payable and accrued liabilities in the consolidated statements of financial position. The board designated reserve is invested as "quasi-endowment" in a specially segregated account. These funds are eligible for use for purposes that are authorized by the Board.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 5 – INVESTMENTS (Continued)

Activity in the investments during the years ended December 31, was as follows:

	<u>2018</u>	<u>2017</u>
Balance, beginning of year	\$ 21,091,188	\$ 18,657,722
Increases:		
Dividends and interest reinvested	474,029	439,061
Purchase of investments	<u>1,865,209</u>	<u>3,882,810</u>
	2,339,238	4,321,871
Decreases:		
Sales, redemptions and distributions	(2,467,929)	(3,917,640)
Realized gains	62,390	331,543
Unrealized (losses) gains	<u>(1,134,836)</u>	<u>1,697,692</u>
Realized and unrealized (losses) gains, net	<u>(1,072,446)</u>	<u>2,029,235</u>
Balance, end of year	<u>\$ 19,890,051</u>	<u>\$ 21,091,188</u>

Information about net realized and unrealized gains (losses) during the years ended December 31, is as follows:

	<u>2018</u>	<u>2017</u>
From investments	\$ (1,072,446)	\$ 2,029,235
From remainder trust	57,290	70,843
From perpetual trust	<u>(40,789)</u>	<u>18,785</u>
	<u>\$ (1,055,945)</u>	<u>\$ 2,118,863</u>

NOTE 6 – OTHER RECEIVABLES

Other receivables include the following as of December 31:

	<u>2018</u>	<u>2017</u>
Pledges receivable	\$ 1,430,947	\$ 556,031
Remainder trusts	683,964	626,674
Perpetual trusts beneficial interest	<u>271,689</u>	<u>312,477</u>
Total other receivables	<u>\$ 2,386,600</u>	<u>\$ 1,495,182</u>

Charitable remainder trusts and beneficial interest of perpetual trusts are presented at fair value based on significant unobservable inputs and accordingly are categorized as Level 3, whose activities are disclosed in Note 5. The beneficial interest in charitable remainder and perpetual trusts is distributed by the Organization as stipulated in the trust agreements.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 6 – OTHER RECEIVABLES (Continued)

Activity of contributions receivable during the years ended December 31, was as follows:

	<u>2018</u>	<u>2017</u>
Beginning balance:	\$ 556,031	\$ 499,806
New contributions promised	4,531,166	785,996
Pledge payments received	<u>(3,656,250)</u>	<u>(729,771)</u>
Ending balance:	<u>\$ 1,430,947</u>	<u>\$ 556,031</u>

Repayment schedule of contributions receivable are as follows as of December 31, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Less than one year	\$ 1,230,947	\$ 356,031
Between one year and three years	<u>200,000</u>	<u>200,000</u>
Pledges receivable, net	<u>\$ 1,430,947</u>	<u>\$ 556,031</u>

NOTE 7 – PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following as of December 31:

	<u>2018</u>	<u>2017</u>
Land	\$ 2,034,821	\$ 2,034,821
Buildings and improvements	43,263,835	43,191,136
Fixtures and equipment	27,922,736	25,361,779
Transportation equipment	3,406,558	3,338,806
Construction in progress	<u>254,655</u>	<u>12,500</u>
	76,882,605	73,939,042
Less accumulated depreciation	<u>(47,925,422)</u>	<u>(43,729,072)</u>
	<u>\$ 28,957,183</u>	<u>\$ 30,209,970</u>

Depreciation expense for the years ended December 31, 2018 and 2017, was approximately \$4,336,000 and \$4,323,000, respectively.

Construction Allowance: The Organization has several lease arrangements that provide for the payment of a construction allowance. The costs of improvement are included with property, plant and equipment. Typically, the construction allowance is repaid when the building is opened for occupancy. The value of the allowance is amortized over the life of the lease.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 7 – PROPERTY, PLANT AND EQUIPMENT (Continued)

The unamortized value of the construction allowance is reported in the consolidated statements of financial position as deferred rent – construction allowance as of December 31:

	<u>2018</u>	<u>2017</u>
Construction allowance	\$ 5,071,660	\$ 4,845,625
Deferred rent recognized	<u>(2,373,933)</u>	<u>(1,840,209)</u>
	<u>\$ 2,697,727</u>	<u>\$ 3,005,416</u>

Sale-leaseback Transaction: During 2012, the Organization sold its real estate investments in three of its properties for approximately \$6,996,000. After the sale, the Organization leased back the three buildings under 15 year lease agreements. In accordance with GAAP, the Organization accounted for the transaction as a sale-leaseback and deferred a portion of the gain on the sale equal to the net present value of the Organization’s future minimum lease payments of approximately \$5,700,000. The deferred gain is being amortized on a straight line basis over the 15 year life of the lease. This amount is reported as a reduction of rent expense in each year.

The unamortized gain is reported in the consolidated statements of financial position as deferred gain on sale-leaseback as of December 31:

	<u>2018</u>	<u>2017</u>
Unrecognized gain	\$ 5,699,806	\$ 5,699,806
Sale-leaseback deferred rent recognized	<u>(2,244,832)</u>	<u>(1,863,342)</u>
	<u>\$ 3,454,974</u>	<u>\$ 3,836,464</u>

The future amortization of the deferred gain based on minimum rents for years ending December 31 is as follows:

2019	\$ 378,839
2020	378,839
2021	378,839
2022	378,839
2023	378,839
Thereafter	<u>1,560,779</u>
	<u>\$ 3,454,974</u>

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 8 – NOTE PAYABLE

The Organization maintains borrowing facilities with a commercial bank. The arrangement provides for a term loan for \$10,000,000 and, access to a revolving line-of-credit for \$5,000,000. The term loan requires payment of principal and interest monthly through October 31, 2022, when the remaining principal balance plus any interest is due. The revolving line-of-credit was scheduled to expire February 28, 2019. Subsequent to year-end, the Organization entered into an amendment with the bank to extend the expiration date of the line-of-credit to September 1, 2020. Both the term loan and the revolving line-of-credit are collateralized by real property. The interest rate on the term loan was fixed at 3.66% at December 31, 2018 and 2017. The interest rate on the revolving line-of-credit is the LIBOR daily floating rate plus 1.5% (3.88% and 2.94% at December 31, 2018 and 2017, respectively). At December 31, 2018 and 2017, \$8,805,148 and \$9,126,620, respectively, was outstanding on the term loan. At December 31, 2018 and 2017, the revolving line-of-credit was unused. The terms of the credit facilities and master lease require the Organization to meet or exceed certain ratios and to communicate financial results to the bank on a regular basis. Management believes they were in compliance with such covenants as of December 31, 2018 and 2017.

Principal payments to be made through to the maturity date as of December 31, 2018, are as follows:

2019		\$ 356,508
2020		371,452
2021		384,162
2022		<u>7,693,026</u>
		<u>\$ 8,805,148</u>

In 2016 the Organization negotiated a master lease with a commercial bank not to exceed \$500,000. The master lease provides for the Organization to enter into distinct and separate leases for the purchase of capitalized equipment. The lease requires payment of principal and interest monthly through September 30, 2023. The interest rate on the lease is 4.68%.

2019		\$ 85,769
2020		85,769
2021		85,769
2022		85,769
2023		70,870
Thereafter		<u>21,164</u>
Total payments		435,110
Less amount representing interest		<u>(48,742)</u>
Net present value of minimum payments		<u>\$ 386,368</u>

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 9 – NET ASSETS

Net assets without donor restrictions: At December 31, unrestricted and board-designated net assets are as follows:

	<u>2018</u>	<u>2017</u>
Net assets without donor restrictions		
Board designated reserve	\$ 1,207,627	\$ 507,302
Invested in property, plant and equipment	<u>19,765,667</u>	<u>20,636,855</u>
Board designated	<u>20,973,294</u>	<u>21,144,157</u>
Net assets without donor restrictions	<u>\$ 20,973,294</u>	<u>\$ 21,144,157</u>

Net assets with donor restrictions: Activity in net assets with donor restrictions during the years ended December 31, 2018 and 2017 was as follows:

	<u>Balance January 1, 2018</u>	<u>Contributions and other Increases</u>	<u>Release from restrictions and other decreases</u>	<u>Balance December 31, 2018</u>
Capital campaign	\$ -	\$ 381	\$ (381)	\$ -
Program services	3,200,501	3,494,790	(2,835,522)	3,859,769
Charitable remainder trusts	626,674	57,290	-	683,964
Unexpended endowment	1,162,972	-	(500,475)	662,497
Perpetual trusts	312,477	-	(40,789)	271,688
Named endowments	<u>2,156,110</u>	<u>-</u>	<u>-</u>	<u>2,156,110</u>
Net assets with donor restrictions	<u>\$ 7,458,734</u>	<u>\$ 3,552,461</u>	<u>\$ (3,377,167)</u>	<u>\$ 7,634,028</u>

	<u>Balance January 1, 2017</u>	<u>Contributions and other Increases</u>	<u>Release from Restrictions</u>	<u>Balance December 31, 2017</u>
Capital campaign	\$ -	\$ 19,544	\$ (19,544)	\$ -
Program services	2,032,500	3,084,960	(1,916,959)	3,200,501
Charitable remainder trusts	555,831	70,843	-	626,674
Unexpended endowment	787,070	375,902	-	1,162,972
Perpetual trusts	293,692	18,785	-	312,477
Named endowments	<u>2,156,110</u>	<u>-</u>	<u>-</u>	<u>2,156,110</u>
Net assets with donor restrictions	<u>\$ 5,825,203</u>	<u>\$ 3,570,034</u>	<u>\$ (1,936,503)</u>	<u>\$ 7,458,734</u>

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 December 31, 2018 and 2017

NOTE 9 – NET ASSETS (Continued)

	<u>2018</u>	<u>2017</u>
Purpose and time restrictions	\$ 3,659,769	\$ 3,000,501
Time restrictions	883,964	826,674
Unexpended endowment	662,497	1,162,972
Perpetual Trusts	271,688	312,477
Named endowments	<u>2,156,110</u>	<u>2,156,110</u>
Net assets with donor restrictions	<u>\$ 7,634,028</u>	<u>\$ 7,458,734</u>

Net assets were released from donor restrictions during the year ended December 31, as follows:

	<u>2018</u>	<u>2017</u>
Passage of time available to support operations and programs	\$ 3,335,997	\$ 1,916,959
Completion of construction or acquisition of property and equipment	<u>381</u>	<u>19,544</u>
	<u>\$ 3,336,378</u>	<u>\$ 1,936,503</u>

NOTE 10 – COMMITMENTS AND CONTINGENCIES

Leases: The Organization leases certain stores, facilities and office and transportation equipment. The leases have various expiration dates through 2027. Minimum annual rental payments, excluding any future inflation adjustments, are as follows:

2019	\$ 26,014,951
2020	22,250,026
2021	18,899,566
2022	15,159,454
2023	11,361,345
Thereafter	<u>21,181,387</u>
	<u>\$ 114,866,729</u>

Rental expense for the years ended December 31, 2018 and 2017, was approximately \$27,976,000 and \$25,889,000, respectively.

Sublease Rental Income: The Organization has agreements with non-profit organizations to provide subleased space in a facility in Los Angeles. Minimum annual rental payments excluding any future inflation adjustments are as follows:

2019	\$ 179,956
2020	55,361
2021	<u>21,670</u>
	<u>\$ 256,987</u>

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 10 – COMMITMENTS AND CONTINGENCIES (Continued)

Rental revenue from sublease rents during the year ended December 31, 2018 and 2017, was both approximately \$161,000.

Litigation: In the normal course of operations, the Organization is named as defendant in lawsuits and is subject to periodic examinations by regulatory agencies. After consultation with legal counsel, management is of the opinion that any liabilities arising from such litigation and examinations have been properly reported in the consolidated statements of financial position within accounts payable and accrued liabilities.

Environmental Matter: An adjoining property owner has alleged that contamination at one of their properties was caused by operations taking place at one of the Organization's sites. The ultimate outcome of this uncertainty cannot presently be determined, and management believes that any liability, if determined, will not have a material adverse impact in the Organization's consolidated financial condition.

Government Grants: Certain programs of the Organization receive funding and support from the local, state or federal governments. Accordingly, these programs are subject to audit that could result in adjustments. Management believes that liabilities, if any, resulting from any such audits will not have a material effect on the consolidated financial statements.

NOTE 11 – RETIREMENT PLAN

The Organization has a 403(b) Retirement Plan ("Plan") for the benefit of its employees. All employees are eligible to make contributions from their pre-tax and/or post-tax salary. At the discretion of management, and after one year of service, certain full-time employees may receive an employer contribution of up to 5% of eligible compensation. The employer contribution was discontinued November 1, 2014. Participants are fully vested in their own contributions. Employees are vested in the employer contributions as follows:

<u>Years of service</u>	<u>% Vested</u>
2	25%
3	50%
4	75%
5 or more	100%

For the years ended December 31, 2018 and 2017, the Organization did not contribute to the plan.

In addition, the Organization has a Supplemental Executive Retirement Plan ("SERP") for certain executives. The Organization did not contribute to the SERP for the year ended December 31, 2018. For the year ended December 31, 2017 the Organization contributed approximately \$20,000 to the SERP.

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 December 31, 2018 and 2017

NOTE 12 – SELF-INSURANCE

The Organization has elected not to pay state unemployment insurance (“SUI”) taxes and, instead, is charged for its share of unemployment benefits actually paid by the State of California to former employees.

The Organization is self-insured under its workers’ compensation insurance program. Excess policies provide insurance coverage on individual claims which exceed specified amounts. Each year, the Organization estimates its liability for any claims outstanding, including claims incurred but not reported. The ultimate liability for claims is estimated based on historical data related to the timing and nature of claims paid and current payroll data. The workers’ compensation accrual has been discounted with a rate of 3%. The undiscounted amount of the liability was \$16,379,000 and \$15,836,000, respectively, as of December 31, 2018 and 2017.

Accrued insurance claims reported in the consolidated statements of financial position include estimated obligations for state unemployment insurance and workers’ compensation.

The estimated claims payable and changes in the claims payable amount for fiscal years 2018 and 2017 are listed below:

	<u>Workers’ Compensation</u>	<u>CA SUI</u>	<u>Insurance Claims</u>
<u>2018</u>			
Claims payable at beginning of year	\$ 14,778,030	\$ 1,057,965	\$ 15,835,995
Claims incurred/changes in estimate	7,264,496	694,538	7,959,034
Claim payments	<u>(6,643,465)</u>	<u>(772,968)</u>	<u>(7,416,433)</u>
	<u>\$ 15,399,061</u>	<u>\$ 979,535</u>	<u>\$ 16,378,596</u>
	<u>Workers’ Compensation</u>	<u>CA SUI</u>	<u>Insurance Claims</u>
<u>2017</u>			
Claims payable at beginning of year	\$ 13,662,385	\$ 1,233,674	\$ 14,896,059
Claims incurred/changes in estimate	7,641,094	362,336	8,003,430
Claim payments	<u>(6,525,449)</u>	<u>(538,045)</u>	<u>(7,063,494)</u>
	<u>\$ 14,778,030</u>	<u>\$ 1,057,965</u>	<u>\$ 15,835,995</u>

(Continued)

NOTE 13 – ENDOWMENTS

The Organization's endowment consists of individual funds established for a variety of purposes. The net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Organization has interpreted the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Organization classifies as net assets with donor restrictions (a) the original value of gifts donated to the restricted endowment, (b) the original value of subsequent gifts to the restricted endowment, (c) the fair value of the Organization's interest in split-interest agreements at the time of termination of the trust as stipulated by the trust agreement to be restricted endowment and (d) accumulations to the restricted endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

Additionally, the Organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- (1) The duration and preservation of the fund
- (2) The mission of the Organization and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The expected total return from income and the appreciation of investments
- (6) Other resources of the Organization
- (7) The Organization's investment policies

Investment Return Objectives, Risk Parameters and Strategies: The Organization has adopted investment and spending policies, approved by the Board of Directors, for endowment assets that attempt to provide a predictable stream of funding while also maintaining the purchasing power of those endowment assets over the long-term. Accordingly, the investment process seeks to achieve investment income with minimum risk. Endowment assets are invested in mutual funds.

Spending Policy: Although UPMIFA permits a more aggressive spending policy, funds will only be transferred out of the endowment fund when approved specifically by the finance committee provided that this is consistent with the wishes of the donors. Income from donor-restricted endowments is restricted for specific purposes, with the exception of the amounts available for general use, which on an annual basis is calculated as 7% of the average balance of the prior twelve quarters.

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 13 – ENDOWMENTS (Continued)

Endowment Net Asset Composition by Type of Fund: For the year ended December 31, 2018 endowment net assets have been classified as follows:

	Net Assets Without Donor <u>Restrictions</u>	Net Assets With Donor <u>Restrictions</u>	<u>Total</u>
Board designated reserve	\$ 16,553,054	\$ -	\$ 16,553,054
Perpetual trusts	-	271,688	271,688
Unexpended endowment	-	662,497	662,497
Named endowments	-	2,156,110	2,156,110
Subtotal	<u>16,553,054</u>	<u>3,090,295</u>	<u>19,643,349</u>
Release from designation	<u>(15,345,427)</u>	<u>-</u>	<u>(15,350,427)</u>
	<u>\$ 1,207,627</u>	<u>\$ 3,090,295</u>	<u>\$ 4,297,922</u>

Named investment endowments as of December 31, 2018, are as follows:

Lawrence Page	\$ 46,385
Garret Family	503,121
Ludwig EG Erb	2,137,087
Thomas Barry	110,663
Capital Campaign	<u>21,351</u>
	<u>\$ 2,818,607</u>

For the year ended December 31, 2017 endowment net assets have been classified as follows:

	Net Assets Without Donor <u>Restrictions</u>	Net Assets With Donor <u>Restrictions</u>	<u>Total</u>
Board designated reserve	\$ 17,056,000	\$ -	\$ 17,056,000
Perpetual trusts	-	312,477	312,477
Unexpended endowment	-	1,162,972	1,162,972
Named endowments	-	2,156,110	2,156,110
Subtotal	<u>17,056,000</u>	<u>3,631,559</u>	<u>20,687,559</u>
Release from designation	<u>(16,548,698)</u>	<u>-</u>	<u>(16,548,698)</u>
	<u>\$ 507,302</u>	<u>\$ 3,631,559</u>	<u>\$ 4,138,861</u>

(Continued)

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018 and 2017

NOTE 13 – ENDOWMENTS (Continued)

Named investment endowments as of December 31, 2017, are as follows:

Lawrence Page	\$ 54,928
Garret Family	595,906
Ludwig EG Erb	2,531,214
Thomas Barry	114,871
Capital Campaign	<u>22,163</u>
	<u>\$ 3,319,082</u>

Changes in Endowment Net Assets During the Year:

Activity in the endowment during the year was as follows:

	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	Total Endowment
<u>2018</u>			
Balance December 31, 2017	\$ 507,302	\$ 3,631,559	\$ 4,138,861
Dividends and interest	489,114	-	489,114
Realized and unrealized gain (loss)	(872,405)	(541,264)	(1,413,669)
Distribution and expense	<u>-</u>	<u>-</u>	<u>-</u>
	124,011	3,090,295	3,214,306
Change in restriction	<u>1,083,616</u>	<u>-</u>	<u>1,083,616</u>
Balance December 31, 2018	<u>\$ 1,207,627</u>	<u>\$ 3,090,295</u>	<u>\$ 4,297,922</u>

	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	Total Endowment
<u>2017</u>			
Balance December 31, 2016	\$ 2,039,479	\$ 3,236,872	\$ 5,276,351
Dividends and interest	354,055	-	354,055
Realized and unrealized gains	1,712,358	394,687	2,107,045
Distribution and expense	<u>(50,000)</u>	<u>-</u>	<u>(50,000)</u>
	4,055,892	3,631,559	7,687,451
Change in restriction	<u>(3,548,590)</u>	<u>-</u>	<u>(3,548,590)</u>
Balance December 31, 2017	<u>\$ 507,302</u>	<u>\$ 3,631,559</u>	<u>\$ 4,138,861</u>

NOTE 14 – SUBSEQUENT EVENTS

The Organization evaluated its December 31, 2018 consolidated financial statements for subsequent events through May 9, 2019, the date the consolidated financial statements were available to be issued. The Organization is not aware of any additional subsequent events which would require recording or disclosure in the consolidated financial statements, with the exception of the line of credit extension disclosed in Note 8.

GOODWILL INDUSTRIES OF SOUTHERN CALIFORNIA AND AFFILIATES
SUPPLEMENTAL SCHEDULE – CLASSIFIED CONSOLIDATED STATEMENTS
OF FINANCIAL POSITION
As of December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Current assets		
Cash and cash equivalents	\$ 14,290,386	\$ 13,193,618
Cash and cash equivalents designated for improvements	331,690	533,350
Accounts and other receivables, net	4,363,474	4,522,572
Inventory	8,731,781	7,630,764
Prepaid expenses and deposits	<u>2,249,575</u>	<u>2,716,146</u>
Total current assets	29,966,906	28,596,450
Investments	19,890,051	21,091,188
Other receivables, net of current	2,386,600	1,139,151
Property, plant and equipment, net	<u>28,957,183</u>	<u>30,209,970</u>
Total assets	<u>\$ 81,200,740</u>	<u>\$ 81,036,759</u>
Current liabilities		
Accounts payable and accrued liabilities	\$ 10,719,638	\$ 10,360,991
Accrued compensation and related expenses	6,113,988	5,741,081
Current portion of capitalized lease obligation	68,239	65,121
Current portion of note payable	356,508	345,381
Current portion of deferred gain on sale-leaseback	378,839	378,839
Current portion of deferred rent from construction allowance	307,689	419,750
Current portion of accrued insurance claims	<u>7,416,432</u>	<u>7,063,494</u>
Total current liabilities	25,361,333	24,374,657
Capitalized lease obligation	318,129	381,374
Note payable	8,448,640	8,781,239
Deferred gain on sale-leaseback	3,076,135	3,457,625
Deferred rent	4,036,979	4,080,806
Deferred rent from construction allowance	2,390,038	2,585,666
Insurance claims estimated to be paid after one year	<u>8,962,164</u>	<u>8,772,501</u>
Total liabilities	<u>52,593,418</u>	<u>52,433,868</u>
Net assets		
Net assets without donor restrictions	20,973,294	21,144,157
Net Assets with donor restrictions	<u>7,634,028</u>	<u>7,458,734</u>
Total net assets	<u>28,607,322</u>	<u>28,602,891</u>
Total liabilities and net assets	<u>\$ 81,200,740</u>	<u>\$ 81,036,759</u>