



**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Combined Financial Statements
and
Supplementary Information
December 31, 2015
(With Independent Auditor's Report Thereon)**

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Goodwill Industries of Orange County,
California and Affiliate

We have audited the accompanying combined financial statements of Goodwill Industries of Orange County and Affiliate (the Organization), which comprise the combined statement of financial position as of December 31, 2015, and the related combined statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these combined 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 combined 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 combined financial statements based on our audit. We conducted our audit 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 combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined 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 combined 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 combined financial statements.

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

INDEPENDENT AUDITOR'S REPORT
(Continued)

Opinion

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of the Organization as of December 31, 2015, and the changes in net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Our audits were conducted for the purpose of forming an opinion on the combined financial statements as a whole. The supplemental combining information included in Schedules 1 through 4 is presented for purposes of additional analysis and is not a required part of the combined 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 combined financial statements. The information has been subjected to the auditing procedures applied in the audit of the combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements or to the combined 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 combined financial statements as a whole.

Report on Summarized Comparative Information

We have previously audited the Organization's combined and consolidated financial statements, and we expressed an unmodified audit opinion on those audited combined and consolidated financial statements in our report dated May 27, 2015. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2014 is consistent, in all material respects, with the audited combined and consolidated financial statements from which it has been derived.

: Kushner, Smith, Joanou, and Gregson, LLP

May 25, 2016

Kushner, Smith, Joanou, and Gregson, LLP
100 Spectrum Center Drive, Suite 1000, Irvine, California 92618

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Combined Statement of Financial Position
December 31, 2015**

(with summarized financial information as of December 31, 2014)

<u>ASSETS</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Totals</u>	
				<u>2015</u>	<u>2014</u>
Cash and cash equivalents	\$ 5,312,360	\$ 10,363	\$ --	\$ 5,322,723	\$ 4,614,304
Restricted cash (Note 7)	470,000	--	--	470,000	870,000
Investments (Note 2)	10,964,143	750	52,980	11,017,873	12,551,365
Accounts receivable (net of allowance for doubtful accounts of \$174,316 and \$95,582, respectively) (Note 5)	3,480,011	--	--	3,480,011	3,015,995
Contributions receivable - net (Note 2 and 3)	--	1,206,632	--	1,206,632	1,043,889
Inventory (Note 5)	1,739,759	--	--	1,739,759	1,656,603
Prepaid expenses and deposits	1,062,930	--	--	1,062,930	1,094,446
Bond issuance cost - net (Note 8)	187,558	--	--	187,558	202,096
Land, buildings and equipment - net of accumulated depreciation (Notes 4 and 5)	<u>24,277,345</u>	<u>--</u>	<u>--</u>	<u>24,277,345</u>	<u>25,087,603</u>
Total assets	<u>\$ 47,494,106</u>	<u>\$ 1,217,745</u>	<u>\$ 52,980</u>	<u>\$ 48,764,831</u>	<u>\$ 50,136,301</u>
 <u>LIABILITIES AND NET ASSETS</u>					
Liabilities:					
Accounts payable	\$ 2,243,430	\$ --	\$ --	\$ 2,243,430	\$ 2,449,931
Accrued salaries, wages and vacation payable	3,210,590	--	--	3,210,590	4,324,271
Income taxes payable	2,000	--	--	2,000	2,000
Other accrued liabilities (Notes 9 and 14)	4,113,451	--	--	4,113,451	3,626,338
Annuity payable	3,540	--	--	3,540	4,115
Derivative instruments (Notes 2 and 7)	366,339	--	--	366,339	440,312
Bonds payable (Note 8)	5,185,000	--	--	5,185,000	5,490,000
Total liabilities	<u>15,124,350</u>	<u>--</u>	<u>--</u>	<u>15,124,350</u>	<u>16,336,967</u>
Commitments and contingencies and related party transactions (Notes 12 and 13)					
Net assets (Notes 10 and 11):					
Unrestricted	32,369,756	--	--	32,369,756	32,688,338
Temporarily restricted	--	1,217,745	--	1,217,745	1,058,016
Permanently restricted	--	--	52,980	52,980	52,980
Total net assets	<u>32,369,756</u>	<u>1,217,745</u>	<u>52,980</u>	<u>33,640,481</u>	<u>33,799,334</u>
Total liabilities and net assets	<u>\$ 47,494,106</u>	<u>\$ 1,217,745</u>	<u>\$ 52,980</u>	<u>\$ 48,764,831</u>	<u>\$ 50,136,301</u>

See accompanying notes to combined financial statements

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Combined Statement of Activities
Year Ended December 31, 2015**

(with summarized financial information for the year ended December 31, 2014)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>	
				<u>2015</u>	<u>2014</u>
Public support and revenue					
Public support:					
Indirect public support	\$ 1,875	\$ --	\$ --	\$ 1,875	1,995
Contributions	1,543,445	1,166,847	--	2,710,292	3,155,786
Donated merchandise	34,803,144	--	--	34,803,144	34,965,370
Total public support	<u>36,348,464</u>	<u>1,166,847</u>	<u>--</u>	<u>37,515,311</u>	<u>38,123,151</u>
Revenue:					
Thrift store sales	55,165,281	--	--	55,165,281	52,305,220
Other sales	2,187,143	--	--	2,187,143	2,197,942
Contract services	7,391,050	--	--	7,391,050	7,133,194
Rehabilitation revenue	16,898,569	--	--	16,898,569	15,300,184
Technology services	2,495,189	--	--	2,495,189	2,049,175
Interest and other income	399,568	--	--	399,568	479,789
Realized and unrealized (losses) gains on investments, net	(588,037)	--	--	(588,037)	131,844
Realized (losses) gains on disposal of land, buildings and equipment (Note 14)	(270,765)	--	--	(270,765)	950
Realized (losses) on assets disposed of through restructuring (Note 14)	(177,639)	--	--	(177,639)	--
Unrealized gains on derivative instruments	73,974	--	--	73,974	30,703
Total revenue	<u>83,574,333</u>	<u>--</u>	<u>--</u>	<u>83,574,333</u>	<u>79,629,001</u>
Net assets released from restrictions	<u>1,007,118</u>	<u>(1,007,118)</u>	<u>--</u>	<u>--</u>	<u>--</u>
Total public support and revenue	<u>120,929,915</u>	<u>159,729</u>	<u>--</u>	<u>121,089,644</u>	<u>117,752,152</u>
Expenses					
Program services:					
Store operations	71,540,353	--	--	71,540,353	69,446,711
Processing of donated merchandise	7,417,990	--	--	7,417,990	6,665,544
Solicitation and transportation	6,915,841	--	--	6,915,841	6,710,648
Rehabilitation	17,675,778	--	--	17,675,778	16,138,849
Contract services	7,190,579	--	--	7,190,579	7,219,763
Technology services	1,046,793	--	--	1,046,793	730,914
Restructuring (Note 14)	285,835	--	--	285,835	--
Total program services	<u>112,073,169</u>	<u>--</u>	<u>--</u>	<u>112,073,169</u>	<u>106,912,429</u>
Supporting services:					
General and administrative	8,017,423	--	--	8,017,423	7,560,787
Fundraising	1,157,905	--	--	1,157,905	1,249,430
Total supporting services	<u>9,175,328</u>	<u>--</u>	<u>--</u>	<u>9,175,328</u>	<u>8,810,217</u>

(Combined statement of activities continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Combined Statement of Activities
(Continued)**

Year Ended December 31, 2015

(with summarized financial information for the year ended December 31, 2014)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Totals</u>	
				<u>2015</u>	<u>2014</u>
Total expenses	121,248,497	--	--	121,248,497	115,722,646
Change in net assets	(318,582)	159,729	--	(158,853)	2,029,506
Net assets at beginning of year	32,688,338	1,058,016	52,980	33,799,334	31,769,828
Net assets at end of year	<u>\$ 32,369,756</u>	<u>\$ 1,217,745</u>	<u>\$ 52,980</u>	<u>\$ 33,640,481</u>	<u>\$ 33,799,334</u>

See accompanying notes to combined financial statements

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Combined Statement of Functional Expenses
Year Ended December 31, 2015**
(with summarized financial information for the year ended December 31, 2014)

	<u>Program Services</u>							<u>Subtotal</u>
	<u>Store Operations</u>	<u>Processing of Donated Merchandise</u>	<u>Solicitation and Transportation</u>	<u>Rehabilitation</u>	<u>Contract Services</u>	<u>Technology Services</u>	<u>Restructuring</u>	
Salaries and related expenses:								
Salaries and wages	\$ 14,052,233	\$ 3,887,688	\$ 3,488,956	\$ 11,324,374	\$ 3,800,122	\$ 523,539	\$ 8,288	\$ 37,085,200
Employee benefits	1,309,319	616,370	519,098	1,952,696	761,818	53,722	(165)	5,212,858
Payroll taxes	1,898,157	592,711	529,526	1,213,958	567,055	51,876	(1,200)	4,852,083
Total salaries and related expenses	<u>17,259,709</u>	<u>5,096,769</u>	<u>4,537,580</u>	<u>14,491,028</u>	<u>5,128,995</u>	<u>629,137</u>	<u>6,923</u>	<u>47,150,141</u>
Other expenses:								
Cost of goods sold	41,288,729	205,754	--	--	8,725	--	--	41,503,208
Professional services	1,266,314	43,731	10,454	686,165	199,165	31,170	65,921	2,302,920
Supplies	726,169	244,683	142,790	116,275	343,099	12,041	9,750	1,594,807
Telephone	170,602	37,194	69,125	194,042	39,098	45,456	501	556,018
Postage	996,636	31,207	1,881	3,514	4,350	29	10,742	1,048,359
Occupancy	7,063,487	1,364,456	950,213	503,425	670,559	127,749	184,747	10,864,636
Equipment rent and maintenance	132,005	19,293	78,375	27,142	86,169	65,220	2,664	410,868
Advertising	340,078	600	10,560	17,516	45	3,488	--	372,287
Printing and publishing	102,813	12,992	6,955	127,994	13,389	3,561	585	268,289
Travel and vehicle	59,287	44,606	718,122	1,019,376	235,027	27,518	3,827	2,107,763
Conferences, conventions and meetings	81,898	14,966	2,491	58,871	7,518	14,382	175	180,301
Membership and dues to national organization	132,527	450	--	36,793	14,681	3,452	--	187,903
Awards, grants and special assistance	4,546	2,207	455	22,065	438	60	--	29,771
Interest expense	--	--	--	--	--	--	--	--
Bad debt expense	--	--	--	141,669	71,283	25,256	--	238,208
Other operating expenses	(142)	--	--	--	--	--	--	(142)
Total expenses before depreciation	<u>69,624,658</u>	<u>7,118,908</u>	<u>6,529,001</u>	<u>17,445,875</u>	<u>6,822,541</u>	<u>988,519</u>	<u>285,835</u>	<u>108,815,337</u>
Depreciation and amortization	<u>1,915,695</u>	<u>299,082</u>	<u>386,840</u>	<u>229,903</u>	<u>368,038</u>	<u>58,274</u>	<u>--</u>	<u>3,257,832</u>
Total expenses	<u>\$ 71,540,353</u>	<u>\$ 7,417,990</u>	<u>\$ 6,915,841</u>	<u>\$ 17,675,778</u>	<u>\$ 7,190,579</u>	<u>\$ 1,046,793</u>	<u>\$ 285,835</u>	<u>\$ 112,073,169</u>

(Combined statement of functional expenses continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Combined Statement of Functional Expenses
(Continued)**

Year Ended December 31, 2015

(with summarized financial information for the year ended December 31, 2014)

	<u>Supporting Services</u>				<u>Total Expenses</u>	
	<u>Subtotal</u>	<u>General & Admin</u>	<u>Fund Raising</u>	<u>Subtotal</u>	<u>2015</u>	<u>2014</u>
Salaries and related expenses:						
Salaries and wages	\$ 37,085,200	\$ 4,317,801	\$ 451,400	\$ 4,769,201	\$ 41,854,401	\$ 39,933,128
Employee benefits	5,212,858	644,779	36,059	680,838	5,893,696	5,841,942
Payroll taxes	4,852,083	413,822	32,907	446,729	5,298,812	4,719,504
Total salaries and related expenses	<u>47,150,141</u>	<u>5,376,402</u>	<u>520,366</u>	<u>5,896,768</u>	<u>53,046,909</u>	<u>50,494,574</u>
Other expenses:						
Cost of goods sold	41,503,208	--	--	--	41,503,208	40,758,841
Professional services	2,302,920	734,642	105,738	840,380	3,143,300	2,599,191
Supplies	1,594,807	82,358	12,958	95,316	1,690,123	1,540,798
Telephone	556,018	79,701	8,374	88,075	644,093	678,594
Postage	1,048,359	13,168	5,750	18,918	1,067,277	1,169,443
Occupancy	10,864,636	371,877	6,519	378,396	11,243,032	10,468,175
Equipment rent and maintenance	410,868	188,006	67,559	255,565	666,433	524,403
Advertising	372,287	10,605	128,162	138,767	511,054	485,215
Printing and publishing	268,289	89,940	58,257	148,197	416,486	437,205
Travel and vehicle	2,107,763	37,276	8,110	45,386	2,153,149	2,070,823
Conferences, conventions and meetings	180,301	190,377	227,849	418,226	598,527	535,462
Membership and dues to national organization	187,903	21,503	(20,504)	999	188,902	240,208
Awards, grants and special assistance	29,771	14,718	18,136	32,854	62,625	38,811
Interest expense	--	157,055	--	157,055	157,055	178,013
Bad debt expense	238,208	--	2,500	2,500	240,708	47,328
Other operating expenses	(142)	--	--	--	(142)	528
Total expenses before depreciation	<u>108,815,337</u>	<u>7,367,628</u>	<u>1,149,774</u>	<u>8,517,402</u>	<u>117,332,739</u>	<u>112,267,612</u>
Depreciation and amortization	<u>3,257,832</u>	<u>649,795</u>	<u>8,131</u>	<u>657,926</u>	<u>3,915,758</u>	<u>3,455,034</u>
Total expenses	<u>\$ 112,073,169</u>	<u>\$ 8,017,423</u>	<u>\$ 1,157,905</u>	<u>\$ 9,175,328</u>	<u>\$ 121,248,497</u>	<u>\$ 115,722,646</u>

See accompanying notes to combined financial statements

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Combined Statement of Cash Flows
Year Ended December 31, 2015**

(with summarized financial information for the year ended December 31, 2014)

	2015	2014
Cash flows from operating activities:		
Change in net assets	\$ (158,853)	\$ 2,029,506
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Change in donated inventory	(83,156)	(98,161)
Change in donated investments	--	(18,534)
Provision for bad debts	78,734	(14,046)
Depreciation and amortization	3,903,391	3,442,668
Amortization of bond issuance cost	12,367	11,898
Realized and unrealized losses (gains) on investments, net	588,037	(131,844)
Realized losses (gains) on the disposal of land, buildings and equipment	270,765	(950)
Realized losses on assets disposed of through restructuring	177,639	--
Unrealized (gains) on derivative instruments	(73,973)	(30,703)
(Increase) decrease in:		
Restricted cash	400,000	--
Accounts receivable - net	(217,960)	99,599
Contributions receivable - net	(162,743)	(784,072)
Prepaid expenses and deposits	33,687	(229,448)
Increase (decrease) in:		
Accounts payable	(206,501)	242,537
Accrued salaries, wages and vacation payable	(1,113,681)	808,948
Other accrued liabilities	487,113	48,655
Annuity payable	(575)	(564)
Net cash provided by operating activities	3,934,291	5,375,489
Cash flows from investing activities:		
Purchase of investments	(12,686)	(1,179,386)
Proceeds from the sale of investments	958,141	44,271
Purchase of land, buildings and equipment	(3,901,623)	(3,337,095)
Proceeds from sale of land, buildings and equipment	35,296	950
Net cash (used in) investing activities	(2,920,872)	(4,471,260)

(Combined statement of cash flows continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Combined Statement of Cash Flows
(Continued)**

Year Ended December 31, 2015

(with summarized financial information for the year ended December 31, 2014)

	<u>2015</u>	<u>2014</u>
Cash flows from financing activities:		
Principal repayments of bonds	(305,000)	(290,000)
Net cash (used in) financing activities	<u>(305,000)</u>	<u>(290,000)</u>
Net increase in cash	708,419	614,229
Cash and cash equivalents at beginning of year	<u>4,614,304</u>	<u>4,000,075</u>
Cash and cash equivalents at end of year	<u>\$ 5,322,723</u>	<u>\$ 4,614,304</u>
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	<u>\$ 158,608</u>	<u>\$ 178,702</u>

Supplemental disclosure of non-cash investing activity:

During the year ended December 31, 2015, the Organization sold document destruction equipment in exchange for receivables totaling \$324,790.

See accompanying notes to combined financial statements

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
December 31, 2015**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization - Goodwill Industries of Orange County, California provides evaluation, rehabilitation, training, and employment services for people with disabilities and other barriers in the local community. Revenue to fund these services is derived from thrift store sales, donated merchandise, rehabilitation services, contract services, contributions, fund-raising activities, grants from federal and state agencies and other charitable organizations, technology services, and indirect public support. Goodwill operates thrift stores located throughout Orange County.

In 2001, Goodwill formed Landmark Services, Inc., an affiliate, as a nonprofit public benefit corporation. Landmark is dedicated to assisting individuals with severe disabilities in obtaining productive and valuable training and employment under federal, state, and local set aside programs and other commercial ventures.

Principles of Combination - The combined financial statements include the accounts of Goodwill Industries of Orange County, California as well as Landmark Services, Inc. All inter-entity accounts and transactions have been eliminated in the combination.

Basis of Presentation - The accompanying combined financial statements include the accounts of Goodwill Industries of Orange County, California as well as its affiliate, Landmark Services, Inc. (the Organization), and have been prepared on the accrual basis of accounting. Net assets are classified based on the existence or absence of third-party donor restrictions and are reported as follows:

- Unrestricted net assets represent the portion of expendable funds available for support of operations.
- Temporarily restricted net assets are classified as such based on donor stipulations that they be used in a later period, be used for a specific purpose, or both. As donor restrictions are satisfied, amounts are reclassified to the unrestricted class as net assets released from restrictions.
- Permanently restricted net assets represent an endowment to be held in perpetuity. Investment income earned on this endowment is unrestricted.

The Organization's policy is to record temporarily restricted gifts that are received and spent in the same year as unrestricted support.

(Note 1 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Comparative Data - The combined financial statements include prior-year summarized comparative information in total, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Organization's combined financial statements for the year ended December 31, 2014 from which the summarized information was derived.

Concentration of Credit Risk - The Organization maintains cash deposits with major banks, which are FDIC insured up to \$250,000. As of December 31, 2015, the Organization had certain monies deposited in excess of the FDIC insurance limit.

Cash and Cash Equivalents - The Organization considers all highly liquid investments with an original maturity of three months or less when purchased and money market funds to be cash equivalents.

Donated Merchandise - The Organization estimates the value of its donated merchandise at fair value at the date of contribution.

Investments - Investments represent monies invested in mutual funds, marketable securities, U.S. government securities, alternative assets, and a hedge fund. Investments in equity securities with readily determined fair values and all debt securities, alternative assets, and the hedge fund are reported at fair market value with realized and unrealized gains and losses included in the combined statement of activities.

The Organization has adopted policies for its investments that are intended to produce results that exceed the price and yield results of custom benchmarks while assuming a moderate level of risk.

Derivative Instruments - Interest rate swap contracts are reported at fair value and are recognized in the combined statement of financial position as either assets or liabilities, depending on the rights or obligations under the contracts. Such derivative instruments are used to hedge against the risk resulting from the variability of interest rates. Changes in fair value of derivative instruments are recognized as a change in net assets in the period of change.

(Note 1 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Charitable Gift Annuity - Amounts due under charitable gift annuity agreements represents gifts received under agreements which guarantee interest payments until the death of the donor. Annuities are placed in excess and reserve accounts, as received. These funds are managed by an independent fiduciary. Outsourcing the administration of these accounts is a management tool used by the Organization to assure that adequate monies are available to pay the annuity liabilities; however, there is no donor or other outside restrictions on the funds in these accounts. The differences between the amounts received and the discounted value of future annuity payments are recorded as contributions. The discounted value of future annuity payments has been determined annually based on the ages and life expectancies of the donors as of the combined statement of financial position date.

Contributed Services - A number of volunteers have made significant contributions of their time to support the Organization's functions. Only those amounts for which an objective basis is available to measure the value of such services are reflected in the combined financial statements. Contributed services are recognized if the services (a) create or enhance long-lived assets, or (b) require specialized skills, are provided by individuals possessing those skills and would need to be purchased if not provided by donation. As of December 31, 2015, the value of this contributed time does not meet the criteria for recognition of contributed services and, accordingly, is not reflected in the accompanying combined financial statements.

Land, Buildings and Equipment - Land, buildings and equipment are stated at cost. Depreciation and amortization expenses are calculated on the straight-line method. The depreciation and amortization methods are designed to amortize the cost of the assets over the estimated useful lives, in years, of the respective assets as follows:

Buildings	10 to 30 years
Building improvements	5 to 10 years
Furniture and equipment	3 to 10 years
Vehicles	3 to 10 years
Computer hardware	2 ½ years
Computer software	2 years

Maintenance and repairs are charged to expense as incurred. Renewals and improvements of a major nature are capitalized. At the time of retirement or other disposition of property and equipment, or once property and equipment have been fully depreciated, the cost and accumulated depreciation are removed from the accounts and any resulting gains or losses are reflected in income.

(Note 1 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Impairment of Long-Lived Assets and Long-Lived Assets to be Disposed of - Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows (undiscounted and without interest) expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of support, revenues and expenses during the reporting period. Actual results could differ from those estimates.

Functional Allocation of Expenses - The costs of providing the various programs and other activities have been summarized on a functional basis in the combined statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Restructuring - The Organization is currently undergoing a one-time restructuring initiative (Note 14). Identifying and calculating the cost of restructuring and exiting operations requires certain assumptions to be made, such as anticipated future liabilities attributable to the restructuring activities, which are accrued and recognized as expense in the current period. The Organization believes its estimates are reasonable, however, significant judgement is required, and these estimates and assumptions may change as additional information becomes available.

Income Taxes - Goodwill Industries of Orange County, California and Landmark Services, Inc. are exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code (the Code), and are exempt from state income taxes under the comparable state tax code, as charitable organizations whereby only unrelated business income, as defined by Section 512(a)(1) of the Code, is subject to federal income tax.

The Organization has adopted the provisions of the accounting standard relating to accounting and reporting for uncertainty in income taxes. For the Organization, these provisions could be applicable to the incurrence of unrelated business income. Because of the Organization's general tax-exempt status, adoption of the standard does not have a material impact on the Organization's combined financial statements.

(Note 1 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Net Assets - Unrestricted net assets include quasi-endowment accounts. Such accounts primarily represent transactions that the Organization's board of directors have designated as income-producing investments where the principal is not to be used to support the Organization's general activities. Such assets have no donor-imposed restrictions or the restrictions have already expired. Quasi-endowments totaled \$387,305 at December 31, 2015 and have been included in unrestricted net assets in the accompanying combined statement of financial position (Note 11).

Advertising Costs - All advertising costs, which include direct response advertising costs, are expensed by the Organization as they are incurred. Total advertising cost for the year ended December 31, 2015 was \$511,054.

Contributory Retirement Plan - Effective January 1, 1989, the Organization adopted a contributory retirement plan covering all employees over 21 years of age. The plan, as amended in 1990, provides for an employer base contribution of 4.0% of participating employees' salaries, as defined, for all participating employees that contribute at least 1% of their eligible salary during the plan year. Participating employees may also contribute up to a maximum allowable limit established by the Internal Revenue Service. The Organization matches 100% of these contributions up to a maximum of 3.0% of salary. Participants become fully vested after four years of service. The total amount charged to expense related to the plan for the year ended December 31, 2015 was \$1,441,357.

Leases - The Organization leases certain trucks, equipment and retail stores under operating and capital leases. Leases which meet certain criteria are classified as capital leases, and assets and liabilities are recorded at amounts equal to the lesser of the present value of the minimum lease payments or the fair value of leased properties at the beginning of the respective lease terms. Such assets are amortized in a manner consistent with the Organization's normal depreciation policies over the related lease terms or their economic lives. Interest expense relating to the lease liabilities is recorded at constant rates of interest over the terms of the leases. Leases which do not meet such criteria are classified as operating leases, and related rentals are charged to expense as incurred.

Restricted Cash - The Organization has restricted cash of \$470,000 at December 31, 2015 on deposit with a financial institution in conjunction with the cash collateral interest rate swap agreement (Note 7). The deposited amount can fluctuate based on interest rates. The minimum collateral deposit is \$300,000 and the funds may not be used by the Organization until the termination or expiration of the agreement.

(Note 1 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Fair Value Measurements - The carrying value of financial instruments in the combined financial statements approximates fair value.

For fair value measurements of financial assets and financial liabilities (Note 2), and for fair value measurements of non-financial items that are recognized and disclosed at fair value in the combined financial statements on a recurring basis, the Organization has adopted generally accepted accounting principles (GAAP) standards that define fair value 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.

GAAP establishes a three-level fair value hierarchy that describes the inputs that are used to measure the fair values of respective assets and liabilities:

- Level 1: fair values are based on quoted prices in active markets for identical assets and liabilities. The Organization's Level 1 assets include mutual funds, and marketable securities, including U.S. government securities.
- Level 2: fair values are based on observable inputs that include: quoted market prices for similar assets or liabilities, quoted market prices that are not in an active market, or other inputs that are observable in the market and can be corroborated by observable market data for substantially the full term of the asset. The Organization's Level 2 assets include charitable gift annuities and a master limited partnership fund and Level 2 liabilities include derivative instruments.
- Level 3: fair values are calculated by the use of pricing models and/or discounted cash flow methodologies, and may require significant management judgment or estimation. These methodologies may result in a significant portion of the fair value being derived from unobservable data. The Organization's Level 3 assets include alternative assets, a hedge fund, and contributions receivable.

Fair value estimates are made at a specific point in time, based on available market information and judgments about the financial asset, including estimates of timing, amount of expected future cash flows, and the credit standing of the issuer. In some cases, the fair value estimates cannot be substantiated by comparison to independent markets. In addition, the disclosed fair values may not be realized in the immediate settlement of the financial asset or liability. In addition, the disclosed fair values do not reflect any premium or discount that could result from offering for sale at one time an entire holding of a particular financial asset. Potential taxes and other expenses that would be incurred in an actual sale or settlement are not reflected in amounts disclosed.

(Note 1 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recent Accounting Pronouncements - In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, *Leases (Topic 842)*. Under ASU No. 2016-02, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date:

- A lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and
- A right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term.

ASU No. 2016-02 is effective for fiscal years beginning after December 15, 2019. The Organization is in the process of assessing the potential impact of the ASU on its financial statements.

In April 2014, the FASB issued ASU No. 2014-8, *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*, which changes the criteria for reporting discontinued operations and requires additional disclosures about discontinued operations. The standard requires that an entity report as a discontinued operation only a disposal that represents a strategic shift in operations that has a major effect on its operations and financial results. ASU No. 2014-8 is effective prospectively for new disposals that occur within annual periods beginning on or after December 15, 2014. The Organization adopted ASU No. 2014-8 for the year ended December 31, 2015 as the disposal of its document destruction business did not qualify as a discontinued operation as determined under the new guidance because it was not considered a strategic shift in operations that had a major effect on the operations of the Organization (Note 14).

Subsequent Events - The Organization evaluated subsequent events through May 25, 2016, the date these combined financial statements were available to be issued. There were no material subsequent events that required recognition or additional disclosure in these combined financial statements.

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 2 - INVESTMENTS AND FINANCIAL ASSETS AND LIABILITIES

The following table summarizes the fair values of the Organization's investments and other applicable assets and liabilities at December 31, 2015 in accordance with these fair-value levels:

	<i>Fair Value as of December 31, 2015</i>			<i>Total</i>
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	
Assets:				
Mutual funds:				
Balanced funds	\$ 392,007	\$ --	\$ --	\$ 392,007
Fixed income funds	2,396,160	--	--	2,396,160
Domestic funds	1,861,855	--	--	1,861,855
International funds	3,450,749	--	--	3,450,749
Total mutual funds	<u>8,100,771</u>	<u>--</u>	<u>--</u>	<u>8,100,771</u>
Hedge fund	--	--	2,279,239	2,279,239
Master limited partnership fund	--	249,808	--	249,808
Charitable gift annuities	--	750	--	750
Alternative assets	--	--	387,305	387,305
Total investments	<u>8,100,771</u>	<u>250,558</u>	<u>2,666,544</u>	<u>11,017,873</u>
Contributions receivable - net	<u>--</u>	<u>--</u>	<u>1,206,632</u>	<u>1,206,632</u>
Total assets	<u>\$ 8,100,771</u>	<u>\$ 250,558</u>	<u>\$ 3,873,176</u>	<u>\$ 12,224,505</u>
Liabilities:				
Derivative instruments	<u>\$ --</u>	<u>\$ 366,339</u>	<u>\$ --</u>	<u>\$ 366,339</u>
Total liabilities	<u>\$ --</u>	<u>\$ 366,339</u>	<u>\$ --</u>	<u>\$ 366,339</u>

Investment income for the year ended December 31, 2015 is summarized as follows:

Interest and dividend income	\$ 363,709
Investment fees	(65,310)
Realized and unrealized losses, net	<u>(588,037)</u>
	<u>\$ (289,638)</u>

(Note 2 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 2 - INVESTMENTS AND FINANCIAL ASSETS AND LIABILITIES (Continued)

The following table sets forth a summary of all of the Organization's Level 3 assets measured at fair value for the year ended December 31, 2015.

	<u>Investments</u>	<u>Contributions Receivable</u>
Balance, beginning of year	\$ 2,681,266	\$ 1,043,889
New contributions/payments received (net)	--	167,541
Change in allowance for uncollectibles	--	(6,694)
Change in present value discount	--	1,896
Interest and dividends	4,576	--
Investment losses (net)	<u>(19,298)</u>	<u>--</u>
Balance, end of year	<u>\$ 2,666,544</u>	<u>\$ 1,206,632</u>

NOTE 3 - CONTRIBUTIONS RECEIVABLE

The Organization has recognized uncollected contribution promises as temporarily restricted support. These receivables represent unconditional promises to give to the Organization to be collected through 2024. Uncollected promises at December 31, 2015 that are expected to be collected within one year are recorded at the estimated net realizable value. Uncollected promises at December 31, 2015 that are expected to be collected in future years are recorded at the present value of the estimated future cash flows. The discounts on those amounts are computed using a 5% rate applicable in the year in which the promises were made. Amortization of the discount is included in contributions revenue for the year ended December 31, 2015. Future collections of the contributions receivable are scheduled as follows:

Amounts due in:	
Less than one year	\$ 428,960
One to five years	550,735
More than five years	<u>400,000</u>
	1,379,695
Less: allowance for uncollectibles	(63,118)
Less: unamortized discount	<u>(109,945)</u>
	<u>\$ 1,206,632</u>

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 4 - LAND, BUILDINGS AND EQUIPMENT

Land, buildings and equipment are recorded at cost and consist of the following at December 31, 2015:

Land	\$ 4,546,888
Buildings and improvements	23,171,096
Furniture and equipment	9,065,006
Vehicles	486,602
Construction in process	<u>1,339,306</u>
Total land, buildings and equipment	38,608,898
Less accumulated depreciation	<u>(14,331,553)</u>
Net land, buildings and equipment	<u>\$ 24,277,345</u>

Total depreciation and amortization expense for the year ended December 31, 2015 was \$3,903,391.

NOTE 5 - LINE OF CREDIT

At December 31, 2015, the Organization has a \$3,510,000 revolving line of credit with a bank to be drawn down upon as needed with an interest rate of 0.5% above prime rate (prime rate at December 31, 2015 was 3.50%). This bank borrowing is collateralized by accounts receivable, inventories and land, buildings and equipment, and is set to expire on August 1, 2016. There was no outstanding balance on this line of credit at December 31, 2015.

The Organization has \$2,364,000 of stand-by letters of credit with the bank in connection with its workers compensation policy (Note 6), which is part of the total indebtedness allowed under the revolving line of credit and subject to the same terms and conditions. At December 31, 2015, the Organization did not have any balances outstanding against this credit facility. These letters of credit reduce the available amount which can be borrowed against the bank's revolving line of credit. Accordingly, availability on the line of credit was \$1,146,000 at December 31, 2015.

(Note 5 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 5 - LINE OF CREDIT (Continued)

The Organization has a \$5,261,710 direct-pay letter of credit with the bank, independent of the revolving line of credit, in connection with the 2006 Bonds (Note 8). At December 31, 2015, the Organization did not have any balances outstanding against this credit facility. The letter of credit is renewed annually on March 9, unless notice is given by either party, with a final maturity on March 9, 2017. This bank borrowing is collateralized by real property at the main campus in Santa Ana, California.

Under the terms of the above agreement, the Organization is subject to maintaining a maximum debt to tangible net worth ratio, a minimum level of EBITDA coverage ratio, change in net assets, capital expenditures and unencumbered liquid assets. As of December 31, 2015, the Organization was in compliance with the aforementioned financial covenants.

NOTE 6 - SELF INSURANCE

The Organization carries a large-deductible workers' compensation policy and is responsible for paying the first \$350,000 of each claim occurrence up to \$3,200,000 in aggregate per policy plan year. The Organization has paid certain amounts of the claims known to date and has provided additional accrued liabilities for an estimate of the ultimate claims known to date. In developing these estimates, the Organization uses estimated losses (loss picks) provided by actuaries of the insurance broker to estimate the ultimate claim exposure. Given the estimation nature of this area, it is reasonably possible that future adjustments to these estimates will be required. Based upon the information known at December 31, 2015, management believes it has provided adequate reserves for all claims that will be paid by the Organization.

Accrued liabilities for workers compensation for the year ended December 31, 2015 was \$2,317,903 and this amount is included in other accrued liabilities in the Organization's combined statement of financial position (Note 9).

The Organization has elected to be self-insured for the purposes of employees' unemployment claims and has elected to reimburse the Employment Development Department, under the prorated cost of benefits method, for all claims filed by its employees. Estimated accrued unemployment liability at December 31, 2015 of \$285,327 represents estimated future claims arising from payroll paid up to December 31, 2015 and this amount is included in other accrued liabilities in the Organization's combined statement of financial position.

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 7 - DERIVATIVE INSTRUMENTS

The Organization used variable-rate debt to finance the \$9,850,000 Variable Rate Demand Revenue Bonds issued in 2006 (2006 Bonds) and the \$7,700,000 Variable Rate Demand Revenue Bonds issued in 2008 (2008 Bonds) (Note 8). The debt obligations expose the Organization to variability in interest payments due to changes in interest rates. Management believes that it is prudent to limit the variability of its interest payments. To meet this objective, management entered into interest rate swap agreements to manage fluctuations in cash flows resulting from interest rate risk. The swaps changed the variable-rate cash flows exposure on the debt obligations to fixed-rate cash flows. Under the terms of the interest rate swaps, the Organization receives variable interest rate payments and makes fixed interest rate payments, thereby creating the equivalent of fixed-rate debt.

By using derivative financial instruments to hedge its exposure to changes in interest rates, the Organization exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Organization, which creates credit risk for the Organization. When the fair value of a derivative contract is negative, the Organization owes the counterparty and, therefore, it does not possess credit risk. The Organization minimizes the credit risk in derivative instruments by entering into transactions with high-quality counterparties.

Market risk is the adverse effect on the value of a financial instrument that results from a change in interest rates. The market risk associated with interest-rate contracts is managed by establishing the monitoring parameters that limit the types and degree of market risk that may be undertaken.

On February 12, 2010, the Organization entered into an interest rate swap transaction, collateralized by cash, with an effective date of February 12, 2010, and a termination date of January 1, 2020. The swap contract was executed with the purpose of fixing the interest rate on approximately 50% of the 2006 and 2008 Bonds (Note 8). Under the terms of the agreement, the Organization pays interest at a fixed rate of 3.06% and receives interest at 70% of 3-month LIBOR. The difference between interest earned and the interest obligation accrued is received or paid the first day of each month and is recorded as interest expense. At December 31, 2015, the notional amount was \$5,265,000 and the estimated liability on the contract reflected on the combined statement of financial position was \$366,339. A cumulative gain of \$73,974 from changes in the swap's contract fair value has been recognized as a change in net assets in the current period. At December 31, 2015, the required cash on deposit with a financial institution totaled \$470,000 and is included as restricted cash in the combined statement of financial position.

(Note 7 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 7 - DERIVATIVE INSTRUMENTS (Continued)

On January 27, 2010, the Organization entered into a \$4,186,250 interest rate cap transaction with an effective date of February 1, 2010. The cap was executed with the purpose of limiting the interest rates on approximately 25% of the 2006 and 2008 Bonds (Note 8). Under the agreement, the Organization paid interest at a floating rate of 70% of 3-month LIBOR up to 8.57%. If the floating interest rate based on LIBOR exceeded 8.57%, the interest paid by the Organization would be capped at 70% of 3-month LIBOR (effectively 6.00%). The interest rate cap agreement terminated on January 1, 2015.

NOTE 8 - BONDS PAYABLE

On March 9, 2006, the Organization authorized the issuance of \$9,850,000 of Variable Rate Demand Revenue Bonds, payable to the California Infrastructure and Economic Development Bank. The bonds mature on March 1, 2031 and bear interest at a Weekly Interest Rate as determined by the Remarketing Agent. The debt repayment schedule provides for principal payments commencing March 1, 2007. The bonds are supported by a direct-pay letter of credit with a bank (Note 6). The costs associated with this bond issue are being amortized over twenty-five years. The proceeds of these bonds were used to finance the renovation and expansion of the Organization's retail and wholesale store facilities, to make certain improvements related to street beautification and parking lot lighting and to purchase equipment and fixtures to be used or installed in conjunction with the project.

The annual aggregate maturities of bond obligations are as follows:

Years ending December 31:	
2016	\$ 320,000
2017	335,000
2018	355,000
2019	370,000
2020	390,000
Thereafter	<u>3,415,000</u>
	<u>\$ 5,185,000</u>

Amortization expense associated with the cost of issuing the bonds totaled \$12,367 for the year ended December 31, 2015.

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 9 - OTHER ACCRUED LIABILITIES

Other accrued liabilities at December 31, 2015 consist of the following:

Deferred rent	\$ 704,083
Loss contingencies (Note 12)	214,357
Unemployment benefits (Note 6)	285,327
Workers' compensation (Note 6)	2,317,903
Restructuring (Note 14)	285,835
Other	<u>305,946</u>
	<u>\$ 4,113,451</u>

NOTE 10 - NET ASSETS

Temporarily restricted net assets at December 31, 2015 consist of the following:

Charitable Gift Annuity investments in which the Organization is the beneficiary of the assets upon the death of the donor.	\$ 11,113
Uncollected contribution promises	<u>1,206,632</u>
Total temporarily restricted net assets	<u>\$ 1,217,745</u>

NOTE 11 - ENDOWMENTS

The endowment consists of various individual funds established for a variety of purposes, consisting of both donor-restricted endowment funds and funds designated by the Board of Directors to function as endowment. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowment, are classified and reported based on the existence or absence of donor-imposed restrictions.

(Note 11 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 11 - ENDOWMENTS (Continued)

Interpretation of Relevant Law

The Board of Directors has interpreted Uniform Prudent Management of Institutional Funds Act ("UPMIFA"), which the State of California has enacted, as requiring the preservation of the historic dollar 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 permanently restricted net assets:

- The original value of gifts donated to the permanent endowment,
- The original value of subsequent gifts to the permanent endowment, and
- Accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time accumulation is added to the fund.

Endowment Net Assets Composition by Type of Fund

	<u>Unrestricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ --	\$ 52,980	\$ 52,980
Board-designated endowment funds	<u>387,305</u>	<u>--</u>	<u>387,305</u>
Total	<u>\$ 387,305</u>	<u>\$ 52,980</u>	<u>\$ 440,285</u>

(Note 11 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 11 - ENDOWMENTS (Continued)

Changes in Endowment Net Assets

	<u>Unrestricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 406,817	\$ 52,980	\$ 459,797
Investment return:			
Investment income, net	4,576	--	4,576
Net appreciation (realized and unrealized)	(24,088)	--	(24,088)
Total investment return	(19,512)	--	(19,512)
Total	\$ 387,305	\$ 52,980	\$ 440,285

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Organization to retain as a fund of perpetual duration. There were no such deficiencies as of December 31, 2015.

Return Objectives and Risk Parameters

The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Organization must hold in perpetuity as well as board-designated funds. Under this policy, as approved by the Board of Directors, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of major indices (e.g. S&P 500) while assuming a moderate level of investment risk. The Organization expects its endowment funds, over time, to provide an average annual rate of return of the National Consumer Price Index plus 5% for the aggregate investments over a period of five years. Actual returns in any given year may vary from this amount.

(Note 11 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 11 - ENDOWMENTS (Continued)

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization targets a diversified asset allocation to achieve its long-term objectives within prudent risk constraints.

Spending Policy and Investment Objectives

The Organization has a policy that allows for the appropriation for distribution each year of up to 5% of its endowment fund's average year-end value over the past three years, provided that such payout shall not cause the total value of the endowment account to decline below the cumulative value of the original amounts donated. In establishing this policy, the Organization considered the long-term expected return on its endowment. Accordingly, over the long term, the Organization expects the current spending policy to allow its endowment to grow at an average of 2% annually. This is consistent with the Organization's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

NOTE 12 - COMMITMENTS AND CONTINGENCIES

Leases

The Organization leases trucks, office equipment and certain retail stores under noncancelable operating lease agreements. The monthly rents on the aforementioned leases range from \$150 to \$107,828 expiring at various dates through August 2025. Under the leasing arrangements for the retail stores, the Organization is required to pay property taxes and common area charges (maintenance, utilities and property insurance) attributable to the leases.

The Organization also leases space for various attended donation centers. The operating lease agreements are month to month and require monthly payments ranging from none to \$1,055.

(Note 12 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 12 - COMMITMENTS AND CONTINGENCIES (Continued)

Future minimum annual rental payments under noncancelable operating leases at December 31, 2015 are as follows:

Years ending December 31,	
2016	\$ 5,282,963
2017	5,392,485
2018	4,889,085
2019	3,989,990
2020	3,564,651
Thereafter	<u>7,893,125</u>
	<u>\$ 31,012,299</u>

Rent expense related to the aforementioned operating lease agreements was \$6,640,779 for the year ended December 31, 2015.

Loss Contingencies

The Organization is subject to certain outside claims and litigation arising in the ordinary course of business. The Organization's management and its legal counsel assess such contingent liabilities, and such assessment inherently involves an exercise of judgment. In assessing loss contingencies related to legal proceedings that are pending against the Organization or unasserted claims that may result in such proceedings, the Organization's legal counsel evaluates the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought therein.

If the assessment of a contingency indicates that it is probable that a material loss has been incurred and the amount of the liability can be estimated, then the estimated liability would be accrued in the Organization's combined financial statements. If the assessment indicates that a potentially material loss contingency is not probable, but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material, would be disclosed.

(Note 12 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

**Notes to Combined Financial Statements
(Continued)
December 31, 2015**

NOTE 12 - COMMITMENTS AND CONTINGENCIES (Continued)

Loss contingencies considered remote are generally not disclosed unless they involve guarantees, in which case the nature of the guarantee would be disclosed.

At December 31, 2015 the Organization had accrued \$214,357 in its combined statement of financial position for pending legal proceedings against the Organization (Note 9).

NOTE 13 - RELATED PARTY TRANSACTIONS

Landmark Services, Inc. pays Goodwill Industries of Orange County, California, a related entity through common board members, approximately \$18,000 a month for administrative services. The total amount received for such administrative and other services for the year ended December 31, 2015 amounted to \$239,652. This amount has been eliminated during the combination.

NOTE 14 - RESTRUCTURING

During the year ended December 31, 2015, the Organization underwent a restructuring initiative which included the disposal of its document destruction business, the termination of a major lease agreement for the facility containing the document destruction business, the relocation of certain other business functions to preexisting facilities, and the opening of a distribution center that will house its inventory processing and distribution activities.

Upon announcing the restructuring initiative, the Organization has recorded future charges related to the restructuring such as lease termination fees, decommissioning expenses, facility carrying costs, and fees for professional services provided in connection with the initiative. As of and for the year ended December 31, 2015, the Organization has recorded future charges relating to the restructuring initiative totaling \$285,835, which are included in other accrued liabilities in the combined statement of financial position as well as in restructuring expenses in the combined statement of activities (Note 9). Such costs are classified in further detail in the combined statement of functional expenses.

In addition, the Organization sold certain equipment that was used in its document destruction business and also disposed of other assets that were abandoned upon terminating the lease agreement for the facility housing the document destruction operations. During the year ending December 31, 2015, the Organization recorded losses on the disposal of property and equipment upon termination of the facility lease and losses the sale of document destruction equipment of \$270,765 and \$177,639, respectively, which are included in the combined statement of activities.

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

Supplementary Information

**Goodwill Industries of Orange County
Statement of Financial Position
December 31, 2015**

<u>ASSETS</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Cash and cash equivalents	\$ 3,765,503	\$ 10,363	\$ --	\$ 3,775,866
Restricted cash	470,000	--	--	470,000
Investments	10,964,143	750	52,980	11,017,873
Accounts receivable (net of allowance for doubtful accounts of \$165,040)	2,929,630	--	--	2,929,630
Contributions receivable - net	--	1,206,632	--	1,206,632
Due from Landmark Services, Inc.	3,826	--	--	3,826
Inventory	1,739,759	--	--	1,739,759
Prepaid expenses and deposits	1,006,630	--	--	1,006,630
Bond issuance cost - net	187,558	--	--	187,558
Land, buildings and equipment - net of accumulated depreciation	<u>24,225,741</u>	<u>--</u>	<u>--</u>	<u>24,225,741</u>
Total assets	<u>\$ 45,292,790</u>	<u>\$ 1,217,745</u>	<u>\$ 52,980</u>	<u>\$ 46,563,515</u>
 <u>LIABILITIES AND NET ASSETS</u>				
Liabilities:				
Accounts payable	\$ 2,023,437	\$ --	\$ --	\$ 2,023,437
Accrued salaries, wages and vacation payable	3,208,496	--	--	3,208,496
Income taxes payable	2,000	--	--	2,000
Other accrued liabilities	3,767,591	--	--	3,767,591
Annuity payable	3,540	--	--	3,540
Derivative instruments	366,339	--	--	366,339
Bonds payable	<u>5,185,000</u>	<u>--</u>	<u>--</u>	<u>5,185,000</u>
Total liabilities	<u>14,556,403</u>	<u>--</u>	<u>--</u>	<u>14,556,403</u>
Net assets:				
Unrestricted	30,736,387	--	--	30,736,387
Temporarily restricted	--	1,217,745	--	1,217,745
Permanently restricted	<u>--</u>	<u>--</u>	<u>52,980</u>	<u>52,980</u>
Total net assets	<u>30,736,387</u>	<u>1,217,745</u>	<u>52,980</u>	<u>32,007,112</u>
Total liabilities and net assets	<u>\$ 45,292,790</u>	<u>\$ 1,217,745</u>	<u>\$ 52,980</u>	<u>\$ 46,563,515</u>

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

Supplementary Information

**Goodwill Industries of Orange County
Statement of Activities
Year Ended December 31, 2015**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Public support and revenue				
Public support:				
Indirect public support	\$ 1,875	\$ --	\$ --	\$ 1,875
Contributions	1,543,445	1,166,847	--	2,710,292
Donated merchandise	34,803,144	--	--	34,803,144
Total public support	<u>36,348,464</u>	<u>1,166,847</u>	<u>--</u>	<u>37,515,311</u>
Revenue:				
Thrift store sales	55,165,281	--	--	55,165,281
Other sales	2,187,143	--	--	2,187,143
Contract services	3,392,588	--	--	3,392,588
Rehabilitation revenue	16,898,569	--	--	16,898,569
Technology services	2,495,189	--	--	2,495,189
Interest and other income	398,844	--	--	398,844
Realized and unrealized losses on investments, net	(588,037)	--	--	(588,037)
Realized losses on disposal of Land, buildings and equipment	(270,765)	--	--	(270,765)
Realized losses on assets disposed of through restructuring	(177,639)	--	--	(177,639)
Unrealized gains on derivative instruments	73,974	--	--	73,974
Total revenue	<u>79,575,147</u>	<u>--</u>	<u>--</u>	<u>79,575,147</u>
Net assets released from restrictions	<u>1,007,118</u>	<u>(1,007,118)</u>	<u>--</u>	<u>--</u>
Total public support and revenue	<u>116,930,729</u>	<u>159,729</u>	<u>--</u>	<u>117,090,458</u>

(Schedule 2 continued on the following page)

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

Supplementary Information

**Goodwill Industries of Orange County
Statement of Activities
Year Ended December 31, 2015**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Expenses				
Program services:				
Store operations	71,540,353	--	--	71,540,353
Processing of donated merchandise	7,417,990	--	--	7,417,990
Solicitation and transportation	6,915,841	--	--	6,915,841
Rehabilitation	17,675,778	--	--	17,675,778
Contract services	3,837,117	--	--	3,837,117
Technology services	1,046,793	--	--	1,046,793
Restructuring	285,835	--	--	285,835
Total program services	<u>108,719,707</u>	<u>--</u>	<u>--</u>	<u>108,719,707</u>
Supporting services:				
General and administrative	7,652,806	--	--	7,652,806
Fundraising	1,157,905	--	--	1,157,905
Total supporting services	<u>8,810,711</u>	<u>--</u>	<u>--</u>	<u>8,810,711</u>
Total expenses	<u>117,530,418</u>	<u>--</u>	<u>--</u>	<u>117,530,418</u>
Change in net assets	(599,689)	159,729	--	(439,960)
Net assets at beginning of year	<u>31,336,076</u>	<u>1,058,016</u>	<u>52,980</u>	<u>32,447,072</u>
Net assets at end of year	<u>\$ 30,736,387</u>	<u>\$ 1,217,745</u>	<u>\$ 52,980</u>	<u>\$ 32,007,112</u>

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

Supplementary Information

**Landmark Services, Inc.
Statement of Financial Position
December 31, 2015**

<u>ASSETS</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Cash and cash equivalents	\$ 1,546,857	\$ --	\$ --	\$ 1,546,857
Accounts receivable (net of allowance for doubtful accounts of \$9,276)	550,381	--	--	550,381
Prepaid expenses and deposits	56,300	--	--	56,300
Land, buildings and equipment - net of accumulated depreciation	<u>51,604</u>	<u>--</u>	<u>--</u>	<u>51,604</u>
Total assets	<u>\$ 2,205,142</u>	<u>\$ --</u>	<u>\$ --</u>	<u>\$ 2,205,142</u>
 <u>LIABILITIES AND NET ASSET</u>				
Liabilities:				
Accounts payable	\$ 219,993	\$ --	\$ --	\$ 219,993
Accrued salaries, wages and vacation payable	2,094	--	--	2,094
Other accrued liabilities	345,860	--	--	345,860
Due to Goodwill Industries of Orange County	<u>3,826</u>	<u>--</u>	<u>--</u>	<u>3,826</u>
Total liabilities	<u>571,773</u>	<u>--</u>	<u>--</u>	<u>571,773</u>
Net assets:				
Unrestricted net assets	<u>1,633,369</u>	<u>--</u>	<u>--</u>	<u>1,633,369</u>
Total net assets	<u>1,633,369</u>	<u>--</u>	<u>--</u>	<u>1,633,369</u>
Total liabilities and net assets	<u>\$ 2,205,142</u>	<u>\$ --</u>	<u>\$ --</u>	<u>\$ 2,205,142</u>

**GOODWILL INDUSTRIES OF ORANGE COUNTY,
CALIFORNIA AND AFFILIATE**

Supplementary Information

**Landmark Services, Inc.
Statement of Activities
Year Ended December 31, 2015**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenue:				
Contract services	\$ 3,998,462	\$ --	\$ --	\$ 3,998,462
Interest and other income	724	--	--	724
Total revenue	<u>3,999,186</u>	<u>--</u>	<u>--</u>	<u>3,999,186</u>
Expenses:				
Contract services	<u>3,353,462</u>	<u>--</u>	<u>--</u>	<u>3,353,462</u>
Total program services	<u>3,353,462</u>	<u>--</u>	<u>--</u>	<u>3,353,462</u>
Supporting services:				
General and administrative	<u>364,617</u>	<u>--</u>	<u>--</u>	<u>364,617</u>
Total supporting services	<u>364,617</u>	<u>--</u>	<u>--</u>	<u>364,617</u>
Total expenses	<u>3,718,079</u>	<u>--</u>	<u>--</u>	<u>3,718,079</u>
Change in net assets	281,107	--	--	281,107
Net assets at beginning of year	<u>1,352,262</u>	<u>--</u>	<u>--</u>	<u>1,352,262</u>
Net assets at end of year	<u>\$ 1,633,369</u>	<u>\$ --</u>	<u>\$ --</u>	<u>\$ 1,633,369</u>