Sonnenberg & Company CPA • AUDITS • TAXES • RESERVE STUDIES

Sonnenberg & Company, CPAs
A Professional Corporation

5190 Governor Drive, Suite 201, San Diego, California 92122

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Sonnenberg & Company 50 YEARS IN PRACTICE

Leonard C. Sonnenberg, CPA

WORDS ALIVE
Audited Financial Statements
Year Ended June 30, 2021

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
WORDS ALIVE

Report on the Financial Statements

We have audited the accompanying financial statements of Words Alive (a nonprofit organization), which comprise the statement of financial position as of June 30, 2021, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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 financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Member: The American Institute of Certified Public Accountants and California Society of Certified Public Accountants

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Words Alive as of June 30, 2021 and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited Words Alive's June 30, 2020 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated October 20, 2020. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2020, is consistent, in all material respects, with the audited financial statements from which it has been derived.

October 15, 2021

Sonnenberg & Company, CPAs

WORDS ALIVE

Statement of Financial Position

June 30, 2021

(With Comparative Information for June 30, 2020)

	2021	2020
ASSETS:		
Cash & cash equivalents	$ 374,001	$ 175,549
Accounts receivable	4,757	19,772
Contributions receivable	20,000	22,000
Prepaid expenses	6,714	4,866
Office equipment, net	13,120	18,040
Endowment at The San Diego Foundation	13,535	10,892
Total Assets	$ 432,127	$ 251,119
LIABILITIES:		
Accounts payable & accrued expenses	$ 18,659	$ 38,261
Payroll liabilities	27,569	22,632
Line of credit	-	20,107
Paycheck Protection Program forgivable loan	21,216	12,415
Capital lease obligation	13,120	18,040
Total Liabilities	80,564	111,455
NET ASSETS:		
Without donor restrictions	284,561	80,680
With donor restrictions	67,002	58,984
Total Net Assets	351,563	139,664
Total Liabilities & Net Assets	$ 432,127	$ 251,119

The accompanying notes are an integral part of the financial statements

WORDS ALIVE

Statement of Activities

For the Year Ended June 30, 2021

(With Summarized Comparative Information for the Year Ended June 30, 2020)

	Without Donor Restrictions	With Donor Restrictions	2021 Total	2020 Total
SUPPORT & REVENUE:				
Support:				
Contributions & grants	$ 632,058	$ 61,185	$ 693,243	$ 539,562
Payroll Protection Program grant	92,599		92,599	87,885
In-kind contributions-books & supplies	136,234		136,234	1,990
Special event:				
Gross special event revenue	64,890		64,890	105,743
Less: cost of direct benefits to donors	(5,992)		(5,992)	(64,272)
In-kind contributions			-	47,400
Less: use of in-kind contributions			-	(47,400)
Net special event revenue	58,898		58,898	41,471
Revenue:				
Program services	34,377		34,377	41,740
Investment income	1,867	2,643	4,510	10
Other income	625		625	849
Net assets released from restrictions	55,810	(55,810)	-	-
Total Support & Revenue	1,012,468	8,018	1,020,486	713,507
EXPENSES:				
Program services	568,586		568,586	438,870
Management & general	119,675		119,675	116,681
Fund raising	120,326		120,326	121,171
Total Expenses	808,587	-	808,587	676,722
CHANGE IN NET ASSETS	203,881	8,018	211,899	36,785
NET ASSETS, BEGINNING OF YEAR	80,680	58,984	139,664	102,879
NET ASSETS, END OF YEAR	$ 284,561	$ 67,002	$ 351,563	$ 139,664

The accompanying notes are an integral part of the financial statements

WORDS ALIVE

Statement of Functional Expenses

For the Year Ended June 30, 2021

(With Summarized Comparative Information for the Year Ended June 30, 2020)

	Program Services	Management & General	Fund Raising	2021 Total	2020 Total
EXPENSES:					
Personnel & related expenses					
Salaries	$ 278,216	$ 64,204	$ 85,605	$ 428,025	$ 428,133
Payroll taxes	15,979	3,687	4,917	24,583	34,086
Employee benefits	20,283	4,681	6,241	31,205	30,474
Total personnel & related expenses	314,478	72,572	96,763	483,813	492,693
Operating expenses					
Accounting & audit		13,875		13,875	14,075
Amortization	3,198	738	984	4,920	4,920
Bank & credit card fees		356	4,549	4,905	6,458
Book purchases	26,482			26,482	20,562
Computer, internet, & telephone	22,101	5,100	6,800	34,001	20,470
Contract services		3,900		3,900	206
Cost of direct benefits to donors			5,992	5,992	64,272
Dues & subscriptions		5,741		5,741	3,393
Employee and volunteer recognition		2,940		2,940	1,595
Insurance		4,522		4,522	4,817
Interest		3,426		3,426	9,975
In-kind contributions-books and supplies	136,234			136,234	1,860
Marketing/public relations		597	1,161	1,758	4,859
Office rent	11,778	2,718	3,624	18,120	18,120
Office expenses	7,182	1,657	2,210	11,049	5,895
Payroll processing	788	182	243	1,213	5,290
Printing		651	3,061	3,712	7,114
Professional development	980			980	770
Program expenses	12,328			12,328	8,376
Repairs & maintenance	3,030	699	932	4,662	653
Scholarships	28,810			28,810	41,309
Travel & transportation	1,196			1,196	3,314
Total operating expenses	254,108	47,103	29,556	330,766	248,302
Total expenses by function	568,586	119,675	126,318	814,579	740,994
Less expenses included with revenues on the statement of activities					
Cost of direct benefits to donors	-	-	(5,992)	(5,992)	(64,272)
Total expenses included in the expense section on the statement of activities	$ 568,586	$ 119,675	$ 120,326	$ 808,587	$ 676,722

The accompanying notes are an integral part of the financial statements

WORDS ALIVE
Statement of Cash Flows
For the Year Ended June 30, 2021
(With Comparative Information for the Year Ended June 30, 2020)

		2021		2020
CASH FLOWS FROM OPERATING ACTIVITIES:				
Change in net assets	$	211,899	$	36,785
Adjustments to reconcile change in net assets to net cash provided by operating activities:				
(Gain) loss on investments		(2,643)		18
Amortization		4,920		4,920
(Increase) Decrease:				
Accounts receivable		15,015		(19,772)
Contributions receivable		2,000		64,285
Prepaid expenses		(1,848)		2,910
Increase (Decrease) in:				
Accounts payable & accrued expenses		(19,602)		6,951
Payroll liabilities		4,937		3,431
Paycheck Protection Program forgivable loan		8,801		12,415
Net cash provided by operating activities		223,479		111,943
CASH FLOWS FROM FINANCING ACTIVITIES:				
Repayments on line of credit		(20,107)		(1,971)
Principal payments on capital lease obligations		(4,920)		(4,920)
Net cash used in financing activities		(25,027)		(6,891)
Net Increase in Cash & Cash Equivalents		198,452		105,052
Cash & Cash Equivalents at Beginning of Year		175,549		70,497
Cash & Cash Equivalents at End of Year	$	374,001	$	175,549
SUPPLEMENTAL CASH FLOW DISCLOSURE				
Cash paid for interest	$	3,426	$	9,975

The accompanying notes are an integral part of the financial statements

Note 1. **Organization**

Words Alive (the Organization) was founded in May 1999 as a California non-profit corporation. The mission of the Organization is to foster literacy. Through the Read Aloud, Teen Services, and Family Literacy programs, the Organization fosters a love of reading among over 4,000 children, teens, and families each month.

The Organization is supported by grants, contributions, and program service revenue.

Note 2. **Significant Accounting Policies**

Basis of Financial Presentation: The accompanying financial statements are prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

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

> *Net Assets Without Donor Restrictions* - Net assets available for use in general operations and not subject to donor (or certain grantor) restrictions.
>
> *Net Assets With Donor Restrictions* - Net assets subject to donor (or certain grantor) restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both.

Cash and Cash Equivalents: The Organization has defined cash and cash equivalents as cash in banks and highly liquid investments with an initial maturity of three months or less. Cash and highly liquid financial instruments restricted to endowments that are perpetual in nature, or other long-term purposes are excluded from this definition.

Accounts and contributions receivable: Accounts receivable consist of trade receivables related to the program services provided. Contributions receivable are unconditional promises to make future gifts. The Organization recognizes a receivable and contribution revenue at the time the promise is made by the donor if it is verifiable, measurable, and probable of collection. Conditional promises to give, which depend on the occurrence of specified future events, are recognized when the conditions are met.

All outstanding balances at year end are analyzed for collectability through a review of specific accounts that factor in historical trends. Based on that analysis, management has determined that no allowance for uncollectable accounts should be established as of June 30, 2021.

Note 2. Summary of Significant Accounting Policies, continued

Property and Equipment: Property and equipment additions over $2,000 is recorded at cost, or if donated, at fair value on the date of donation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. Costs of maintenance and repairs that do not improve or extend the useful lives of the respective assets are expensed.

Investments: Investment purchases are recorded at cost, or if donated, at fair value on the date of donation. Thereafter, investments are reported at their fair values in the statement of financial position. Net investment return/(loss) is reported in the statement of activities and consists of interest and dividend income, realized and unrealized capital gains and losses, less external and direct internal investment expenses.

Compensated Absences: Unpaid employee leave benefits are recognized as liabilities of the Organization. Accrued vacation liability is $27,569 as of June 30, 2021.

Revenue and Revenue Recognition: Program revenue is recognized when the programs are delivered. Contributions are recognized when the donor makes a promise to give to the Organization that is in substance, unconditional. Conditional promises to give, that is, those with a measurable performance or other barrier, and a right of return, are not recognized until the conditions on which they depend have been substantially met.

Donated Services and In-Kind Contributions: Volunteers contribute significant amounts of time to the Organization's program services, administration, and fundraising and development activities; however, the financial statements do not reflect the value of these contributed services because they do not meet recognition criteria prescribed by accounting principles generally accepted in the United States of America. Donated professional services are recorded at the respective fair values of the services received if the services (a) create or enhance non-financial assets, or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased by the Organization. Contributed goods are recorded at fair value on the date of donation.

Income Taxes: Words Alive is exempt from federal and state income taxes under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California State Revenue and Taxation Code. The Organization qualifies for the charitable contribution deduction under IRC Sections 170(b)(1)(A)(vi) and (viii). Words Alive is annually required to file a Return of Organization Exempt from Income Tax (Form 990) with the IRS. In addition, it is subject to income tax on net income that is derived from business activities that are unrelated to its exempt purposes. Management has determined that Words Alive is not subject to unrelated business income tax and have not filed an Exempt Organization Business Income Tax Return (Form 990-T) with the IRS for the year ended June 30, 2021. Management of Words Alive has evaluated its tax positions and related income tax contingencies. Management does not believe that any material uncertain tax positions exist.

Note 2. <u>Summary of Significant Accounting Policies, continued</u>

<u>Estimates:</u> The preparation of the 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 revenues and expenses during the reporting period. Actual results could differ from these estimates, and those differences could be material. Estimates made in the preparation of the financial statements include functional expense allocations.

<u>Functional Allocation of Expenses:</u> The costs of program and supporting services activities have been summarized on a functional basis in the statement of activities. The statement of functional expenses presents the natural classification detail of expenses by function. Accordingly, certain costs have been allocated among the programs and supporting services benefited. The expenses that are allocated include personnel and related expenses, amortization, computer, internet, and telephone, office rent, and office expenses are allocated on the basis of estimates of time and effort.

<u>Comparative Financial Information:</u> The accompanying financial statements include certain 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 audited financial statements for the year ended June 30, 2020, from which the summarized information was derived. Certain reclassifications of amounts previously reported have been made to the accompanying financial statements to maintain consistency between periods presented. The reclassifications had no impact on previously reported net assets.

<u>Accounting Pronouncements Adopted:</u> In August 2018, the FASB issued ASU 2018-13, Fair Value Measurement, Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement. This standard removed, modified, and added additional disclosure requirements on fair value measurements, specifically surrounding: (a) the amount of and reasons for transfers between Level 1 and Level 2 investments, (b) the policy for timing of these transfers, (c) the valuation process for Level 3 fair value measurements, and (d) the changes in unrealized gains and losses for the period including earnings on Level 3 fair value measurements held at the end of the reporting period. The Organization has adopted this ASU for the year ended June 30, 2021. The adoption had no material effect on the June 30, 2021 financial statements.

Note 3. <u>Concentrations of Credit Risk</u>

Financial instruments that potentially subject the Organization to credit risk consist of cash deposits and accounts and contributions receivable. Cash balances are insured by the Federal Deposit Insurance Corporation (FDIC) up to $250,000 per banking institution. As of June 30, 2021, there were combined cash deposits of $36,037 in excess of FDIC limits. The Organization has not experienced losses in any of these accounts.

Note 3. Concentrations of Credit Risk, continued

Credit risk associated with accounts and contributions receivable is considered to be limited due to high historical collection rates and because substantial portions of the outstanding amounts are due from governmental agencies, and donors supportive of the Organization's mission. The accounts and contribution receivable balances outstanding as of June 30, 2021 were collected in full after year end.

Note 4. Liquidity and Availability of Financial Assets

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

Cash	$ 374,001
Accounts receivable	4,757
Contributions receivable	20,000
	398,758
Funds subject to donor-imposed restrictions	(47,002)
Financial assets available to meet general expenditures within one year	$ 351,756

The Organization receives contributions with donor restrictions to be used in accordance with the associated purpose restrictions. The Organization must maintain sufficient resources to meet those responsibilities to its donors. Thus, financial assets may not be available for general expenditures within one year. The contributions receivable are subject to implied time restrictions but are expected to be collected within one year.

As part of the Organization's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. Cash in excess of daily requirements is held in money market savings account. The Organization also maintains a $100,000 line of credit available to meet cash flow needs.

Note 5. Fair Value Measurements and Disclosures

Fair value is defined as the price that would be received to sell an asset in the principal, or most advantageous market, for the asset in an orderly transaction between market participants on the measurement date. Fair value should be based on the assumptions market participants would use when pricing an asset. Accounting principles generally accepted in the United States of America establish a fair value hierarchy that prioritizes investments based on those assumptions. The fair value hierarchy gives the highest priority to quoted prices in active markets (observable inputs) and the lowest priority to an entity's assumptions (unobservable inputs). The Organization groups assets at fair value in three levels, based on the markets in which the assets and liabilities are traded, and the reliability of the assumptions used to determine fair value.

Note 5. Fair Value Measurements and Disclosures, continued

These levels are:

Level 1: Quoted prices in active markets for identical securities.
Level 2: Other significant observable inputs (including quoted prices for similar securities, interest rates, prepayments, spreads, credit risk, etc.).
Level 3: Significant unobservable inputs (including the Organization's own assumptions in determining the fair value of investments).

The following table represents the Organization's Level 3 financial instruments, the valuation techniques used to measure the fair value of those financial instruments, and the significant unobservable inputs and the range of values for those inputs as of June 30, 2021:

Instrument	Fair Value	Principal valuation technique	Unobservable inputs	Significant input values	Weighted average
Beneficial interest in endowment at The San Diego Foundation	$ 13,535	Valuation of underlying assets as provided by issuer	Base price	N/A	N/A

Note 6. Endowment at The San Diego Foundation

The Organization is the beneficiary of an endowment. The assets, in the possession of the San Diego Foundation, are to be held indefinitely. The Organization has legally enforceable rights and claims to such assets, including the sole right to income therefrom.

The Organization's Board of Directors 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 date of the donor-restricted endowment funds unless there are explicit donor stipulations to the contrary. As of June 30, 2021, there were no such donor stipulations. As a result of this interpretation, the Organization retains in perpetuity (a) the original value of initial and subsequent gift donated to the Endowment and (b) any accumulations to the endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added. Donor-restricted amounts not retained in perpetuity are subject to appropriation for expenditure by the Board of Directors in a manner consistent with the standard of prudence prescribed by UPMIFA.

The assets are kept in a balance pool that is intended to result in a consistent rate of return. Investment assets are managed to not expose the fund to unacceptable level of risk. Distributable earnings are added to the fund or may be distributed to the Organization to be used for operations.

Note 6. Endowment at The San Diego Foundation, continued

Changes in endowment net assets for the year ended June 30, 2021 are as follows:

Balance- July 1, 2020	$	10,892
Investment earnings, net of fees		2,643
Balance- June 30, 2021	$	13,535

Note 7. Line of Credit

On March 22, 2021, the Organization renewed a line of credit agreement with First Citizens Bank & Trust Company to replace the expired agreement. The credit limit is $100,000. The interest rate is the prime rate as published in The Wall Street Journal plus 0.5%. Accrued interest and principal, if any, are due at maturity (April 1, 2022). The line of credit is secured by all accounts, general intangibles, inventory, equipment, and other goods and requires the Organization to comply with certain financial and non-financial covenants. There was no outstanding balance as of June 30, 2021.

Note 8. Payroll Protection Program

On April 22, 2020, The Organization received loan proceeds in the amount of $100,300 under a first draw Paycheck Protection Program (PPP). The PPP was established as part of the Coronavirus Aid, Relief, and Economic Security (CARES) Act and is administered by the U.S. Small Business Administration (SBA). Under the terms of CARES Act, PPP loan recipients can apply for and be granted forgiveness for all or portion of the loans granted under PPP.

The Organization has accounted for the PPP loan as a conditional contribution. The contribution is considered to be conditioned upon certain performance requirements and the incurrence of qualifying expenses. The proceeds are recognized as revenue when the Organization has incurred expenses in compliance with the loan provisions. The funds were used by the Organization to pay eligible payroll costs and the Organization otherwise complied with the terms of the PPP Loan.

The Organization has recorded grant revenue in the amount of $87,885 based on qualifying expenses for the year ended June 30, 2020. The balance of the loan in the amount of $12,415 was recorded as a liability as of June 30, 2020 and was used for eligible payroll costs in July 2020. Corresponding contribution revenue was recorded during the year ended June 30, 2021. On December 2, 2020, the Organization was notified that the eligibility criteria have been met and the loan has been forgiven in full.

On February 3, 2021, the Organization obtained a second draw loan from the SBA in the amount of $101,400. The loan terms are similar to the first draw loan described above. Grant revenue in the amount of $80,184 based on qualifying expenses was recorded for the year ended June 30, 2021. The balance of the loan in the amount of $21,216 was recorded as a liability as of June 30, 2021 and was used for qualifying expenses in July 2021. On October 1, 2021 the Organization was notified that the eligibility criteria have been met and the loan has been forgiven in full.

Note 9. **Capital Lease**

The Organization leases a copier under a 60-month capital lease agreement starting March 2019. The copier is recorded at the fair value in the amount of $24,600 and amortized over the term of the lease. Amortization expense is $4,920 for the year ended June 30, 2020. The amount includes finance cost that has not been considered in these financial statements. Minimum future lease payments under the capital lease as of June 30, 2021 are as follows:

June 30,	
2022	$ 4,920
2023	4,920
2024	3,280
	$ 13,120

Note 10. **Net Assets With Donor Restrictions**

Net assets with donor restrictions as of June 30, 2021 are as follows:

	July 1, 2020	Additions	Released	June 30, 2021
Subject to expenditure for specified purpose:				
Scholarships	$ 26,092	$ 41,185	$ (33,810)	$ 33,467
Subject to the passage of time:				
Contributions receivable that are not restricted by donors, but which are unavailable for expenditure until due	22,000	20,000	(22,000)	20,000
Endowment at The San Diego Foundation for general use	10,892	2,643		13,535
Total	$ 58,984	$ 63,828	$ (55,810)	$ 67,002

Note 11. **In-Kind Donations**

For the year ended June 30, 2021, the fair value of donated books used in the Organization's programs was $132,995. Additionally, donations of various supplies with the estimated fair market value of $3,239 were received during the year to be used for the programs. These amounts have been reported as both in-kind contribution revenue and expenses in the statements of activities and functional expenses.

Note 12. **Office Facilities Lease**

The Organization's lease agreement for the office facilities expired in March 2017. Beginning April 2017, the facilities are leased on a month-to-month basis. The monthly rent was $1,510 for the year ended June 30, 2021. Total expense for the year ended June 30, 2021 was $18,120.

Note 13. **Employee Benefits**

The Organization maintains a 403(b) plan for its employees. Employees may defer part of their compensation each year up to a maximum amount allowed by the Internal Revenue Code. The Organization also maintains a "Cafeteria Plan" for the benefit of its employees. Employees can pay certain qualified expenses on a pre-tax basis. No employer contributions were made to the plans for the year ended June 30, 2021.

Note 14. **Subsequent Events**

The Organization's management has evaluated subsequent events through October 15, 2021, the date the financial statements were available to be issued.

The spread of Coronavirus (COVID-19) in the first months of 2020 has caused a substantial impact on the U.S. economy. There is significant uncertainty around the effects and duration of business interruption related to COVID-19. The extent of the impact on the Organization's operations, donors, employees, and vendors will depend on certain developments, which cannot be determined at this time.