

Special Kids, Inc.

Financial Statements

December 31, 2005 and 2004

With Independent Accountant's Report Thereon

H A Beasley & Company
Certified Public Accountants
Murfreesboro, Tennessee

Member:
American Institute of CPAs
Tennessee Society of CPAs
Institute of Management Accountants

HAB
H A BEASLEY & COMPANY
Certified Public Accountants

237 W. Northfield Blvd.
First Place Bldg., Suite 102
Murfreesboro, TN 37129
Phone: (615) 895-5675
Fax: (615) 895-5660
E-Mail: HA@HABeasley.com
www.HABeasley.com

INDEPENDENT ACCOUNTANT'S REPORT

Board of Directors
Special Kids, Inc.

We have audited the accompanying statement of financial position of Special Kids, Inc. (a non-profit corporation) as of December 31, 2005 and 2004 and the related statements of activities and change in net assets and cash flows for the periods then ended. These financial statements are the responsibility of Special Kids, Inc. management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards of 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of Special Kids, Inc. as of December 31, 2005 and 2004, and the results of operations and its cash flows for the periods then ended in conformity with generally accepted accounting principles of the United States of America.



Murfreesboro, TN
June 14, 2006

SPECIAL KIDS, INC.
STATEMENTS OF FINANCIAL POSITION
As of December 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
<u>ASSETS</u>		
Current Assets		
Cash and Cash Equivalents	\$ 255,787	\$ 326,033
Investments (Note C)	1,500	1,500
Accounts Receivable	102,180	76,838
Prepaid Expenses	12,141	-
	<hr/>	<hr/>
Total Current Assets	371,608	404,371
Land, Buildings and Equipment, net (Note D)	286,490	279,628
	<hr/>	<hr/>
TOTAL ASSETS	<u>\$ 658,098</u>	<u>\$ 683,999</u>
 <u>LIABILITIES</u>		
Accounts Payable and Accrued Expenses	\$ 7,965	\$ 14,075
	<hr/>	<hr/>
Total Current Liabilities	7,965	14,075
 <u>NET ASSETS</u>		
Unrestricted Net Assets (Note F)	650,133	-
	<hr/>	<hr/>
TOTAL LIABILITIES & NET ASSETS	<u>\$ 658,098</u>	<u>\$ 683,999</u>

See accompanying notes and independent accountant's report.

SPECIAL KIDS, INC.
STATEMENTS OF ACTIVITIES AND
CHANGE IN NET ASSETS
For the Years Ended December 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
<u>REVENUES, GAINS & RECLASSIFICATIONS:</u>		
Patient Fees	\$ 649,280	\$ 740,163
Private Gifts & Grants	224,997	219,730
Fundraising	215,478	184,781
Dividend and Interest Income	5,492	1,067
	<hr/>	<hr/>
Total Revenue, Gains & Reclassifications	1,095,247	1,145,741
	<hr/>	<hr/>
<u>EXPENSES & LOSSES:</u>		
Program Services:		
Rehabilitation	597,017	531,616
Nursing	344,697	266,118
Administration	118,149	93,474
Fundraising	55,175	36,155
	<hr/>	<hr/>
Total Expenses	1,115,038	927,363
	<hr/>	<hr/>
Change in Net Assets	(19,791)	218,378
Net Assets at Beginning of Year	669,924	451,546
	<hr/>	<hr/>
NET ASSETS AT END OF YEAR	\$ 650,133	\$ 669,924
	<hr/>	<hr/>

See accompanying notes and independent accountant's report.

SPECIAL KIDS, INC.
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
<u>OPERATING ACTIVITIES</u>		
Change in Net Assets	\$ (19,791)	\$ 218,378
Adjustments to Reconcile to Cash From Operations:		
Depreciation	16,654	17,704
Amortization	84	1,322
Non-cash donations	-	(1,500)
(Increase)/Decrease in Accounts Receivable	(25,342)	40,986
(Increase)/Decrease in Prepaid Expenses	(12,141)	
Increase/(Decrease) in Accounts Payable and Accrued Expenses	(6,110)	12,716
	<u>(46,646)</u>	<u>289,606</u>
Net Cash Provided/(Used) by Operations		
<u>INVESTING ACTIVITIES</u>		
Acquisition of Equipment	<u>(23,600)</u>	<u>(26,229)</u>
Net Cash (Used) in Investing Activities	<u>(23,600)</u>	<u>(26,229)</u>
<u>FINANCING ACTIVITIES</u>		
Reduction of Short-term Debt	<u>-</u>	<u>(19,708)</u>
Net Cash Provided/(Used) in Financing Activities	<u>-</u>	<u>(19,708)</u>
Net Increase/(Decrease) in Cash	(70,246)	243,669
Beginning Cash and Cash Equivalents	<u>326,033</u>	<u>82,364</u>
Ending Cash and Cash Equivalents	<u>\$ 255,787</u>	<u>\$ 326,033</u>

See accompanying notes and independent accountant's report.

SPECIAL KIDS, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2005 and 2004

NOTE A--NATURE OF ACTIVITIES

Special Kids, Inc. is located in Murfreesboro, Tennessee. Special Kids, Inc. is a tax-exempt organization under 501(c)(3) of the Internal Revenue Code. Special Kids, Inc. is dedicated to providing quality and affordable rehabilitation and nursing services in a loving, Christian environment with the support and guidance of the physician. The goal is that no family would be denied due to lack of funding, or access to services. They believe the family unit is important and by offering quality-coordinated services, Special Kids, Inc. strives to minimize the pressures of parenting a child with special needs.

NOTE B--SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accrual Basis

The financial statements of the organization have been prepared on the accrual basis.

Basis of Presentation

The organization has adopted the Statement of Financial Accounting Standard (SFAS) No. 117, *Financial Statements of Not-for-Profit Organizations*. Under SFAS 117, net assets, revenues, gains and losses are classified based on the existence or absence of donor-imposed restrictions as follows:

-Unrestricted net assets- Net assets that are not subject to donor-imposed stipulations.

-Temporarily restricted net assets- Net assets subject to donor-imposed stipulations that can be fulfilled by actions of the organization pursuant to those stipulations or that expire by the passage of time.

-Permanently restricted net assets- Net assets subject to donor-imposed stipulations that they be maintained permanently by the organization. Generally, the donors of such assets permit the organization to use all or part of the income earned on the assets.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets (i.e. the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassification between the applicable classes of net assets.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles includes the use of estimates that affect the financial statements. Accordingly, actual results could differ from these estimates.

SPECIAL KIDS, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2005 and 2004

Cash and Cash Equivalents

For purposes of the statement of cash flows, cash equivalents include time deposits and certificates of deposit except investments purchased with endowment assets or deposits with trustees that are classified as long-term investments.

Compensated Absences

Employees of the organization are entitled to paid vacation, paid sick days and personal days off, depending on job classification, length of service and other factors. It is impractical to estimate the amount of compensation for future absences, and accordingly, no liability has been recorded in the accompanying financial statements. The organization's policy to recognize the cost of compensated absences when actually paid to its employees would not materially change the financial statements if an estimate were accrued.

Land, Buildings and Equipment

Land, buildings and equipment are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the assets (5 to 40 years). Expenditures for equipment costing over \$250 are capitalized.

Contributions of long-lived assets or contributions restricted for acquisition of long-lived assets are reported as increases in temporarily restricted net assets. When restrictions are considered met, an appropriate amount is reclassified to unrestricted net assets. The useful lives of the long-lived assets are calculated based on the organization's depreciation policy.

Contributions

The Organization accounts for contributions in accordance with the recommendation of the FASB in SFAS No. 116, "Accounting for Contributions Received and Contributions Made." Contributions, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. Amortization or discounts is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for uncollectible contribution receivables is provided based upon management's judgement, including such factors as prior collection history, type of contribution, and nature of fund-raising activity.

Restricted contributions whose restrictions are met or accrued in the period the contributions are received are reported as unrestricted contributions.

Income Taxes

The organization is a not-for-profit organization that is exempt from federal income tax under Internal

SPECIAL KIDS, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2005 and 2004

Revenue Code Section 501(c)(3) whereby only unrelated business income, as defined in Section 512(a)(1) of the Code, is subject to federal income tax.

NOTE C--INVESTMENTS

Investments as of December 31, 2005 includes a diamond given by a donor that is being held for sale.

NOTE D--LAND BUILDINGS AND EQUIPMENT

Land, buildings and equipment are composed of the following:

	<u>2005</u>	<u>2004</u>
Land	\$ 35,404	\$ 35,404
Buildings and improvements	253,225	253,225
Furniture and equipment	43,133	59,158
Grant equipment	37,026	13,194
Grant software	10,476	10,450
Software	<u>4,988</u>	<u>4,645</u>
	384,252	376,076
Less accumulated depreciation and amortization	<u>(97,762)</u>	<u>(96,448)</u>
Total	<u>\$286,490</u>	<u>\$ 279,628</u>

Fixed assets with a total cost of \$16,025 and book value of \$600 were donated to various organizations, resulting in a reduction of accumulated depreciation in the amount of \$15,425 for the year ended December 31, 2005.

NOTE E--PROGRAM SERVICE AND FUNDRAISING EXPENSES

During the current fiscal year, volunteers have performed a significant number of hours of service in accomplishing the organization's purposes. These hours were donated and if they were recorded in the records based on a reasonable hourly wage would result in a dramatic increase in private donations as well as a multi-fold increase in program service expenses. The organization did not incur any significant third-party fundraising expenses during the fiscal year.

NOTE F--RESTRICTIONS ON NET ASSETS

All net assets are unrestricted at December 31, 2005 and 2004. On November 30, 2004 the Finance Committee of the board of Directors designated \$114,973 of unrestricted net assets for the building fund.

SPECIAL KIDS, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2005 and 2004

NOTE G-CONCENTRATION OF RISK

The organization is highly dependent on insurance company reimbursement of fees for rehabilitation and nursing services and on charitable contributions. If the insurance funding for rehabilitation and nursing services decreased extensively, the organization would experience serious difficulty in continuing operations. Also, because the organization is a TennCare provider there is a risk related to continuance of the TennCare program and any state or federal program that may replace the TennCare program. The dollar impact of this risk has not been quantified. Management indicated that it is expected that if the TennCare program is discontinued, another provider arrangement would be made or the services would revert to the federal Medicaid program.

Charitable contributions are solicited across the middle Tennessee regions using a variety of methods. While the organization enjoys a broad base of donors, a decrease in contributions would present an economic challenge for the organization.

Member:
American Institute of CPAs
Tennessee Society of CPAs
Institute of Management Accountants

HAB
H A BEASLEY & COMPANY
Certified Public Accountants

237 W. Northfield Blvd.
First Place Bldg., Suite 102
Murfreesboro, TN 37129
Phone: (615) 895-5675
Fax: (615) 895-5660
E-Mail: HA@HABeasley.com
www.HABeasley.com

June 14, 2006

Board of Directors and Senior Management
Special Kids, Inc.
Murfreesboro, Tennessee

In planning and performing our audit of the financial statements of Special Kids, Inc., for the year ended December 31, 2005, we considered the corporation's internal control in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements, not to provide assurance on internal control.

During our audit, we became aware of several matters that are opportunities for strengthening internal control and operation efficiency. This letter does not affect our report dated June 14, 2006, on the financial statements of Special Kids, Inc.

We will review the status of these comments during our next audit engagement. We have already discussed many of these comments and suggestions with various personnel and we will be pleased to discuss these comments in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations. Our comments are summarized as follows:

Accounting Manual

The Organization does not have a formal accounting manual documenting the procedures for fiscal operations. A written accounting manual is necessary to ensure that transactions are treated in a standardized manner and that proper internal controls exist in the accounting system. Should employees have a question as to the proper handling of a transaction in accordance with management's authorization, such information is not available in writing. Also, if there were unexpected turnover in accounting, then the transition would not be nearly as overwhelming if procedures were in writing. We recommend that operating guidelines for fiscal activities be prepared including a description of each fiscal procedure, such as invoice paying, maintenance of accounts receivable and accounts payable subsidiary records, and payroll procedures. In addition, an expense allocation methodology should also be incorporated into the accounting manual.

Protection of Assets

We recommend tracking furniture and equipment by conducting physical inventories, accounting for serial numbers and using property ownership labels.

Accounts Receivable

Due to the large charge-off amounts resulting from third party payments (insurance payments), management must closely examine open EOB's, amounts charged off as not collectible and delinquent patient receivables. Success of operations is dependent on collecting the maximum amount on a timely basis. This is especially true of insurance company billings. Service invoices are submitted electronically to some insurance companies. Consideration should be given to continue increasing the use of electronic submissions with other insurance companies in order to speed up the process and in order to correct errors on a timely basis.

Dependency on Donations

The Organization depends significantly on donations for the funding of ongoing operations. Should economic or social events transpire to bring hardship upon the Organization's support group, Special Kids, Inc. may find it difficult to continue operations. One way to reduce the exposure to this risk is through the development of substantial endowment funds. We recommend that the organization establish and implement long-range plans for increasing the amount of income available to support Special Kids' continued operations.

We also recommend that the organization consider finding new sources of revenue such as selling advertising or making affinity items available for sale. The revenue generated from ad sales, affinity item sales, or other auxiliary sources will help to offset the cost of the publications.

Grant Purchases


When items are bought with money from Grants or Contributions, the items should either be expensed or set up as a fixed asset according to the same criteria as other purchases. Only those items costing over \$250 should be capitalized as equipment in accordance with the organization's capitalization policy.

Contract Labor

While contractor labor expenses decreased in 2005, management should continue to work to ensure that all guidelines are adhered to relating to contract labor. It was noted in the organization's records that contract labor personnel have signed contracts on file similar to employment contracts, which refer to them as employees. Also contract labor personnel have completed employee timesheets for payment. If deemed appropriate, contract labor personnel should sign contracts that are specifically designed for contract labor not for employees. Also, they should not complete employee timesheets but should prepare and present invoices for payment of services. Failure to follow the recommended guidelines relating to contract labor could present a problem if an audit by the Department of Labor is conducted.

We wish to thank the administration and staff for their support and assistance during our audit.

This report is intended solely for the information and use of the Board of Directors, management and others within Special Kids and is not intended to be and should not be used by anyone other than these specified parties.



H A Beasley & Company
Memphis, Tennessee