

WAVES, INC.

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JOHN R. POOLE, CPA
CERTIFIED PUBLIC ACCOUNTANT

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Independent Auditor's Report

To the Board of Directors of
WAVES, Inc.
Franklin, Tennessee

I have audited the accompanying statement of financial position of WAVES, Inc. (a nonprofit organization) as of June 30, 2005, and the related statements of activities, functional expenses, and cash flows for the year then ended. These financial statements are the responsibility of the Organization's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted the audit in accordance with generally accepted auditing standards in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that I 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. I believe that my audit provides a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of WAVES, Inc., as of June 30, 2005, and the changes in its net assets and its cash flows for the year then ended in conformity with generally accepted principles.

In accordance with Government Auditing Standards, I have also issued my report dated December 10, 2005, on my consideration of WAVES, Inc.'s internal control over financial reporting and tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of the testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in conjunction with this report in considering the results of the audit.

My audit was performed for the purpose of forming an opinion on the basic financial statements of WAVES, Inc. The accompanying schedule of State Financial Assistance is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in my opinion, is fairly stated in all material respects in relation to the financial statements.

John R. Poole, CPA

December 10, 2005

WAVES, INC.

Statement of Financial Position

June 30, 2005

Assets

Current assets:

Cash	\$	24,260
Accounts receivable		568,800
Unconditional promises receivable		85,254
Prepaid assets		4,808
Total current assets		<u>683,122</u>

Property and equipment at cost:

Land and building		699,882
Vehicles		247,607
Furniture and equipment		110,904
Less: accumulated depreciation		<u>(422,061)</u>
Net property and equipment		<u>636,332</u>

Other assets

6,321

Total assets

\$ 1,325,775

Liabilities and Net Assets

Current liabilities:

Accounts payable	\$	31,186
Accrued expenses		142,206
Deferred revenue		168,270
Current portion of long-term debt		25,112

Total current liabilities

366,774

Long-term debt

439,455

Net assets:

Temporarily restricted		85,254
Unrestricted		<u>434,292</u>
Total net assets		<u>519,546</u>

Total liabilities and net assets

\$ 1,325,775

The accompanying notes are an integral part of these statements.

WAVES, INC.

Statement of Activities

For the year ended June 30, 2005

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Revenues			
Public support:			
Tennessee Department of:			
Mental Health and Mental Retardation	\$ 1,849,619	-	1,849,619
TEIS	24,101	-	24,101
Human Services	99,406	-	99,406
Medicaid waiver	797,780	-	797,780
United Way	-	85,254	85,254
Grants	10,476	-	10,476
Private pay and room and board	140,679	-	140,679
City and County	72,635	-	72,635
In-kind	18,960	-	18,960
Recycle fees	17,545	-	17,545
Contributions	17,458	-	17,458
Interest	124	-	124
Miscellaneous	8,691	-	8,691
Net assets released from restrictions:			
United Way funding for the year 2004-2005	85,254	(85,254)	-
Total public support and revenues	<u>3,142,728</u>	<u>-</u>	<u>3,142,728</u>
Expenses:			
Residential services	1,657,596	-	1,657,596
Day services	618,928	-	618,928
Employment services	241,770	-	241,770
Child services	197,411	-	197,411
Management and General	345,472	-	345,472
Fundraising	4,406	-	4,406
Total expenses	<u>3,065,583</u>	<u>-</u>	<u>3,065,583</u>
Increase (decrease) in net assets	<u>77,145</u>	<u>-</u>	<u>77,145</u>
Beginning of year net assets	357,147	85,254	442,401
End of year net assets	<u>\$ 434,292</u>	<u>85,254</u>	<u>519,546</u>

WAVES, INC.

Statement of Functional Expenses

For the year ended June 30, 2005

	Program Services					Supporting Services			Total Expenses
	Residential Services	Day Services	Employment Services	Child	Total	Management and General	Fundraising	Total	
Salaries	\$ 1,163,208	344,107	154,124	133,953	1,795,392	217,998	1,485	219,483	2,014,875
Employee benefits	139,972	59,806	22,503	13,508	235,789	39,402	179	39,581	275,370
Payroll taxes	85,599	24,580	10,706	10,062	130,947	16,062	-	16,062	147,009
Travel	5,215	616	4,784	10,898	21,513	1,629	32	1,661	23,174
Printing	2,321	3,256	1,336	413	7,326	5,287	-	5,287	12,613
Utilities	15,587	11,173	-	-	26,760	-	-	-	26,760
Communications	14,175	9,524	4,180	2,034	29,913	7,781	-	7,781	37,694
Maintenance and repairs	15,673	15,292	425	2,306	33,696	1,460	-	1,460	35,156
Professional services	12,818	23,968	1,130	4,287	42,203	13,235	1,560	14,795	56,998
Supplies	14,165	8,651	4,842	2,077	29,735	8,209	1,150	9,359	39,094
Food	27,314	1,235	59	443	29,051	1,138	-	1,138	30,189
Rent	12,397	37,094	1,385	11,845	62,721	17,114	-	17,114	79,835
Insurance	7,221	1,718	211	549	9,699	3,159	-	3,159	12,858
Vehicle expense	60,360	50,659	16,210	-	127,229	2,905	-	2,905	130,134
Client benefits	28,995	8,131	6,061	3,403	46,590	421	-	421	47,011
Training	3,438	1,255	2,097	475	7,265	1,163	-	1,163	8,428
Miscellaneous	2,097	331	186	275	2,889	1,835	-	1,835	4,724
Interest	19,247	44	514	-	19,805	182	-	182	19,987
Depreciation	27,794	17,488	11,017	883	57,182	6,492	-	6,492	63,674
Total Expenses	\$ 1,657,596	618,928	241,770	197,411	2,715,705	345,472	4,406	349,878	3,065,583

WAVES, INC.

Statement of Cash Flows

For the year ended June 30, 2005

Cash flows from operating activities:	
Support and revenue received	\$ 2,991,754
Cash paid for:	
Salaries and related expenses	(2,437,254)
Program and support services	(521,563)
Net cash provided by operating activities	<u>32,937</u>
Cash flows used by financing activities:	
Proceeds from long-term debt	123,750
Payment of long-term debt	(18,031)
Net cash used by financing activities	<u>105,719</u>
Cash flows used by investing activities:	
Acquisition of fixed assets	(159,986)
Net cash used by investing activities	<u>(159,986)</u>
Net increase in cash	(21,330)
Cash and cash equivalents at beginning of year	45,590
Cash and cash equivalents at end of year	\$ <u><u>24,260</u></u>

Reconciliation of Increase in Net Assets to Net Cash Provided by Operating Activities

Increase (decrease) in net assets	\$ 77,145
Adjustments to reconcile decrease in net assets to net cash provided by operating activities:	
Depreciation	63,674
Changes in assets (increase) decrease:	
Accounts receivable	(150,974)
Prepaid assets	2,030
Other assets	(500)
Changes in liabilities increase (decrease)	
Accounts payable	10,365
Accrued expenses	32,594
Deferred revenue	(1,397)
Net cash provided by operating activities	\$ <u><u>32,937</u></u>

WAVES, INC.

Notes to the Financial Statements June 30, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities

WAVES, Inc. is a non-profit organization in Williamson County, Tennessee. The Organization's mission is to enable persons with disabilities to achieve their highest level of functioning and progress toward their full potential.

Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles and recommendations of the American Institute of Certified Public Accountants in its industry audit and accounting guide, "Not-for-Profit Organizations."

Basis of Presentation

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board in its Statement of Financial Standards (SAS) No. 117, *Financial Statements of Not-for-Profit Organizations*. Under SAS No. 117, the Organization is required to report information regarding its financial position and activities according to the three classes of net assets. In addition, the Organization is required to present a statement of cash flows. As permitted by the statement, the Organization has discontinued its use of fund accounting.

Contributions

In accordance with SAS 116, *Accounting for Contributions Received and Contributions Made*, contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence or nature of any donor restrictions.

Promises to Give

Contributions are recognized when the donor makes a promise to give to the Organization that is, in substance, unconditional. Contributions that are restricted by the donor are reported as increases in unrestricted net assets if the restrictions expire in the fiscal year in which the contributions are recognized. All other donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets.

WAVES, INC.

Notes to the Financial Statements June 30, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

Donated Services

WAVES, Inc. receives many hours of donated time from various citizens. It is impractical to estimate a value for these services, as such no such value has been placed on these services in the WAVES, Inc.'s financial statements.

Donated Rent

WAVES, Inc. receives office space rent free. These amounts are recorded at their fair value as in-kind revenue and as rental expense in the financial statements.

Donor -Imposed Restrictions

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are restricted for future periods or donor-restricted for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset classes. When a donor- stipulated time restriction is accomplished, then the restricted net assets are reclassified to unrestricted net assets. If a restriction is fulfilled in the same time period in which the contribution is received, the contribution is reported as unrestricted.

Depreciation

Depreciation is provided for over the estimated useful lives of the assets. Assets are depreciated using the straight-line method of depreciation.

Promises to Give/Pledges

Unconditional promises to give that are expected to be collected within one year are recorded at their net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of estimated future cash flows. Conditional promises to give are not included as support until such time as the conditions are substantially met.

Functional Allocation of Expenses

The costs of providing the WAVES, Inc's various programs and supporting services have been summarized on a functional basis in the statement of activities. Accordingly, certain costs may have been allocated among the programs and supporting services benefited.

Income Taxes

The Organization is a not-for-profit organization that is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code.

WAVES, INC.

Notes to the Financial Statements June 30, 2005

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Organization considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Deferred Revenue

Deferred revenue is recorded when a potential revenue does not meet the 'measurable' and 'available' criteria for recognition in the current period. In subsequent periods, when both of these criteria are met, revenue is recognized.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Economic Dependence

Approximately 25% of WAVES, Inc.'s revenues for the year ended June 30, 2005, was from the Medicaid program and approximately 63% of WAVES, Inc.'s revenues for the year ended June 30, 2005, was from the contracts from various State of Tennessee departments. The Medicaid Program and the State may, at its discretion, request reimbursement of expenses or return of funds, or both as a result of non-compliance by the WAVES, Inc. with the terms of the programs.

2. FIXED ASSETS

A summary of fixed asset activity is noted below:

	Balance 6/30/04	Addition	Retirement	Balance 6/30/05
Land and buildings	\$ 543,910	155,972	-	699,882
Vehicles	245,457	2,150	-	247,607
Furniture and equipment	109,040	1,864	-	110,904
Total	898,407	159,986	-	1,058,393
Less: Accumulated depreciation	(353,799)			(422,061)
Net assets	\$ 544,608			636,332

Depreciation expense for the year ended June 30, 2005 was \$ 63,674.

WAVES, INC.

Notes to the Financial Statements June 30, 2005

3. LONG -TERM DEBT

Long-term debt at June 30, 2005 consists of the following:

6.375% mortgage note payable in monthly payments of \$691 to July 2017, collateralized by Land and Buildings of the Organization.	\$ 69,782
6.375% mortgage note payable in monthly payments of \$691 to July 2017, collateralized by Land and Buildings of the Organization.	69,782
5.750% mortgage note payable in monthly payments of \$1,406 to April 2024, collateralized by Land and Buildings of the Organization.	186,703
6.700% mortgage note payable in monthly payments to May 2020, collateralized by Land and Buildings of the Organization.	123,750
5.00% note payable in monthly payments of \$348 to April 2009, collateralized by a vehicle of the Organization.	<u>14,550</u>
Total long-term debt	464,567
Less amount classified as current	<u>25,112</u>
Total long-term debt excluding current portion	<u>\$ 439,455</u>

Principal requirements of long-term debt in the next five years consists of:

2006	\$ 25,112
2007	26,780
2008	28,140
2009	30,765
2010	<u>23,112</u>
Total	133,909
Thereafter	<u>330,658</u>
Total debt	<u>464,567</u>

WAVES, INC.

Notes to the Financial Statements June 30, 2005

4. LINE OF CREDIT

WAVES, Inc. renewed the line of credit of \$80,000, with an interest rate of 1% above prime rate as established by the bank with interest to be paid monthly. The note matures on September 1, 2006. There was no outstanding balance on the line of credit as of June 30, 2005.

5. PENSION PLAN

WAVES, Inc. adopted in 1997 a 403(b) thrift plan covering substantially all of its full time employees. Employees as of July 1, 1997, were covered immediately. Employees hired after that date were covered after one year of service. The employer contributions to the plan were 3.0% of each eligible employee's annual gross pay and will make a matching contribution equal to 50% of the first 4% contributed by an employee. Each employee's contribution is 100% vested immediately. All employer contributions are earned over seven years of service. Employer contributions for the year ended June 30, 2005, were \$43,586.

6. COMMITMENTS

WAVES, Inc. has leases for certain of its facilities. All leases expire during the next twelve months with the latest expiration date being June 2006. These leases are renewable annually. Rent expense for the year ended June 30, 2005 was \$79,835.

7. STATE CONTRACTS AND GRANTS:

Amounts received from the State of Tennessee are subject to audit and adjustment by the State of Tennessee. Any disallowed claims including amounts already collected, could become a liability of the Organization.

SUPPLEMENTAL INFORMATION

Financial schedules are used to demonstrate finance related legal and contractual compliance, provide details of data summarized in the financial statements and present other information deemed useful.

WAVES, INC.

Schedule of State Financial Assistance

For the Year ended June 30, 2005

CFDA#	Program Name	Grant #	Grantor Agency	Balance 6/30/2004	Cash Receipts	Cash Expenditures	Balance 6/30/2005
N/A	Mental Health and Mental Retardation	N/A	State of Tennessee Finance and Administration Services	371,034	1,687,483	1,849,619	533,170
N/A	TEIS	N/A	State of Tennessee Department of Education	9,837	33,938	24,101	-
N/A	Human Services	N/A	State of Tennessee Department of Human Services	-	99,406	99,406	-
N/A	Equipment Grant	N/A	State of Tennessee Department of Human Services	-	10,476	10,476	-
Total				380,871	1,831,303	1,983,602	533,170

The accompanying notes are an integral part of these statements.

**COMPLIANCE AND
INTERNAL CONTROL**

JOHN R. POOLE, CPA
CERTIFIED PUBLIC ACCOUNTANT

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

To the Board of Directors of
WAVES, Inc.
Franklin, Tennessee

I have audited the financial statements of WAVES, Inc. as of and for the year ended June 30, 2005, and have issued a report thereon dated December 10, 2005. I conducted the audit in accordance with generally accepted auditing standards in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether WAVES, Inc.'s financial statements are free of material misstatement, I performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of the financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of the audit and, accordingly, I do not express such an opinion. The results of the tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing the audit, I considered WAVES, Inc.'s internal control over financial reporting in order to determine the auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control over financial reporting. My consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by errors or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. I noted no matters involving the internal control over financial reporting and its operation that I consider to be material weaknesses.

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This report is intended for the information of the State Comptroller's Office, management and federal awarding agencies. However, this report is a matter of public record and its distribution is not limited.

John R. Poole, CPA

December 10, 2005