

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit
of the County of San Mateo)

Independent Auditor's Reports,
Management's Discussion and Analysis
and Financial Statements

Years Ended June 30, 2012 and 2011



Certified Public Accountants.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

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First 5 San Mateo County Commission
San Mateo, California

Independent Auditor's Report

We have audited the financial statements of the governmental activities and the major fund of First 5 San Mateo County (First 5), a discretely presented component unit of the County of San Mateo, California (County), as of and for the year ended June 30, 2012. These financial statements are the responsibility of the First 5's management. Our responsibility is to express opinions on these financial statements based on our audit. The financial statements of the First 5 as of June 30, 2011 were audited by other auditors whose report dated October 11, 2011 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted 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 we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the First 5's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 opinions.

In our opinion, the 2012 financial statements referred to previously present fairly, in all material respects, the respective financial position of the governmental activities and the major fund of the First 5 as of June 30, 2012, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 17, 2012 on our consideration of the First 5's internal control over financial reporting and on our 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 our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the Schedule of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Macias Gini & Connell LLP

Walnut Creek, California
October 17, 2012

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Management's Discussion and Analysis (Unaudited)
Year Ended June 30, 2012



In November 1998, voters passed a statewide ballot initiative, Proposition 10, to fund programs that promote the physical, cognitive and emotional development of children ages 0-5. Proposition 10 funds are generated by a tax on tobacco products and are intended to facilitate the creation and implementation of an integrated and collaborative system of care for young children in the areas of health, family support and early learning. All revenue generated is collected in the California Children and Families (First 5 California) Trust Fund Account and allocations are made to each of the 58 counties in the State based on the number of births recorded in the relevant county in proportion to the number of births recorded in California. Each county must establish a local First 5 Commission to oversee the use of these funds in accordance with their strategic plan.

This Management's Discussion and Analysis is intended to serve as a narrative overview and analysis of the financial activities of First 5 San Mateo County (First 5) for the years ended June 30, 2012 and 2011. The information presented should be read in conjunction with the information furnished in the financial statements and notes to the financial statements.

Financial Highlights

During the fiscal year ended June 30, 2012, First 5 contributed over \$7.4 million in a wide variety of local programs and services for young children and their families. During this same period, the passage of Assembly Bill 99 (AB99) required First 5 Commissions, statewide, to remit 50% of their FY2010 available fund balances to the State of California's Children and Families Health and Services fund. The passage of AB99 resulted in First 5 setting aside \$15.3 million for remittance to the State.

In November 2011, AB99 was overruled. As a result, the \$15.3 million previously set aside for remittance to the State was restored to First 5's fund balance and First 5's long-term financial plan was revised. The new financial plan preserves specialized programs and services an additional year, through June 30, 2017, with a total investment of approximately \$50 million. By extending the long-term financial plan an additional year, First 5 was able to utilize the amount originally set aside for AB99 and one more year of new revenue.

Government-wide Financial Analysis

- The assets of First 5 exceeded its liabilities as of June 30, 2012 by \$24,580,005 (*net assets*). Of this amount, \$1,043 was restricted for specific purpose. The remaining balance may be used to meet First 5's ongoing obligations to grantees and creditors.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)
Management's Discussion and Analysis (Unaudited)
Year Ended June 30, 2012

Fund Financial Analysis

- Total fund balance as of June 30, 2012 was \$24,496,677. Of this amount, \$1,043 was restricted for the New Parent Kit Program; \$14,048,096 was committed for current executed grants and contracts and for contract amendments not yet executed (obligated); and the remaining \$10,447,538 was set aside for future programs, projects, and activities. All funding awards were in accordance with First 5's Strategic Plan and Long-Term Financial Plan.
- Contributions to local projects decreased by \$1,463,193 or 16.4% from the previous fiscal year. The reduced funding was a result of strategic decisions made in anticipation of AB99.

Overview of the Financial Statements

This discussion and analysis serves as an introduction to First 5 basic financial statements which include three components:

1. *Government-wide* financial statements
2. *Fund* financial statements
3. *Notes* to the basic financial statements

Government-wide financial statements provide readers with a broad overview of First 5 finances, in a manner similar to a private-sector business.

The *statement of net assets* presents information on all of First 5 assets and liabilities, with the difference between the two reported as *net assets*.

The *statement of activities* presents information showing how First 5 net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus revenues and expenses are reported in this statement for some items that will only result in cash flows in a future fiscal period (e.g. earned but unused vacation leave).

The government-wide financial statements can be found on pages 8 and 9 of this report.

Fund financial statements are groupings of related accounts used to maintain control over resources that have been segregated for specific activities or objectives. Fund financial statements report essentially the same functions as those reported in the government-wide financial statements; however they focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year.

The fund financial statements can be found on pages 10 and 11 of this report.

Notes to the basic financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

The notes can be found on pages 12 through 25 of this report.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)
Management's Discussion and Analysis (Unaudited)
Year Ended June 30, 2012

Government-wide Financial Analysis

As of June 30, 2012, First 5 assets exceeded liabilities by \$24,580,005.

Net Assets

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Total Assets	\$ 26,632,688	\$ 30,013,083 *	\$ 39,471,990 *
Total Liabilities	2,052,683	18,663,395	8,381,013
Net Assets:			
Restricted	1,043	91,385	197,067
Unrestricted	<u>24,578,962</u>	<u>11,258,303 *</u>	<u>30,893,910 *</u>
Total	<u>\$ 24,580,005</u>	<u>\$ 11,349,688</u>	<u>\$ 31,090,977</u>

* Notes receivable was restated and decreased by \$100,000 as of July 1, 2010 and \$120,000 as of July 1, 2009.

Fiscal Year 2012 Compared to Fiscal Year 2011

- At the end of fiscal year 2012, total assets decreased by \$3,380,395 (11.3%) when compared to fiscal year 2011. The decrease was primarily due to the decrease in cash and cash equivalents for grant and vendor payments made during the year.
- Total liabilities decreased by \$16,610,712 (89.0%). The decrease was mainly due to the overturning of State Assembly Bill (AB99) in which First 5 was not obligated make the one-time payment to the State of California.
- Net assets increased by \$13,230,317 (116.6%). First 5's net assets are divided into *restricted* and *unrestricted* portions. Restricted funding is money received for specific programs or initiatives that must be used exclusively for the purposes designated. Unrestricted funding is money received that is set aside for programs, projects, and activities to be conducted in the future according to a documented plan, budget or financial forecast formally approved by First 5.

Fiscal Year 2011 Compared to Fiscal Year 2010

- Total assets decreased by \$9,458,907 (24.0%). The decrease was primarily due to decrease in security lending collateral and cash and cash equivalents.
- Total liabilities increased by \$10,282,382 (122.7%). The increase was mainly due to a one-time payment due to the State of California per AB99 in FY 2011 offset by a decrease in securities lending collateral due.
- Net assets decreased by \$19,741,289 (63.5%). First 5's net assets are divided into restricted and unrestricted portions. Restricted funding is money received for specific programs or initiatives that must be used exclusively for the purpose designated. Unrestricted funding is money received that is set aside for programs, projects, and activities to be conducted in the future according to a documented plan, budget or financial forecast formally approved by First 5.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Management's Discussion and Analysis (Unaudited)
Year Ended June 30, 2012

Changes in Net Assets

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Program Revenues	\$ 6,779,641	\$ 6,640,391	\$ 7,624,122
General Revenues	479,385	340,297	583,779
Program Expenses *	<u>(9,368,594)</u>	<u>(11,382,092)</u>	<u>(9,423,833)</u>
Deficiency before extraordinary item	(2,109,568)	(4,401,404)	(1,215,932)
Extraordinary Item	<u>15,339,885</u>	<u>(15,339,885)</u>	<u>-</u>
Change in Net Assets	13,230,317	(19,741,289)	(1,215,932)
Net Assets - beginning *	<u>11,349,688</u>	<u>31,090,977</u>	<u>32,306,909</u>
Net Assets - ending	<u>\$ 24,580,005</u>	<u>\$ 11,349,688</u>	<u>\$ 31,090,977</u>

* Program expenses were restated and decreased by \$20,000 for FY 2010 and FY 2011 and net assets were restated by \$100,000 in 2011 and \$120,000 in 2010.

Fiscal Year 2012 Compared to Fiscal Year 2011

- Program revenues increased by \$139,250 (2.1%) and general revenues increased by \$139,088 (40.9%). The increase in program revenue was primarily due to increases in Proposition 10 allocations. The increase in general revenue was primarily due to First 5 receiving its share of investment recoveries from the County's investments in Lehman Brothers Holding Inc. as part of its bankruptcy plan.
- Program expenses decreased by \$2,013,498 (17.7%). The majority of the decrease was due to a reduction in contributions to local projects.
- The extraordinary loss in fiscal year 2011 was reversed and reported as an extraordinary gain in fiscal year 2012 due to the California Supreme Court overturning AB99 in November 2011. As a result, First 5 was no longer obligated to make the one-time payment to the State of California.

Fiscal Year 2011 Compared to Fiscal Year 2010

- Program revenues decreased by \$983,731 (12.9%) and general revenues decreased by \$243,482 (41.7%). The decreases are primarily due to decreases in Proposition 10 allocations, funding from First 5 California for special projects, private grants, and investment earnings.
- Program expenses increased by \$1,958,259 (20.8%) due to increases in contributions to local projects.
- The extraordinary loss of \$15,339,885 in fiscal year 2011 related to an estimated one-time financial obligation to the State of California per AB99.

Fund Financial Analysis

First 5 uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. As of June 30, 2012, First 5 reported a fund balance of \$24,496,677, an increase of \$13,230,864 (17.4%) from the prior year. The increase was mainly due to the California Supreme Court overturning AB99 and the return of \$15,339,885 to First 5's fund balance. Of the total, \$14.0 million of the fund balance was committed to grantees and contractors through contractual obligations in accordance with First 5's strategic plan and long-term financial plan. These plans are reviewed and approved by First 5 on an annual basis.

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Year Ended June 30, 2012

As of June 30, 2011, fund balance totaled \$11,265,813. The decrease from the prior fiscal year is a result of the extraordinary loss of \$15.3 million resulting from the passage of AB99 during the fiscal year.

Budgetary Highlights

First 5 operating budget for FY2011-12 totaled \$10.8 million. The budget closeout revealed an estimated savings of \$1.5 million, which is the excess of approved budgeted expenditures compared to actual expenditures. A key factor accounting for the \$1.9 million positive budget variance in contributions to local projects which was attributed to under spending in grantee's contracts for System of Care strategies in Cycle One and Cycle two funding.

The budgetary comparison information can be found on page 28 of this report.

Requests for Information

This financial report is designed to provide a general overview of First 5 finances. Questions concerning any of the information provided in this report, or requests for additional financial information should be addressed to Debby Armstrong, Executive Director, First 5 San Mateo County, 1700 S. El Camino Real, Suite 405, San Mateo, CA 94402-3050.

First 5 San Mateo County
(A Discretely Presented Component Unit of the County of San Mateo)
Statements of Net Assets
June 30, 2012 and 2011

	Governmental Activities	
	2012	2011
Assets		
Cash and cash equivalents	\$ 25,213,824	\$ 28,563,339
Receivables, net:		
Intergovernmental	1,197,295	1,198,860
Interest	58,073	89,852
Net OPEB Asset	163,496	161,032
Total Assets	<u>26,632,688</u>	<u>30,013,083</u>
Liabilities		
Accounts payable	1,947,331	3,181,357
Salaries and benefits payable	25,184	64,996
Due to State of California per AB99	-	15,339,885
Compensated absences:		
Payable in less than one year	69,671	77,157
Payable in more than one year	10,497	-
Total Liabilities	<u>2,052,683</u>	<u>18,663,395</u>
Net Assets		
Restricted for:		
Lucile Packard Grant	1,043	91,385
Unrestricted	24,578,962	11,258,303
Total Net Assets	<u>\$ 24,580,005</u>	<u>\$ 11,349,688</u>

The accompanying notes are an integral part of these financial statements.

First 5 San Mateo County
(A Discretely Presented Component Unit of the County of San Mateo)
Statements of Activities
Years Ended June 30, 2012 and 2011

	Governmental Activities	
	2012	2011
Expenses		
Salaries and wages	\$ 788,769	\$ 812,329
Employee benefits	496,196	475,444
General office supplies	21,079	42,848
Professional services	600,206	875,553
Other administrative expenses	28,376	33,583
Contributions to local projects	7,433,968	8,897,161
Other expenses	-	245,174
Total program expenses	<u>9,368,594</u>	<u>11,382,092</u>
Program Revenues		
Operating grants and contributions:		
Tobacco tax	6,779,641	6,629,891
Private grants	-	10,500
Total program revenues	<u>6,779,641</u>	<u>6,640,391</u>
Net program revenues (expenses)	<u>(2,588,953)</u>	<u>(4,741,701)</u>
General Revenues		
Investment earnings	312,128	304,082
Investment loss recovery	123,283	-
Other revenue	43,974	36,215
Total general revenues	<u>479,385</u>	<u>340,297</u>
Extraordinary Item		
Payment due to State of California per AB99	-	(15,339,885)
Restitution of payment to State of California per AB99	<u>15,339,885</u>	<u>-</u>
Changes in net assets	13,230,317	(19,741,289)
Net Assets - Beginning (as restated)	<u>11,349,688</u>	<u>31,090,977</u>
Net Assets - Ending	<u>\$ 24,580,005</u>	<u>\$ 11,349,688</u>

The accompanying notes are an integral part of these financial statements.

First 5 San Mateo County
(A Discretely Presented Component Unit of the County of San Mateo)
Balance Sheets
June 30, 2012 and 2011

	2012	2011
Assets		
Cash and cash equivalents	\$ 25,213,824	\$ 28,563,339
Receivables, net:		
Intergovernmental	1,197,295	1,198,860
Interest	58,073	89,852
Total assets	\$ 26,469,192	\$ 29,852,051
 Liabilities and Fund Balances		
Liabilities		
Accounts payable	\$ 1,947,331	\$ 3,181,357
Salaries and benefits payable	25,184	64,996
Due to State of California per AB99	-	15,339,885
Total liabilities	1,972,515	18,586,238
 Fund balance		
Restricted	1,043	91,385
Committed	14,048,096	10,057,410
Assigned	10,447,538	1,117,018
Total fund balances	24,496,677	11,265,813
Total liabilities and fund balances	\$ 26,469,192	\$ 29,852,051
 Reconciliation of Fund Balance Sheet to the Statement of Net Assets:		
Total fund balance	\$ 24,496,677	\$ 11,265,813
Amounts reported in the Statement of Net Assets are different because:		
Long-term assets are not available to pay for current period expenditures, and long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental fund:		
Net OPEB asset	163,496	161,032
Compensated absences	(80,168)	(77,157)
Net assets	\$ 24,580,005	\$ 11,349,688

The accompanying notes are an integral part of these financial statements.

First 5 San Mateo County
(A Discretely Presented Component Unit of the County of San Mateo)
Statements of Revenues, Expenditures, and Changes in Fund Balance
Years Ended June 30, 2012 and 2011

	2012	2011
Revenues		
Tobacco tax	\$ 6,779,641	\$ 6,629,891
Investment earnings	312,128	304,082
Investment loss recovery	123,283	-
Private grants	-	10,500
Other revenue	2,577	-
Total revenues	7,217,629	6,944,473
Expenditures		
Salaries and benefits	1,243,021	1,246,466
Services and supplies	649,661	951,984
Contributions to local projects	7,433,968	8,897,161
Other	-	245,174
Total expenditures	9,326,650	11,340,785
Deficiency of revenues over expenditures	(2,109,021)	(4,396,312)
Extraordinary Item		
Payment due to State of California per AB99	-	(15,339,885)
Restitution of payment to State of California per AB99	15,339,885	-
Net change in fund balance	13,230,864	(19,736,197)
Fund balance - beginning (as restated)	11,265,813	31,002,010
Fund balance - ending	\$ 24,496,677	\$ 11,265,813
Reconciliation of the Change in Fund Balance to the Change in Net Assets in the Statement of Activities:		
Net change in fund balance	\$ 13,230,864	\$ (19,736,197)
Amounts reported in the Statement of Activities are different because:		
Change in long-term portion of assets and liabilities do not provide or require the use of current financial resources and, therefore, are not reported in the governmental fund:		
Change in net OPEB asset	2,464	3,510
Change in compensated absences	(3,011)	(8,602)
Change in net assets	\$ 13,230,317	\$ (19,741,289)

The accompanying notes are an integral part of these financial statements.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Reporting entity

Under the authority of the California Children and Families First Act of 1998 and sections 130100, et seq. of the Health and Safety Code, the Children & Families First Commission of San Mateo County (Commission) was established in March 1999. The Commission set up the Children and Families First Trust Fund with the County of San Mateo (County) in March 1999 to account for the receipts and disbursements of California Children and Families Trust Fund allocations to the Commission. On January 7, 2003, the County Board of Supervisors passed an ordinance changing the Commission's name to First 5 San Mateo County (First 5).

The financial transactions of First 5 are accounted for in a special revenue fund, as monies received by it are legally restricted or committed to specific use. Moneys allocated and appropriated to First 5 can be expended only for purposes authorized by the California Children and Families First Act of 1998 (Proposition 10) and in accordance with the County Strategic Plan approved by the First 5 Commission and approved through the County budget process.

The County Board of Supervisors appoints all the members of First 5 Commission. The financial activities of First 5 are included in the basic financial statements of the County as a discretely presented component unit.

b) Measurement focus, basis of accounting, and financial statement presentation

The government-wide financial statements (i.e., the Statement of Net Assets and the Statement of Activities) are reported using the *economic resources measurement focus* and the *accrual* basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Contributions to local grantee organizations are recognized as expenditures when criteria for grant payments are met by the grantee organizations. When both restricted and unrestricted net assets are available, restricted resources are generally depleted first before the unrestricted resources are used.

The Statements of Net Assets present First 5's financial position in a net assets approach. The Statements of Activities report the change in net assets in a net program cost format to demonstrate the degree to which the expenses of First 5 is offset by its program revenues – tobacco tax and private grants.

Governmental fund financial statements, presented after the government-wide financial statements, are reported using the *current financial resources measurement focus* and the *modified accrual* basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. Revenues from reimbursement type programs are considered to be *available* when they are collectible within six months of the end of the current fiscal period in order to properly match revenues with related expenditures. Expenditures are recognized in the accounting period in which the liability is incurred, if measurable.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

c) Use of Estimates

The preparation of basic financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results based on subsequent events could differ from those estimates.

d) Budgetary Information

First 5 adopts an annual budget, which can be amended by First 5 throughout the year. The basis used to prepare the budget is the same as the basis used to reflect actual revenues and expenditures, except that liability for compensated absences, postemployment benefits other than pensions and unrealized gains and losses are not included in the budget.

e) Other Postemployment Benefits (OPEB)

First 5 employees participate in the defined benefit post employment healthcare plan administered by the County. The County is not obligated to pay for unused sick leave if employees terminate employment prior to retirement, except for those individuals who are laid off. Upon retirement, unused sick leave can be converted to postemployment healthcare benefits. The amount and duration of the County-paid benefits vary, depending on the bargaining units to which the employee belongs. The public safety employees are eligible to retire after attaining age 50 with at least ten years of service or at any age with 20 years of services. Others must retire from the County on or after attaining age 50 with at least ten years of service.

f) Extraordinary Items

Significant transactions that are unusual in nature and infrequent in occurrence are reported as extraordinary items. In the year ended June 30, 2011, First 5 reported \$15.3 million of an extraordinary loss as a result of State Assembly Bill 99 (AB99). AB99 was subsequently overturned, and thus resulted in an extraordinary gain in the year ended June 30, 2012.

g) Restatement of Notes Receivable

In April 2003, First 5, jointly with the County of San Mateo, provided a zero-interest loan to Bayshore Child Care Services for the Our Second Home project. First 5's share of the loan was \$200,000 and was to be forgiven one-tenth of each full year of project operation commencing with fiscal year 2006-07. Accounting principles generally accepted in the United States of America require that receivables to be stated at their net realizable values. Since the loan's promissory note indicates the loan is to be forgiven over a 10-year period, management evaluated its collectability and determined that its net realizable value should be \$0. As a result, net assets and fund balance decreased by \$120,000 at June 30, 2010, and expenditures for services and supplies decreased by \$20,000.

FIRST 5 SAN MATEO COUNTY
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Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

2. CASH AND CASH EQUIVALENTS

a) Cash and Cash Equivalents

Cash and cash equivalents is pooled with other funds in the San Mateo County Investment Pool (County Pool). The County Pool includes both voluntary and involuntary participants from external public entities. First 5 is a voluntary participant in the County Pool. Interest earned is received quarterly. Cash and cash equivalents in the County Pool are reported at fair value. The change in fair value for the year is recorded as unrealized gain or loss and reported as part of investment earnings. Fair value is based on information provided by the County Treasurer.

The County Pool is a governmental investment pool managed and directed by the elected San Mateo County Treasurer (Treasurer). The County Pool is not registered with the Securities and Exchange Commission as an investment company. California Government Code and the County's Investment Policy govern the County Pool activities. The objectives of this policy, in order of priority, are: safety, liquidity, yield, and public trust. The pool attempts to match maturities with planned outlays and maximize the return on investment over various market cycles. Yield is considered only after safety and credit quality have been met, consistent with limiting risk and prudent investment principles. The County Board reviews the County's Investment Policy annually, and all amendments to the policy must be approved by the County Board.

The fair value of cash and cash equivalents of First 5's investment in the County Pool is reported in the accompanying financial statements at amounts based upon First 5's pro-rated share of the fair value provided by the Treasurer for the County Pool portfolio. First 5's cash and cash equivalents in the pool totaled \$25,213,824 and \$28,563,339 as of June 30, 2012 and 2011, respectively. The contractual withdrawal values (book values) were \$25,107,520 and \$28,500,198 as of June 30, 2012 and 2011, respectively.

b) Authorized Investments of the County Pool

The County's Investment Policy and the California Government Code allow the County Pool to invest in the following, provided the credit ratings of the issuers are acceptable to the County Pool. The following also identifies certain requirements of the County Pool and California Government Code that address interest rate risk, credit risk, and concentrations of credit risk.

Authorized Investment Type	Maximum Maturity	Minimum Credit Quality	Maximum % Allowed in Portfolio	Maximum % Investment in One Issuer
U.S. Treasury Obligations	7 years	-	100	100
Obligations of U.S. agencies or government sponsored enterprises	7 years	AA or A-1	100	40
Callable obligations of U.S. agencies	7 years	AA	100	25
Bankers acceptances	180 days	A1/P-1/F1	15	5
Collateralized time deposits within the State of California	1 year	A1/P-1/F1	15	5

FIRST 5 SAN MATEO COUNTY
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Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

2. CASH AND CASH EQUIVALENTS (continued)

Authorized Investment Type	Maximum Maturity	Minimum Credit Quality	Maximum % Allowed in Portfolio	Maximum % Investment in One Issuer
Negotiable certificates of deposit	5 years	A1/P-1/F1	30	5
Commercial paper	270 days or less	A1/P-1	40	5
Repurchase agreements secured by U.S. Treasury or agency obligations	92 days	AAA	100	See limitation for U.S. Treasury and agency obligation
Corporate bonds, medium term notes and covered bonds	5 years	AA/A	30	5
Local Agency Investment Fund (LAIF)	-	-	-	Up to the current state limit
Shares of beneficial interest	-	A1/P1	10	5
Mortgage backed securities, collateralized mortgage obligations	5 years	A	20	5
Asset backed securities	5 years	AAA	20	

At June 30, 2012, the County Pool was invested in the following securities:

Investment Type	Interest Rate	Maturities	Weighted Average Maturity (Years)	Standard & Poor's Ratings
U.S. government securities	0.625% - 2.125%	1/31/13 - 9/30/18	3.63	AA
U.S. government agency securities	0.061% - 2.240%	7/5/12 - 6/29/17	1.48	AA
U.S. government agency securities - floating rate	0.270%	9/20/2012	0.22	AA
Corporate bonds	0.550% - 3.950%	8/1/12 - 5/15/17	2.69	AAA, AA, A
Floating rate securities	0.450% - 1.250%	11/24/12 - 6/1/15	1.55	AA, A
LAIF	0.360%	8/1/2012	0.08	Unrated
Commercial papers	0.150% - 0.360%	7/13/12 - 7/27/12	0.05	A1
Negotiable certificate of deposits	0.666% - 2.250%	7/17/12 - 3/15/13	0.41	A
Repurchase agreements	0.100%-0.130%	7/2/2012	0.50	AA

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

2. CASH AND CASH EQUIVALENTS (continued)

At June 30, 2011, the County Pool was invested in the following securities:

<u>Investment Type</u>	<u>Interest Rate</u>	<u>Maturities</u>	<u>Weighted Average Maturity (Years)</u>	<u>Standard & Poor's Rating</u>
U.S. government securities	0.045% - 2.125%	7/14/11 - 6/30/16	1.98	AAA
U.S. government agency securities	0.020% - 2.815%	7/15/11 - 11/23/15	1.11	AAA
U.S. government agency securities - floating rate	0.096% - 0.202%	8/1/11 - 5/1/12	0.39	AAA
Corporate bonds	0.875% - 5.900%	8/1/12 - 5/19/16	3.00	AAA, AA
Floating rate securities	0.301% - 1.875%	1/24/12 - 5/30/14	1.99	AAA, AA, A
Commercial papers	0.090% - 0.180%	7/14/11 - 8/26/11	0.08	AA
Negotiable certificate of deposits	0.476% - 0.926%	1/19/12 - 1/18/13	1.05	AA, A
Repurchase agreements	0.000%	7/1/11	*	AAA

* Weighted average maturity is less than 0.01 year.

c) County Pool: Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. State law and the County's investment policy limit the County's investments in commercial paper to the rating of A1 or better by Standard & Poor's or P1 or better by Moody's Investors Service; and corporate bonds to the rating of A or higher by both Standard & Poor's and Moody's Investors Service. No limits are placed on U.S. treasuries securities. The County's Investment Policy limits investments in U.S. government agency securities to AA or better by at least two of the three nationally recognized rating services. The County Pool was unrated as of June 30, 2012 and rated AAf/S1 by Standard & Poor's as of June 30, 2011.

d) County Pool: Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the County Pool's investment in a single issuer of securities. For each authorized investment type, state law restricts the maximum percentage allowed in the portfolio and per issuer. The County Pool has more than five percent of its total investment with the following issuers as of June 30, 2012: 12% in Federal Home Loan Bank, 12% in Federal Home Loan Mortgage Corporation and 18% in Federal National Mortgage Association. As of June 30, 2011, the investment pool has more than 5% of its total investments with the following issuers: 13% in Federal Home Loan Bank, 12% in Federal Home Loan Mortgage Corporation, 10% in Federal National Mortgage Association.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

2. CASH AND CASH EQUIVALENTS (continued)

e) County Pool: Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The longer the duration of the portfolio is, the greater its price sensitivity to changes in interest rates. The County manages its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio to three years or less in accordance with its investment policy. As of June 30, 2012, the County Pool had a weighted average maturity of 1.6 years and its investment in floating rate securities was \$161 million which are tied to the three-month London Interbank Offered Rate (LIBOR) index. As of June 30, 2011, the County Pool had a weighted average maturity of 1.5 years and its investment in floating rate securities was \$213 million which were tied to the three-month London Interbank Offered Rate (LIBOR) index.

f) County Pool: Foreign Currency Risk

Foreign currency risk is the risk that changes in the exchange rates will adversely affect the fair values of an investment or deposit. The County's Investment Policy does not include specific provisions to address foreign currency risk because the County does not invest in foreign securities.

3. INTERGOVERNMENTAL RECEIVABLE

Intergovernmental receivable represents Proposition 10 and Surplus Money Investment Fund (SMIF) revenues that were received after the fiscal year.

	2012	2011
Proposition 10 allocation for:		
May	\$ 532,938	\$ 584,851
June	661,642	610,483
	1,194,580	1,195,334
Surplus Money Investment Fund (SMIF)	2,715	3,526
Total	\$1,197,295	\$1,198,860

4. ACCOUNTS PAYABLE

Accounts payable comprises of funding due to grantees and amounts due to vendors for services and supplies at fiscal year-end:

	2012	2011
Funding due to grantees	\$1,874,702	\$2,809,421
Services and supplies	72,629	371,936
Total	\$1,947,331	\$3,181,357

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

5. DUE TO STATE OF CALIFORNIA PER ASSEMBLY BILL 99

In March 2011, the Governor approved State Assembly Bill 99 (AB99) which would sweep a total of \$1 billion from First 5 County Commissions and First 5 California's fund balances. As of June 30, 2011, First 5 recorded \$15.3 million as a liability as a result of AB99.

In April 2011, several county commissions began litigation against the State of California. The case was heard in California Superior Court and the judge ruled in favor of the county commissions in November 2011. The parties then had a period of time to appeal the decision. In March 2012, the Governor indicated they were not appealing the Judge's decision and AB99 was overruled. As a result, First 5 Commission's fund balances were restored.

The \$15.3 million liability recorded at June 30, 2011, which was reversed, resulted in an extraordinary gain of the same amount for the year ended June 30, 2012.

6. COMPENSATED ABSENCES

First 5 accrues for compensated absences in the government-wide financial statements to pay its employees for unused vacation, compensatory time, and holiday. The accrual for compensated absences includes First 5's share of social security and Medicare contributions payable on behalf of the employees. Unused vacation, compensatory, and holiday time are cashed out upon separation.

The changes in the compensated absences balance for the fiscal years ended June 30, 2012 and 2011 were as follows:

	2012	2011
Balance - beginning of year	\$ 77,157	\$ 68,555
Additions	70,066	8,602
Retirements	(67,055)	-
Balance - end of year	\$ 80,168	\$ 77,157
Due within a year	\$ 69,671	\$ 77,157

7. EMPLOYEES' RETIREMENT PLAN

a) Plan Description

General. First 5 employees are participants in the San Mateo County Employees' Retirement Association (SamCERA), a cost-sharing multiple-employer, defined benefit pension plan established to provide pension benefits for substantially all permanent employees of the County and two special districts. The Board of Retirement of SamCERA governs the County's pension fund. SamCERA issues a publicly available financial report that can be obtained by writing to the San Mateo County Employees' Retirement Association, 100 Marine Parkway, Suite 125, Redwood Shores, California 94065.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

7. EMPLOYEES' RETIREMENT PLAN (continued)

Benefit Provisions. SamCERA provides service retirement, disability, and death benefits to plan members and beneficiaries based on periodic actuarial valuations. SamCERA has four plans that cover members classified as general, safety or probation, and provides annual cost-of-living adjustments upon retirement to members of Plans One, Two, and Four. The benefits of Plan Three are reduced by a portion of Social Security benefits received by the member. The 1937 Act vests the County Board of Supervisors with the authority to initiate benefits, and Government Code Section 31592.2 empowers the Board of Retirement to provide certain ad hoc benefits when the reserve of excess earnings exceeds 1% of assets.

b) Funding Policy

The 1937 Act established the basic obligations for employers and members to make contributions to the pension trust fund. The employer and member contribution rates are based on recommendations made by an independent actuary and adopted by the Board of Retirement. Participating employers are required by statutes to contribute the amounts necessary to fund the estimated benefits accruing to SamCERA members not otherwise funded by member contributions or expected investment earnings. Contribution rates are actuarially determined using the entry age normal method and consist of an amount for normal cost, the estimated amount necessary to finance benefits earned by members during the year, and an amount required to amortize the unfunded actuarial accrued liability (UAAL).

c) Annual Pension Cost

First 5's three-year trend information for required contributions is as follows:

<u>Fiscal Year Ended</u>	<u>Annual Required Contributions (ARC)</u>	<u>Percentage of ARC Contributed</u>
6/30/2010	\$139,966	100%
6/30/2011	\$225,859	100%
6/30/2012	\$224,758	100%

8. OTHER POSTEMPLOYMENT BENEFITS

First 5 employees are also participants of the postemployment benefit (OPEB) sick leave conversion Retiree Health Plan (a single-employer defined benefit plan) administered by the County. The County's Retiree Health Plan is being managed through the California Employers' Retiree Benefits Trust (CERBT), an irrevocable trust fund that allows public employers to prefund the future cost of their retiree health insurance benefits and other postemployment benefits for their covered employees or retirees.

The CERBT's administrator, the California Public Employees' Retirement System (CalPERS), issues a publicly available financial report consisting of financial statements and required supplementary information for CERBT in aggregate. The report may be obtained by writing to CalPERS, Lincoln Plaza North, 400 Q Street, Sacramento, CA 95811.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

8. OTHER POSTEMPLOYMENT BENEFITS (continued)

Contribution requirements for the members and the County are established and may be amended through negotiations between the County and the bargaining units. First 5 participates in the County's Retiree Health Plan on a cost-sharing basis, and contributed \$41,397 and \$36,215 for the fiscal years ended June 30, 2012 and 2011, respectively. The following table shows the components of annual OPEB costs, the amounts contributed to the plan, and changes in First 5's net OPEB assets:

	2012	2011
Annual required contribution	\$ 41,397	\$ 36,215
Annual OPEB cost	\$ 38,933	\$ 32,705
Contribution made	(41,397)	(36,215)
Increase in net OPEB obligation (asset)	(2,464)	(3,510)
Net OPEB obligation (asset) - beginning of year	(161,032)	(157,522)
Net OPEB obligation (asset) - end of year	\$ (163,496)	\$ (161,032)

First 5's annual OPEB cost (AOC), the percentage of AOC contributed to the plan, and the net OPEB asset for the past three years are as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of AOC Contributed	Net OPEB Asset
6/30/2010	\$26,488	112%	\$157,522
6/30/2011	\$32,705	111%	\$161,032
6/30/2012	\$38,933	106%	\$163,496

Additional information relating to the County's Retiree Health Plan and required OPEB disclosures can be obtained from the County's publicly available Comprehensive Annual Financial Report that may be obtained by writing to County of San Mateo Controller's Office, 555 County Center, 4th Floor, Redwood City, California 94063.

9. FUND BALANCE

As prescribed by GASB Statement No. 54, governmental funds report fund balance in classifications based primarily on the extent to which First 5 is bound to honor constraints on the specific purposes for which amounts in the funds can be spent. First 5's fund balances were comprised of the following:

- (a) *Restricted Fund Balance* – includes amounts that can be spent only for specific purposes stipulated by external resources providers, constitutionally or through enabling legislation. Restrictions may effectively be changed or lifted only with the consent of resource provider.
- (b) *Committed Fund Balance* – includes amounts that can only be used for specific purposes determined by a formal action of First 5's highest level decision-making authority, the First 5 Commission. Commitments may be changed or lifted only by First 5 taking the same formal action that imposed the constraint originally.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

9. FUND BALANCE (continued)

(c) *Assigned Fund Balance* – comprises amounts intended to be used by First 5 for specific purposes that are neither restricted nor committed. *Intent* is expressed by (1) First 5’s Commission or (2) a body (for example: a budget or finance committee) or official to which First 5’s Commission has delegated the authority to assign amounts to be used for specific purposes.

In circumstances when an expenditure is made for a purpose for which amounts are available in multiple fund balance classifications, fund balance is depleted in the order of restricted, committed and assigned.

At fiscal year-end, fund balance reported on the *Statements of Revenues, Expenditures and Changes in Fund Balance* includes:

	2012	2011
Restricted		
David and Lucile Packard Grant – New Parent Kit Program	\$ 1,043	\$ 91,385
Committed		
Contracts and amendments to executed contracts:		
Grantees	6,239,788	9,547,435
Others	215,570	349,975
Contracts and amendments to not yet executed contracts	7,592,738	160,000
Assigned	10,447,538	1,117,018
Total Fund Balance	\$ 24,496,677	\$ 11,265,813

10. REVENUES

a) Tobacco Tax and Other Funding

First 5 receives a proportionate share of Proposition 10 money from First 5 California (formerly California Children and Families Commission) based on the number of live births in the county in comparison to the number of live births statewide. Proposition 10 money received by First 5 also includes Surplus Money Investment Fund allocations by First 5 California.

The Surplus Money Investment Fund allocations represent distributions of interest accrued on statewide Proposition 10 money.

Tobacco tax and other revenues are comprised of:

	2012	2011
Proposition 10 money:		
Monthly allocation	\$ 6,776,926	\$ 6,626,365
Surplus Money Investment Fund Allocations	2,715	3,526
Total	\$ 6,779,641	\$ 6,629,891

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

10. REVENUES (continued)

b) Private Grants

First 5 received \$10,500 of private grants from the Silicon Valley Community Foundation for support of First 5's Repayable Loan Program for the year ended June 30, 2011. It did not receive any grant funding in the year ended June 30, 2012.

c) Investment Earnings

Investment earnings of \$312,128 and \$304,082 for the years ended June 30, 2012 and 2011, respectively, comprise of quarterly interest received from the County Treasurer on investments made by First 5 in the County Pool. Interests are recorded in the year earned and available to pay current liabilities.

d) Investment Loss Recovery

In the fiscal year ended June 30, 2009, the County Pool incurred \$155 million of investment losses from the bankruptcy of Lehman Brothers Holdings, Inc. (Lehman Brothers). In April 2012, the County Pool received \$9.3 million as the first of a series of five recovery payments from Lehman Brothers' bankruptcy plan. Recovery payments were distributed to County Pool participants based on the participants' average daily balance in the County Pool for the quarter ended September 30, 2008. First 5's share of the recovery payment was \$123,283.

11. CONTRIBUTIONS TO LOCAL PROJECTS

Over the years from FY 2000-01 to FY 2008-09, First 5 awarded two types of grants to local projects that promote, assist, and improve the early development of children prenatal through age five—planning grants and implementation grants.

Planning grants were designed to allow applicants time and resources to develop an innovative intervention to address a significant opportunity or problem, for which a response did not currently exist or was still evolving. Planning grants ranged from \$5,000 to \$35,000 annually. Implementation grants were for agencies and groups that were clear about their goals, objectives, and strategies and were ready to implement their proposed project. Implementation grants ranged from \$30,000 to \$500,000 annually.

Starting in FY 2009-10, First 5 awarded \$20,167,000 in Cycle One funding to local projects. Cycle One has a three-year term from FY 2009-10 to FY 2011-12. First 5 awarded \$7,234,827 in Cycle Two funding to local projects. Cycle two has a three year term from FY 2011-12 to FY 2013-14.

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

11. CONTRIBUTIONS TO LOCAL PROJECTS (continued)

Grant contributions for the years June 30, 2012 and 2011 included:

	<u>2012</u>	<u>2011</u>
Special Projects:		
First 5 Service Corps Study: Child Care Coordinating Council	\$ -	\$ 20,142
Cycle 1 Continuation funding:		
Child Care Coordinating Council SamCARES	64,661	1,148,748
Child Care Coordinating Council WMG	89,621	179,321
Child Care Coordinating Council Smart Kids	115,173	351,581
Child Care Coordinating Council -		
“Building Kids Up Service Corp Program”	146,177	147,112
Community Gate path - “Demonstration Site”	176,077	289,542
Community Gate path - “Knowledge Center”	62,000	124,332
Community Gate path - “Parent Services”	-	16,692
Daly City Peninsula Partnership	111,080	229,205
San Mateo County Health System -“Pre-to-Three Initiative”	518,000	1,035,421
Jewish Family and Children Services	245,000	488,164
Legal Aid Society of SMC	22,000	42,800
Lucile Packard Children’s Hospital	204,902	388,459
San Mateo County Office of Education	1,309,927	1,498,302
San Mateo Community Health Authority	219,415	419,264
Shelter Network	114,893	230,000
Silicon Valley Community Foundation -		
“School Readiness Initiative Program”	885,354	767,068
South San Francisco Unified School District	8,535	14,831
Star Vista - “Healthy Homes”	630,034	630,633
Star Vista - “School Readiness Initiative Program”	894,629	854,860
Subtotal	<u>5,817,478</u>	<u>8,856,335</u>
Cycle 2 funding:		
Child Care Coordinating Council -		
Supporting Quality Community Based Childcare	47,098	-
Community Gate path-“Demonstration Site”	163,571	-
Daly City Peninsula Partnership	78,900	-
Jewish Family and Children Services	245,000	-
Legal Aid Society of SMC	25,000	-
Lucile Packard Children’s Hospital	170,558	-
San Mateo Community Health Authority	231,750	-
San Mateo County Health System -“Pre-to-Three Initiative”	496,080	-
San Mateo Community Health Center	9,005	-
Shelter Network	116,894	-
South San Francisco Unified School District	2,584	-
Subtotal	<u>1,586,440</u>	<u>-</u>
Miscellaneous adjustments	<u>30,050</u>	<u>20,684</u>
Total per Statements of Activities and Statements of Revenues, Expenditures, and Changes in Fund Balance	<u>\$ 7,433,968</u>	<u>\$ 8,897,161</u>

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

12. REPAYABLE LOAN PROGRAM

In September 2010, the First 5 Commission authorized a repayable loan program (RLP) for qualified State contracted childcare providers. The purpose of the RLP was to assist providers that provided services to children ages 0-5, received at least 75% of funding from the State, and had exhausted all lines of credit with emergency funding due to the State's budget impasse. The term of the RLP was from September 27, 2010 through March 31, 2011 and was administered internally with a \$25,000 contribution from Silicon Valley Community Foundation to offset administrative costs in order to waive 1% interest charge to the providers. A total of \$417,890 was awarded to five qualifying childcare providers during the year ended June 30, 2011. All loans were paid off within fiscal year 2010-11.

13. GRANTS COMMITMENTS

First 5's commitments to grantees at June 30 were as follows:

	2012	2011
Cycle one funding	\$ 591,401	\$ 9,547,435
Cycle two funding	5,648,387	-
Total	\$ 6,239,788	\$ 9,547,435

14. PROGRAM EVALUATION

The commission spent \$340,915 and \$480,377 on program evaluation during fiscal years ended June 30, 2012 and 2011, respectively.

15. RISK MANAGEMENT

First 5 is exposed to various risks of losses related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disaster. The County of San Mateo, through its self-insurance program, provides First 5 with Worker's Compensation and Employer Liability Insurance. First 5 compensates the County for maintaining such insurance. The County Counsel provides legal representation for any claims or litigation of First 5.

Claims have not exceeded coverage in any of the past three fiscal years and there has not been a significant reduction in coverage in the current fiscal year.

16. LEASE OBLIGATIONS

First 5 leases office facilities and other equipment categorized as noncancelable operating leases. Total costs for such leases were \$102,925 and \$99,055 for the years ended June 30, 2012 and 2011, respectively. The future minimum lease payments for the office facilities lease are as follows:

Year Ending June 30		
2013	\$	108,007
2014		36,564
Total	\$	144,571

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Financial Statements
Years Ended June 30, 2012 and 2011

17. RELATED PARTY TRANSACTIONS

The required composition of the Board of Commissioners includes members from the County and other local governments, the San Mateo County Superintendent of Schools and community based organizations which serve children ages 0-5. Many of the programs funded by First 5 San Mateo are operated by organizations represented by the Commissioners. Commissioners must abstain from voting on issues directly related to their representative organizations.

Expenditures of grant awards to organizations represented by Commissioners were as follows:

<u>Organization</u>	<u>2012</u>	<u>2011</u>
San Mateo County Health System	\$ 1,014,080	\$ 1,035,421
San Mateo County Office of Education	1,309,927	1,498,302
Total	<u>\$ 2,324,007</u>	<u>\$ 2,533,723</u>

18. ECONOMIC DEPENDENCY

First 5 has a significant economic dependency on tobacco tax allocations from the State, as these allocations represent a substantial portion of First 5's revenue. First 5's ability to continue operations depends primarily on the continuance of this funding source. Tobacco tax allocations from the State do not have a termination date but are vulnerable to changes in legislation.

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REQUIRED SUPPLEMENTARY INFORMATION

First 5 San Mateo County
(A Discretely Presented Component Unit of the County of San Mateo)
Schedule of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual
Year Ended June 30, 2012

	<u>Budgeted Amounts</u>		<u>Actual Amounts (Budgetary Basis)</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Inflows				
Tobacco tax	\$ 6,224,084	\$ 6,096,000	\$ 6,779,641	\$ 683,641
Investment earnings	262,000	262,000	268,965	6,965
Bad debt recovery	-	-	123,283	123,283
Other revenue	-	-	2,577	2,577
Amounts available for appropriation	<u>6,486,084</u>	<u>6,358,000</u>	<u>7,174,466</u>	<u>816,466</u>
Outflows				
Salaries and benefits	1,056,000	1,056,000	1,243,021	(187,021)
Services and supplies	407,296	407,296	649,661	(242,365)
Contributions to local projects	9,332,000	9,332,000	7,433,968	1,898,032
Total charges to appropriations	<u>10,795,296</u>	<u>10,795,296</u>	<u>9,326,650</u>	<u>1,468,646</u>
Deficiency of revenues over expenditures	<u>\$ (4,309,212)</u>	<u>\$ (4,437,296)</u>	(2,152,184)	<u>\$ 2,285,112</u>
Extraordinary Item				
Restitution of payment to State of California per AB99			<u>15,339,885</u>	
Net change in fund balance			13,187,701	
Fund Balance - Beginning			<u>10,798,428</u>	
Fund Balance - Ending			<u>\$ 23,986,129</u>	

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Notes to the Supplementary Information
Year Ended June 30, 2012

1. BUDGETARY ACCOUNTING AND ENCUMBRANCES

The Board adopts an annual operating budget, which can be amended by the Board throughout the year. As discussed in Note 1(d) of the notes to the basic financial statements, the basis used to prepare the budget is the same as the basis used to reflect actual revenues and expenditures, except the budget excludes unrealized gains and losses and changes to the liabilities for compensated absences and postemployment benefits other than pensions (OPEB). The financial statements record unrealized gains and losses, compensated absences, and OPEB as required by generally accepted accounting principles (GAAP).

First 5 uses an encumbrance system in the County's general ledger system, IFAS, to assist in controlling expenditures. Purchase orders, contracts, and other commitments for the expenditures of monies are recorded under this system in order to reserve applicable appropriations. Any encumbrances outstanding at year-end are included in committed fund balance as they do not constitute expenditures or liabilities.

The net change in fund balance under budgetary basis on page 28 is reconciled to the net change in fund balance under GAAP basis on page 11 as follows:

Deficiency of revenues over expenditures/ net change in fund balance – budgetary basis	\$ 13,187,701
Changes in unrealized (gain)/loss on cash equivalents	<u>43,163</u>
Deficiency of revenues over expenditures/ net change in fund balance – GAAP basis	<u><u>\$ 13,230,864</u></u>

2. EXPENDITURES IN EXCESS OF BUDGET

In fiscal year ended June 30, 2012, salaries and benefits expenditures exceeded the budget by \$187,021 due to the delay of planned reduction of personnel until FY 2012-13. Services and supplies expenditures exceeded budget by \$242,365 because evaluation costs were originally budgeted under contributions to local projects, but are reported as services and supplies in the financial statements. However, total expenditures for the year reflect a positive variance.

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OTHER REPORTS

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First 5 San Mateo County Commission
San Mateo, California

**Independent Auditor's Report on Internal Control Over Financial Reporting and
on Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance With *Government Auditing Standards***

We have audited the financial statements of First 5 San Mateo County (First 5), a discretely presented component unit of the County of San Mateo, California (County), as of and for the year ended June 30, 2012, and have issued our report thereon dated October 17, 2012. We conducted our audit in accordance with auditing standards generally accepted 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.

Internal Control Over Financial Reporting

Management of First 5 is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered First 5's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of First 5's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of First 5's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined previously.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether First 5's financial statements are free of material misstatement, we 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 financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the County Board of Supervisors, the First 5 San Mateo County Commission, the State Commission, and the State Controller's Office, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Macias Gini & Connell LLP

Walnut Creek, California
October 17, 2012

First 5 San Mateo County Commission
 San Mateo, California

Independent Auditor's Report on State Compliance

We have audited the basic financial statements of First 5 San Mateo County (First 5), a discretely presented component unit of the County of San Mateo, California (County), as of and for the year ended June 30, 2012, and have issued our report thereon dated October 17, 2012. We conducted our audit in accordance with auditing standards generally accepted 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. We have also audited the First 5's compliance with the requirements specified in the State of California's *Standards and Procedures for Audits of Local Entities Administering the California Children and Families Act*, issued by the State Controller's Office, applicable to the First 5's statutory requirements identified below for the year ended June 30, 2012. Compliance with the requirements referred to above is the responsibility of First 5's management. Our responsibility is to express an opinion on the First 5's compliance based on our audit.

We conducted our compliance audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and the State of California's *Standards and Procedures for Audits of Local Entities Administering the California Children and Families Act*, issued by the State Controller's Office. Those standards and the State of California's *Standards and Procedures for Audits of Local Entities Administering the California Children and Families Act* require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the compliance requirements referred to above that could have a material effect on the statutory requirements listed below occurred. An audit includes examining on a test basis, evidence about the First 5's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the First 5's compliance with those requirements.

In connection with the audit referred to above, we selected and tested transactions and records to determine the First 5's compliance with the state laws and regulations applicable to the following items:

<u>Description</u>	<u>Audit Guide Procedures</u>	<u>Procedures Performed</u>
Contracting and Procurement	6	Yes
Administrative Costs	3	Yes
Conflict of Interest	3	Yes
County Ordinance	4	Yes
Long-range Financial Plans	2	Yes
Financial Condition of the Commission	1	Yes
Program Evaluation	3	Yes
Salaries and Benefits Policies	2	Yes

The results of our auditing procedures disclosed an instance of noncompliance in which the First 5's program evaluation costs exceeded budget, which is described in the accompanying schedule of finding and recommendation as item 2012-1.

In our opinion, except for the noncompliance described in the preceding paragraph, the First 5 complied, in all material respects, with the compliance requirements referred to above that are applicable to the statutory requirements listed above for the year ended June 30, 2012.

The First 5's response to the finding identified in our audit is described in the accompanying schedule of finding and recommendation. We did not audit the First 5's response and, accordingly, we express no opinion on the response.

This report is intended solely for the information of the County Board of Supervisors, the First 5 Commission, the State Commission, and the State Controller's Office and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Macias Gini & Cannelo LLP

Walnut Creek, California
October 17, 2012

FIRST 5 SAN MATEO COUNTY
(A Discretely Presented Component Unit of the County of San Mateo)

Schedule of Finding and Recommendation
Year Ended June 30, 2012

Finding 2012-1 Program Evaluation

Criteria:

In accordance with Health and Safety Code section 130151(b)(7), a county commission must have policies and practices with respect to the amount it spends on program evaluation and the documented results of these expenditures. First 5's practice is to monitor evaluation costs using its annual budget.

Condition:

During our review of the First 5's compliance with its practice on evaluation costs, we noted that actual evaluation costs consisted of two components – consultant fees and salaries and benefits costs for an evaluation program specialist. Current year evaluation consultant fees of \$222,159 were within the budgeted amount of \$304,000. However, since salaries and benefits were budgeted in total for the entire organization, we compared in total and found that actual salaries and benefits expenditures of \$1,243,021 exceeded the budget of \$1,056,000 by \$187,021.

Cause and Effect:

First 5 planned to reduce its personnel during the fiscal year ended June 30, 2012. However, implementation of the reduction plan was delayed to August 2012, and resulted in additional salaries and benefits costs for the fiscal year.

Management Response:

Salary and benefits expenditures for First 5 staff are appropriated in one line item under Org 19510. This includes all administrative, program, and evaluation staff. Management will conduct a cost analysis of salary and benefits in fiscal year 2013 and will use the County's integrated financial accounting system (IFAS) to separately track the spending for the three components (e.g. using job ledgers to differentiate expenditures).