LUTHERAN SOCIAL SERVICES OF NORTHERN CALIFORNIA AND SUBSIDIARY

Consolidated Financial Statements for the Years Ended June 30, 2011 and 2010 and Independent Auditors' Report

LUTHERAN SOCIAL SERVICES
OF NORTHERN CALIFORNIA AND SUBSIDIARY

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KARLSSON & LANE
AN ACCOUNTANCY CORPORATION

INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Lutheran Social Services of Northern California
Concord, California

We have audited the accompanying consolidated statements of financial position of Lutheran Social Services of Northern California and Subsidiary (a nonprofit organization) (the "Entity") as of June 30, 2011 and 2010, and the related consolidated statements of activities, functional expenses, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Entity's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits 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 audits 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 consolidated financial statements. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Lutheran Social Services of Northern California and Subsidiary as of June 30, 2011 and 2010, and the changes in its net assets and its cash flows for the years 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 January 10, 2012 on our consideration of the Entity'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 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 assessing the results of our audit.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements of the Entity taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Karlsson & Lane, a.c.

Pleasanton, California
January 10, 2012

LUTHERAN SOCIAL SERVICES OF NORTHERN CALIFORNIA AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
JUNE 30, 2011 AND 2010

	2011	2010
ASSETS		
Cash and cash equivalents	$ 788,686	$ 659,293
Cash held for agencies in trust	559,203	631,553
Investments	100,839	85,759
Accounts receivable	583,430	808,543
Prepaid expenses and other assets	16,584	58,531
Property and equipment, net	3,432,202	3,549,137
Total assets	$ 5,480,944	$ 5,792,816
LIABILITIES AND NET ASSETS		
LIABILITIES		
Accounts payable and accrued expenses	$ 472,314	$ 421,669
Amounts payable to agencies in trust	559,203	631,553
Deferred revenue	120,678	233,690
Line of credit	109,535	625,000
Debt	1,611,164	1,002,266
Total liabilities	2,872,894	2,914,178
NET ASSETS		
Unrestricted	853,718	972,763
Temporarily restricted	1,654,332	1,805,875
Permanently restricted	100,000	100,000
Total net assets	2,608,050	2,878,638
Total liabilities and net assets	$ 5,480,944	$ 5,792,816

See notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF NORTHERN CALIFORNIA AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

	2011	2010
UNRESTRICTED NET ASSETS		
Revenue and support:		
Contracts and fees	$ 6,891,459	$ 6,943,088
Contributions	567,679	291,882
Legal settlement	-	800,000
Other income	182,262	101,667
Total revenue and support	7,641,400	8,136,637
Net assets released from restrictions	360,373	260,854
Total revenues and net assets released from restrictions	8,001,773	8,397,491
Expenses:		
Program services	6,802,894	6,642,690
Fundraising	232,687	166,271
Management and general	1,085,237	1,414,756
Total expenses	8,120,818	8,223,717
Change in unrestricted net assets	(119,045)	173,774
TEMPORARILY RESTRICTED NET ASSETS		
Contributions	208,830	100,000
Net assets released from restrictions	(360,373)	(260,854)
Change in temporarily restricted net assets	(151,543)	(160,854)
CHANGE IN NET ASSETS	(270,588)	12,920
NET ASSETS, BEGINNING OF YEAR	2,878,638	2,865,718
NET ASSETS, END OF YEAR	$ 2,608,050	$ 2,878,638

See notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF NORTHERN CALIFORNIA AND SUBSIDIARY

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
YEAR ENDED JUNE 30, 2011

	Program Services						
	Money Management Services	Housing for Youth	Housing for Families and Adults	Total Programs	Fundraising	Management and General	Total
Salaries and benefits	$ 1,144,254	$ 874,833	$ 1,378,701	$ 3,397,788	$ 102,841	$ 452,359	$ 3,952,988
Client assistance	469	814,331	1,338,077	2,152,877	-	751	2,153,628
Professional fees	51,897	41,225	243,898	337,020	65,441	203,498	605,959
Occupancy	88,877	52,128	61,631	202,636	-	37,877	240,513
Insurance	11,736	61,253	147,798	220,787	10	17,091	237,888
Depreciation	-	-	-	-	-	131,567	131,567
Supplies	53,472	16,392	40,132	109,996	2,348	8,178	120,522
Telephone	22,075	33,472	40,106	95,653	857	23,699	120,209
Other	25,628	35,260	12,532	73,420	945	40,552	114,917
Equipment and building repairs	24,160	16,984	10,808	51,952	6,398	35,198	93,548
Travel	5,300	33,384	32,421	71,105	2,845	16,887	90,837
Interest	-	5,226	-	5,226	-	84,464	89,690
Printing and duplicating	18,374	15,574	15,805	49,753	13,363	20,023	83,139
Outreach and education	65	162	8,754	8,981	28,933	955	38,869
Staff and board	7,688	920	2,771	11,379	3,769	5,930	21,078
Postage	8,796	397	543	9,736	3,825	4,858	18,419
Dues and subscriptions	1,046	192	3,347	4,585	1,112	1,350	7,047
Total	$ 1,463,837	$ 2,001,733	$ 3,337,324	$ 6,802,894	$ 232,687	$ 1,085,237	$ 8,120,818

See notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF NORTHERN CALIFORNIA AND SUBSIDIARY

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
YEAR ENDED JUNE 30, 2010

	Program Services						
	Money Management Services	Housing for Youth	Housing for Families and Adults	Total Programs	Fundraising	Management and General	Total
Salaries and benefits	$ 1,145,992	$ 896,514	$ 1,324,109	$ 3,366,615	$ 45,060	$ 716,000	$ 4,127,675
Client assistance	982	1,054,623	1,185,187	2,240,792	-	510	2,241,302
Professional fees	15,184	34,930	194,545	244,659	76,256	197,118	518,033
Occupancy	82,056	65,759	64,269	212,084	-	44,977	257,061
Other	58,649	43,610	26,068	128,327	268	47,600	176,195
Depreciation	-	-	-	-	-	149,094	149,094
Equipment and building repairs	24,247	50,180	15,231	89,658	1,208	51,144	142,010
Supplies	48,260	27,849	45,899	122,008	1,115	15,526	138,649
Telephone	18,532	28,965	31,812	79,309	700	26,348	106,357
Travel	3,820	35,045	33,589	72,454	2,052	10,545	85,051
Interest	-	12,511	-	12,511	1,543	69,901	83,955
Staff and board	12,720	295	9,411	22,426	6,790	31,917	61,133
Printing and duplicating	13,000	13,910	12,234	39,144	6,599	14,400	60,143
Insurance	-	786	-	786	-	25,894	26,680
Outreach and education	214	593	571	1,378	20,246	2,561	24,185
Postage	8,217	347	400	8,964	3,557	7,510	20,031
Dues and subscriptions	1,325	-	250	1,575	877	3,711	6,163
Total	$ 1,433,198	$ 2,265,917	$ 2,943,575	$ 6,642,690	$ 166,271	$ 1,414,756	$ 8,223,717

See notes to consolidated financial statements.

LUTHERAN SOCIAL SERVICES OF NORTHERN CALIFORNIA AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	$ (270,588)	$ 12,920
Adjustments to reconcile change in net assets to cash flows provided by operating activities:		
Depreciation	131,567	149,094
Net realized and unrealized gain on investments	(15,080)	(7,626)
Changes in assets and liabilities that provided (used) cash:		
Accounts receivable	225,113	164,657
Prepaid expenses and other assets	41,947	(1,379)
Accounts payable and accrued expenses	50,645	(146,014)
Deferred revenue	(113,012)	233,690
Net cash provided by operating activities	50,592	405,342
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(14,632)	(69,745)
Net cash used in investing activities	(14,632)	(69,745)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net (repayments) proceeds on line of credit	(515,465)	107,750
Proceeds from issuance of debt	1,305,000	134,464
Principal payments on debt	(696,102)	(38,011)
Net cash provided by financing activities	93,433	204,203
NET CHANGE IN CASH AND CASH EQUIVALENTS	129,393	539,800
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	659,293	119,493
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 788,686	$ 659,293
Supplemental information:		
Cash paid for interest	$ 120,522	$ 142,010

See notes to consolidated financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operation - Lutheran Social Services of Northern California (the "Organization") is a California non-profit organization headquartered in Concord, California. The Organization serves as a social service agency to all of Northern California by providing professional counseling and promotion of welfare work to all persons within society. The Organization's principal sources of funding are contract service fees from governmental agencies and contributions.

Lutheran Housing Development Company LLC (the "Company"), is a single member California limited liability company of which the Organization is the single member. The Company's purpose is to hold real property for use in the Organization's services.

Basis of Consolidation, Accounting and Presentation - Assets, liabilities and operations of the Company are consolidated with the Organization (collectively, the "Entity"). All significant inter-company transactions have been eliminated in consolidation.

The Entity maintains its accounting records and prepares its financial statements using the accrual basis of accounting; therefore, revenue is recognized when earned, regardless of when collected, and expenses are recognized when the obligation is incurred regardless of when paid.

The Entity reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Unrestricted Net Assets - the portion of net assets that is neither temporarily nor permanently restricted by donor - imposed stipulations. These net assets are intended for use of management and the Board of Directors for program services, fundraising activities and general operations.

Temporarily Restricted Net Assets - the portion of net assets of which use by the Entity is limited by donor - imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Entity.

Permanently Restricted Net Assets - the portion of net assets of which use by the Entity is limited by donor - imposed stipulations that neither expire by passage of time nor can otherwise be removed by actions of the Entity.

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

Fair Value - ASC 820 includes a fair value hierarchy that is intended to increase the consistency and comparability in fair value measurements and related disclosures. The fair value hierarchy is based on inputs to valuation techniques that are used to measure fair value that are either observable or unobservable. Observable inputs reflect assumptions market participants would use in pricing an asset or liability based on market data obtained from independent sources while unobservable inputs reflect a reporting entity's pricing based upon their own market assumptions. The fair value hierarchy consists of the following three levels:

Level 1 - instrument valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets.

Level 2 - instrument valuations are obtained from readily-available pricing sources for comparable instruments.

Level 3 - instrument valuations are obtained without observable market values and require a high level of judgment to determine the fair value.

Cash and Cash Equivalents - For the purpose of the statement of cash flows, the Entity considers all temporary investments with original maturities of three months or less to be cash equivalents.

Cash Held for Agencies in Trust - The Entity has established a relationship with social security recipients (the “Recipients”) through city and county contracts, whereby the Recipients’ social security checks are deposited into the Entity’s bank accounts and are withdrawn by the Recipients in accordance with budgets established by the Recipient with the counsel of the Entity. The cash is legally owned by the Recipients, and they may withdraw their cash from the program at any time. Cash held by the Entity on behalf of the Recipients is presented on the statements of financial position as cash held for agencies in trust with a corresponding liability presented as amounts payable to agencies in trust.

Investments - Investments are valued at fair value with realized and unrealized gains and losses reflected in the statements of activities.

Accounts Receivable - Accounts receivable are recorded at the value of the revenue earned and are due upon presentation. Receivable balances with charges over thirty days old are considered delinquent and management begins collection efforts at this time. Delinquent accounts receivable invoices do not accrue interest. The Entity continually monitors the credit worthiness of each account and recognizes allowances for estimated bad debts on accounts that are no longer estimated to be collectible. The Entity regularly adjusts any allowance for subsequent collections and final determination that a receivable is no longer collectible. There was no allowance considered necessary at June 30, 2011 or 2010.

Property and Equipment - Property and equipment is stated at cost, or if donated, at estimated fair value at the date of donation. Depreciation has been provided on the straight-line method over the estimated useful lives of the assets of 3 to 39 years. It is the Entity’s policy to capitalize significant additions above $1,000.

Contracts and Fees - Contracts and fees are recognized when the Entity incurs expenditures related to the required program services. Amounts billed or received in advance are recorded as advances until the related services are performed.

Contributions - Contributions are recognized as revenue when they are received or the promise to give is made. Contributions restricted by the donor are reported as an increase in unrestricted net assets if the restriction expires in the same reporting period in which the support is recognized. All other donor-restricted contributions are reported as increases in temporarily restricted or permanently restricted net assets depending upon the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets. Contributions of assets other than cash are recorded at their estimated fair value.

Income Taxes - The Organization and Company are organized under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code and, accordingly, are exempt from paying Federal and California income taxes.

The Entity has adopted the accounting guidance related to uncertain tax positions, and has evaluated its tax positions taken for all open tax years. Currently, the 2007 through 2010 information returns are open and subject to examination. In management's judgment there are no uncertain tax positions as of June 30, 2011.

Functional Expense Classification - The costs of providing various programs and activities have been summarized on a functional basis in the Statement of Functional Expenses. Accordingly, certain costs have been allocated among the programs, fundraising and administrative activities that have benefited. Allocation is based on the estimates prepared by management.

Subsequent Events - Subsequent events have been evaluated through January 10, 2012, which is the date the financial statements were available to be issued.

2. INVESTMENTS

Investments consist of the following at June 30, 2011 and 2010:

	2011	2010
Corporate equities	$ 67,965	$ 57,802
Bonds	26,823	22,812
Other	6,051	5,145
Total	$ 100,839	$ 85,759

The organization's investments are held in a comingled fund with a third party foundation, and are considered Level 2 instruments.

Investment returns are included in other income on the statements of activities, and consist of the following for the years ended June 30, 2011 and 2010:

	2011	2010
Interest and dividends	$ 51	$ 877
Net unrealized and realized gains	15,080	7,626
Total	$ 15,131	$ 8,503

3. PROPERTY AND EQUIPMENT

Property and equipment consist of the following at June 30, 2011 and 2010:

	2011	2010
Buildings and improvements	$ 2,289,684	$ 2,275,052
Land	1,401,070	1,401,070
Furniture and equipment	520,190	520,191
	4,210,944	4,196,313
Accumulated depreciation	(778,742)	(647,176)
Net property and equipment	$ 3,432,202	$ 3,549,137

Land and buildings with cost basis of $2,259,506 and accumulated depreciation of $182,483 are subject to liens held by state and local governments to use the land, buildings and improvements for program purposes.

4. LINE OF CREDIT

The Entity has a bank line of credit of $600,000, expiring May 2016. The line of credit is secured by all assets of the Entity. Interest of 5.25% is payable monthly. The interest rate reset in May 2011 to Wall Street Journal Prime plus 1%. The rate will update daily through maturity, with a floor of 5.25% and ceiling of 26%. The line of credit has an outstanding balance of $109,535 and $625,000 at June 30, 2011 and 2010, respectively.

5. DEBT

The Entity's debt obligations as of June 30, 2011 and 2010 are as follows:

	2011	2010
Note payable to a bank; interest rate at 6.0% annually; principle and interest payments of $4,449 are due monthly, with remaining principle and interest due in full at maturation in September 2014; collateralized by the Entity's real property. Repaid in 2011.	-	676,307
Note payable to a bank; interest rate at 1 year LIBOR rounded up to nearest 0.125% adjusted each December thirteenth to the 1 year LIBOR plus 2% (2.875% at June 30, 2011); principle and interest payments of $1,295 are due monthly, adjusted each year for changes in the one year LIBOR based on a 300 month amortization ending December 2032, with remaining principle and interest due at maturation in December 2014; collateralized by the Entity's real property.	248,926	264,912

Note payable to a local government; interest at 3% annually; principle and interest payments of $466 due monthly with remaining principle and interest due at maturation; matures October 2023.	57,238	61,047
Note payable to a bank; interest rate at 6.0% annually; principle and interest payments of $8,499 are due monthly, with remaining principle and interest due in full at maturation in December 2016; collateralized by the Entity's real property.	1,305,000	-
Total	$ 1,611,164	$ 1,002,266

Future minimum principle payments as of June 30, 2011 are as follows:

2012	$ 33,562
2013	38,423
2014	40,382
2015	255,902
2016	1,242,895
Total	$ 1,611,164

6. EMPLOYEE BENEFITS

The Entity makes contributions equal to a range of 2% to 3% of salaries of eligible employees to a defined contribution retirement plan sponsored by the Entity. Eligibility is based on hours per week and length of employment. Contributions made for the year ended June 30, 2011 and 2010 were $25,605 and $68,505, respectively.

7. CONCENTRATIONS AND CREDIT RISK

The Entity has identified financial instruments that are potentially subject to credit risk as cash, investments and accounts receivable. At June 30, 2011, the Entity had no deposits in excess of federally insured limits. Investments are diversified into various types of marketable securities in order to limit the concentration of market risk. Accounts receivable are unsecured, however concentrations of credit risk with respect to these receivables are limited as substantially all amounts are receivable from government agencies. Management does not believe there is any risk of bad debts relating to the accounts receivable. Substantially all of the Entity's contract revenues are provided by federal, state or local government agencies.

8. RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following as of June 30, 2011 and 2010:

	2011	2010
Use restrictions:		
Project Hope	$ -	$ 5,000
Disaster preparedness and relief	3,148	10,665
Polk Street	15,708	23,239
Health Shack	52,500	-
Youth leadership	26,216	26,216
Property	1,556,760	1,740,755
Total	$ 1,654,332	$ 1,805,875

At June 30, 2011, the Entity had permanently restricted net assets of $100,000 for the Romaine Hansen Murphy memorial fund, the income of which is restricted for program expenditures of the Entity.

9. RELATED PARTY TRANSACTIONS

During the years ended June 30, 2011 and 2010, the Entity contracted with a company owned by an employee to provide daycare program assistance in the amounts of $115,000 in each year, respectively. Accounts payable to the company were $10,987 and $69,432 as of June 30, 2011 and 2010, respectively.

10. CONTINGENCIES

In prior years the Entity received contributions from state and local government agencies that require the Entity to renovate and operate real property for the purpose of transitional housing for periods of ten years to fifty years. Management believes the possibility of failing to meet the requirements of the contributions is remote. Should the Entity fail to meet the requirements, the properties would be remitted to the government agencies. The contributions are temporarily restricted, and the restrictions are released over the periods of the related agreements.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
JUNE 30, 2011

Federal Grantor Program Title/Pass-Through Grantor Program Title	Federal CFDA Number	Pass-through Number		Federal Expenditures	
U.S. Department of Health and Human Services:					
ARRA - Temporary Assistance for Needy Families – Passed through Sacramento County Department of Human Assistance	93.558	HPRP	$	264,302	
ARRA – Community Services Block Grant – Passed through San Joaquin County	93.674			25,000	
HIV Emergency Relief Project Grants – Passed through the City and County of San Francisco Department of Public Health	93.914	DPHC12000516		501,674	
Total U.S. Department of Health and Human Services			$	790,976	
U.S. Department of Housing and Urban Development:					
Community Development Block Grant – Passed through Sacramento County Department of Human Assistance	14.218	HPRP	$	261,291	
Supportive Housing Program – Passed through City and County of San Francisco Department of Social Services	14.235	9711SN		152,816	*
Supportive Housing Program – Passed through Sacramento County Department of Human Assistance	14.235	DHA\CS-LSS-07-11		541,497	*
Supportive Housing Program – Passed through Sacramento County Department of Human Assistance	14.235	CA0252B9T110802		381,262	*
Supportive Housing Program – Passed through Sacramento County Department of Human Assistance	14.235	DHA\CS-LSS-06-12		551,039	*
Supportive Housing Program – Passed through Sacramento County Department	14.235	DHA\CS-LSS-01-11		307,884	*

of Human Assistance				
Supportive Housing Program – Passed through Sacramento County Department of Human Assistance	14.235	DHA\CS-LSS-02-12	74,170	*
Supportive Housing Program – Passed through Sacramento County Department of Human Assistance	14.235	DHA\CS-LSS-03-11	320,174	*
Supportive Housing Program – Passed through Sacramento County Department of Human Assistance	14.235	DHA\CS-LSS-09-11	220,398	*
Supportive Housing Program – Passed through Sacramento County Department of Human Assistance	14.235	DHA\CS-LSS-10-11	434,381	*
ARRA – Homeless Prevention and Rapid Re-housing Program – Passed through Sacramento County Department of Human Assistance	14.257	HPRP	935,903	*
Total U.S. Department of Housing and Urban Development			$ 4,180,815	
Total			$ 4,971,791	

* Denotes a Major Program

LUTHERAN SOCIAL SERVICES OF NORTHERN CALIFORNIA AND SUBSIDIARY

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2011

Note A - Basis of Presentation

The Schedule of Expenditures of Federal Awards (the "Schedule") includes federal grant activity of the Entity under programs of the federal government for the year ended June 30, 2011. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of the Entity, it is not intended to and does not present the financial position, changes in net assets, or cash flows of the Entity.

Note B - Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the costs principles contained in OMB Circular A-122, *Cost Principles for Non-profit Organizations*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

Pass-through entity identifying numbers are presented where available.

KARLSSON & LANE
AN ACCOUNTANCY CORPORATION

INDEPENDENT AUDITORS' 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

To the Board of Directors of
Lutheran Social Services of Northern California and Subsidiary
Concord, California

We have audited the consolidated financial statements of Lutheran Social Services of Northern California and Subsidiary (a nonprofit organization) (the "Entity") as of and for the year ended June 30, 2011, and have issued our report thereon dated January 10, 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

In planning and performing our audit, we considered the Entity's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Entity'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 a 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 the 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 above.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Entity's consolidated 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 management, the audit committee, board of directors, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Karlsson & Lane, a.c.

Pleasanton, California
January 10, 2012

KARLSSON & LANE
AN ACCOUNTANCY CORPORATION

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Directors of
Lutheran Social Services of Northern California and Subsidiary
Concord, California

Compliance

We have audited Lutheran Social Services of Northern California and Subsidiary's (the "Entity") compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Entity's major federal programs for the year ended June 30, 2011. The Entity's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Entity's management. Our responsibility is to express an opinion on the Entity's compliance based on our audit.

We conducted our audit of compliance 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 OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Entity'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 Entity's compliance with those requirements.

In our opinion, the Entity complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2011.

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Internal Control Over Compliance

Management of the Entity is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Entity's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Entity's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance 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 compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, the audit committee, board of directors, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Karlsson & Lane, a.c.

Pleasanton, California
January 10, 2012

LUTHERAN SOCIAL SERVICES OF NORTHERN CALIFORNIA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
JUNE 30, 2011

I. SUMMARY OF INDEPENDENT AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued: **Unqualified**

Internal control over financial reporting:

Material weakness(es) identified:	____ Yes	X No
Significant deficiency(ies) identified that are not considered to be a material weakness?	____ Yes	X None Reported
Noncompliance material to financial statements noted?	____ Yes	X No

Federal Awards

Internal control over major programs:

Material weakness(es) identified?	____ Yes	X No
Significant deficiency(ies) identified that are not considered to be a material weakness(es)?	____ Yes	X None Reported

Type of auditors' report issued on compliance for major programs: **Unqualified**

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133?	____ Yes	X No

Identification of major program:

CDFA Number(s)	Name of Federal Program or Cluster
14.235	Supportive Housing Program
14.257	ARRA – Homeless Prevention and Rapid Re-housing Program

Dollar threshold used to distinguish between type A and type B programs: **$300,000**

Auditee qualified as low-risk auditee?	X Yes	____ No

I. Financial Statement Findings

None

II. Federal Awards Findings

None

III. Prior Year Findings

Prior year's findings 2010-1 through 2010-5 are considered resolved.