STEPPING STONES, INC.
(A NON-PROFIT ORGANIZATION)

FINANCIAL STATEMENTS
WITH ADDITIONAL INFORMATION

YEARS ENDED JUNE 30, 2008 AND 2007

STEPPING STONES, INC.
FINANCIAL STATEMENTS WITH ADDITIONAL INFORMATION
YEARS ENDED JUNE 30, 2008 AND 2007

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Stepping Stones, Inc.
Lavalette, West Virginia

We have audited the accompanying statements of financial position of Stepping Stones, Inc., (a non-profit organization) as of June 30, 2008 and 2007, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these 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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Stepping Stones, Inc. as of June 30, 2008 and 2007, 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 December 5, 2008 on our consideration of Stepping Stones, Inc.'s internal control over financial reporting and 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 important for assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of Stepping Stones, Inc. taken as a whole. The schedules of functional expenses are presented for purposes of additional analysis and is not part of the basic financial statements of the organization. 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 also not a required part of the basic financial statements of the Organization. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Ware & Hall PLLC

Huntington, West Virginia
December 5, 2008

STEPPING STONES, INC.
STATEMENTS OF FINANCIAL POSITION
JUNE 30, 2008 AND 2007

	2008	2007
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 304,658	$ 264,386
Accounts receivable	323,780	193,760
Prepaid expenses	16,815	19,730
TOTAL CURRENT ASSETS	645,253	477,876
PROPERTY AND EQUIPMENT, NET	306,036	259,486
OTHER ASSETS		
Other	18,360	18,360
TOTAL ASSETS	$ 969,649	$ 755,722
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	$ 135,526	$ 105,996
Note payable - bank	16,740	26,594
Accrued and withheld payroll taxes	10,562	6,628
Accrued vacation	18,899	19,389
Deferred revenue	-0-	15,000
Current portion of long-term debt	15,359	9,705
TOTAL CURRENT LIABILITIES	197,086	183,312
LONG-TERM DEBT , LESS CURRENT PORTION INCLUDED ABOVE	42,342	24,819
TOTAL LIABILITIES	239,428	208,131
NET ASSETS		
Unrestricted	730,221	547,591
TOTAL LIABILITIES AND NET ASSETS	$ 969,649	$ 755,722

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS

STEPPING STONES, INC.
STATEMENTS OF ACTIVITIES
YEARS ENDED JUNE 30, 2008 AND 2007

	2008	2007
UNRESTRICTED NET ASSETS		
SUPPORT AND REVENUE		
Medicaid	$ 255,722	$ 258,388
Residential child care	809,382	725,934
Transition to independence	313,498	64,264
Community Based Teams	15,000	86,597
Department of Education	14,912	14,618
Transitional living	311	247
Contributions	670	250
Interest	8,550	7,819
Other	452	423
TOTAL UNRESTRICTED SUPPORT AND REVENUE	1,418,497	1,158,540
EXPENSES		
Program services		
Residential Child care	693,881	798,869
Community Based Teams	2,913	34,931
Transition to independence	271,083	38,365
TOTAL PROGRAM SERVICES	967,877	872,165
Supporting services		
Management and general	267,990	220,919
TOTAL EXPENSES	1,235,867	1,093,084
CHANGE IN UNRESTRICTED NET ASSETS	182,630	65,456
NET ASSETS AT BEGINNING OF YEAR		
As originally reported	547,591	469,135
Adjustment for understatement of grant revenue	-0-	13,000
Balance at beginning of year as-restated	547,591	482,135
NET ASSETS AT END OF YEAR	$ 730,221	$ 547,591

STEPPING STONES, INC.
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2008 AND 2007

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	$ 182,630	$ 65,456
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	56,892	45,951
(Increase) decrease in operating assets:		
Accounts receivable	(130,020)	(58,033)
Prepaid expenses	2,915	(4,830)
Increase (decrease) in operating liabilities:		
Accounts payable	29,530	9,711
Accrued and withheld payroll taxes	3,934	233
Accrued vacation	(490)	6,183
Deferred revenue	(15,000)	(74,000)
NET CASH (USED) PROVIDED BY OPERATING ACTIVITIES	130,390	(9,329)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(103,442)	(46,108)
NET CASH (USED IN) INVESTING ACTIVITIES	(103,442)	(46,108)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from short-term debt	16,740	26,594
Payment of short-term debt	(26,594)	-0-
Proceeds from long-term debt	33,483	-0-
Principal payments on long-term debt	(10,306)	(9,081)
NET CASH PROVIDED BY FINANCING ACTIVITIES	13,323	17,513

Continued (next page)

STEPPING STONES, INC.
STATEMENTS OF CASH FLOWS (CONTINUED)
YEARS ENDED JUNE 30, 2008 AND 2007

	2008	2007
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	$ 40,272	$ (37,924)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	264,386	302,310
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 304,658	$ 264,386
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the year for:		
Interest	$ 1,714	$ 3,076

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THE FINANCIAL STATEMENTS

STEPPING STONES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2008 AND 2007

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

DESCRIPTION OF ORGANIZATION

Stepping Stones, Inc. is a non-profit organization which provides residential and living support services for adolescent boys in Wayne County, West Virginia. The Organization is supported primarily through third party reimbursements from the West Virginia Department of Health and Human Resources.

PROMISES TO GIVE

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

ESTIMATES

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

ACCOUNTS RECEIVABLE

The Organization provides services to children on a third-party reimbursement basis. The Organization bills the West Virginia Department of Health and Human Resources for Residential Child Care, Medicaid, Community Based Team, and Transition to Independence Programs and the West Virginia Department of Education for breakfast and lunch programs (School Breakfast Program and National School Lunch Program) in accordance with contractual agreements without requiring collateral or any other security.

BAD DEBTS

The Organization utilizes the direct charge - off method of accounting for bad debts. This method does not result in a materially different provision for bad debt expense than would result from the use of the reserve method.

INVENTORY

Disposable supplies and household goods are considered immaterial and are expensed when purchased.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

PROPERTY AND EQUIPMENT

Property and equipment is stated at their purchased cost. Contributed assets are stated at estimated fair value. Major expenditures and those which substantially increase useful lives are capitalized. Maintenance, repairs and minor renewals are charged to operations when incurred. When property and equipment is sold or otherwise disposed of, the asset account and related accumulated depreciation account are relieved, and any gain or loss is included in operations.

Property and equipment acquired with federal funds is owned by the Organization while used in the program for which it was purchased or in other future authorized programs. The funding sources, however, have a reversionary interest in the property and equipment purchased with grant funds; therefore its disposition, as well as the ownership of any sale proceeds therefrom is subject to funding source regulations.

DEPRECIATION

The cost of property and equipment is depreciated over the estimated useful lives of the related assets. Depreciation is computed on the straight line method. The useful lives of property and equipment for purposes of computing depreciation are:

Land improvements	10 to 30 years
Buildings and improvements	5 to 30 years
Furniture and equipment	3 to 10 years
Vehicles	5 years

INCOME TAXES

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

CASH AND CASH EQUIVALENTS

For purposes of the statement of cash flows, cash equivalents include time deposits, certificates of deposit and all unrestricted highly liquid investments.

FUNCTIONAL ALLOCATION OF EXPENSES

The cost of providing the various programs and other activities have been summarized on a functional basis in the Statements of Activities. Accordingly, certain costs have been allocated among the programs and supporting services benefitted.

NOTE 2 - PROPERTY AND EQUIPMENT

Property and equipment consist of the following at June 30, 2008 and 2007:

	2008	2007
Land and improvements	$ 55,085	$ 55,085
Buildings and improvements	387,865	375,037
Furniture and equipment	224,410	184,018
Vehicles	220,900	170,678
	888,260	784,818
Less: Accumulated Depreciation	(582,224)	(525,332)
Property and equipment, net	$ 306,036	$ 259,486

Depreciation expense for the years ended June 30, 2008 and 2007 totaled $56,892 and $45,951, respectively.

NOTE 3 - NOTES PAYABLE - BANK

As of June 30, 2007 the Organization had a 90 day note due United Bank with interest at an annual rate of 6.75% for the purchase of a vehicle for the Transition to Independence Grant program. The note was paid in full August 28, 2007 from grant funds.

As of June 30, 2008 the Organization had a promissory note due United Bank with interest at an annual rate of 6.25% for the purchase of a vehicle for the Transition to Independence Grant program. The note was paid in full October 21, 2008 from grant funds.

NOTE 4 - LONG-TERM DEBT

Notes payable at June 30, 2008 and 2007 are summarized as follows:

	2008	2007
Chase Bank - original face $20,834, payable in 60 monthly installments of $422 including interest at a rate of 7.80% secured by a vehicle with a book value of $10,909 at June 30, 2008, due November, 2011.	$ 9,850	$ 14,451
United Bank - original face $27,108 payable in 55 monthly installments of $576 including interest at an annual rate of 6.75%, secured by a vehicle with a book value of $ 14,185 as of June 30, 2008, due September, 2010.	14,368	20,073
United Bank - original face $33,483 payable in 48 monthly installments of $798 including interest at an annual rate of 6.65% secured by a vehicle with a book value of $30,134 as of June 30, 2008 due July, 2012.	33,483	-0-
Total	57,701	34,524
Less: Current Portion	15,359	9,705
Long -term Portion	$ 42,342	$ 24,819

Following are maturities of long-term debt for each of the next five years and in aggregate:

Year Ending June 30,	2009	$ 15,359
	2010	17,614
	2011	14,712
	2012	9,218
	2013	798
Total		$ 57,701

Interest expense for the years ended June 30, 2008 and 2007 amounted to $1,714 and $3,076, respectively.

NOTE 5 - CONCENTRATION OF CREDIT RISK

Stepping Stones, Inc. is a non-profit organization that provides residential and living support services to adolescent boys under license with the West Virginia Department of Health and Human Services. The Organization provides services according to contractual agreements with WV/DHHR. The accounts receivable from such contractual agreements are unsecured and been adjusted for all known uncollectible accounts.

NOTE 6 - RETIREMENT PLAN

Stepping Stones, Inc. sponsors a "simple" retirement plan for the benefit of its employees. Under the provisions of the Plan, each eligible employee can, at his/her discretion, defer up to $10,500 of their salary into the plan each year. Stepping Stones, Inc. is required to match the employee's contribution in an amount not to exceed 3% of the employee's compensation or the salary deferral amount, whichever is less. All funds are invested with a professional money-manager and are self-directed by the employee in a variety of securities offered by the money-manager. All contributions of the employee and matching contributions by Stepping Stones, Inc. are fully vested to the employee at the date of contribution. The amount of retirement expense was $6,868 and $8,138 for the years ended June 30, 2008 and 2007.

NOTE 7 - LEASES

Stepping Stones, Inc. leases real property under operating leases on a year to year basis. Certain operating leases provide for renewal options. In the normal course of business, operating leases are generally renewed or replaced by other leases. In addition, Stepping Stones, Inc. leases equipment on a monthly basis. Rental expense charged to operations under operating leases for the years ended June 30, 2008 and 2007 amounted to $30,012 and $12,038, respectively.

NOTE 8 - CONTINGENT LIABILITY

Findings from an administrative services audit conducted in December, 2007 resulted in a potential disallowance of Medicaid funding of approximately $32,000 Stepping Stones, Inc. has filed an appeal of these findings with the Bureau of Medicaid Services. No amount has been accrued in these financial statements as the outcome of this matter is uncertain and the amount of a settlement cannot be reasonably established at this time.

NOTE 9 - RESTATEMENT OF PRIOR PERIOD FINANCIAL STATEMENTS

Financial statements for the years ended June 30, 2006 and 2005 have been restated to correct under-reported revenue from the Community Based Teams Start-up Grant. The correction decreases the change in unrestricted net assets by $6,018 for the year ended June 30, 2006. The cumulative effect of the correction on net assets is an increase of $19,018 as of June 30, 2005.

Various financial statement line items are effected by the change as follows:

	2007	2006
Deferred revenue	$ -0-	$ (13,000)
Total current liabilities	-0-	(13,000)
Total liabilities	-0-	(13,000)
Net assets, unrestricted	(13,000)	(13,000)
Revenue - Community Based Teams	-0-	(6,018)
Total unrestricted support and revenue	-0-	(6,018)
Change in unrestricted net assets	-0-	(6,018)
Net assets at beginning of year	13,000	19,018
Net assets at end of year	13,000	13,000

ADDITIONAL INFORMATION

STEPPING STONES, INC.
SCHEDULES OF FUNCTIONAL EXPENSES
YEARS ENDED JUNE 30, 2008 AND 2007

	2008					
	Program Services				Supporting Services	
	Child Care	Community Based Teams	Youth Transition to Independence	Total Program	Management and General	Total
Salaries and wages	$ 311,956	$ -0-	$ 76,786	$ 388,742	$ 128,918	$ 517,660
Employee benefits	86,726	-0-	21,471	108,197	34,767	142,964
Medicaid tax	12,908	-0-	-0-	12,908	-0-	12,908
Professional fees	42,742	550	1,235	44,527	-0-	44,527
Dietary	59,119	-0-	6,316	65,435	-0-	65,435
Housekeeping	3,614	-0-	-0-	3,614	-0-	3,614
Educational materials	-0-	-0-	40,247	40,247	-0-	40,247
Youth personal expense	49,846	1,645	12,358	63,849	-0-	63,849
Supplies	4,245	-0-	3,886	8,131	-0-	8,131
Insurance	-0-	-0-	-0-	-0-	21,709	21,709
Utilities and telephone	23,048	-0-	9,870	32,918	11,597	44,515
Maintenance and repairs	42,581	-0-	-0-	42,581	-0-	42,581
Transportation	25,946	-0-	2,430	28,376	-0-	28,376
Staff travel	20	-0-	2,077	2,097	-0-	2,097
Conferences and training	16,204	471	20,654	37,329	-0-	37,329
Depreciation	13,308	-0-	12,528	25,836	31,056	56,892
Other	1,618	247	34,825	36,690	34,617	71,307
Interest	-0-	-0-	-0-	-0-	1,714	1,714
Rent	-0-	-0-	26,400	26,400	3,612	30,012
Total	$ 693,881	$ 2,913	$ 271,083	$ 967,877	$ 267,990	$1,235,867

STEPPING STONES, INC.
SCHEDULES OF FUNCTIONAL EXPENSES
YEARS ENDED JUNE 30, 2008 AND 2007

2007					
Program Services				Supporting Services	
Child Care	Community Based Teams	Next Step	Total Program	Management and General	Total
$ 367,572	$ 11,424	$ 3,363	$ 382,359	$ 124,318	$ 506,677
103,733	2,582	328	106,643	35,084	141,727
11,716	-0-	-0-	11,716	-0-	11,716
37,698	8,048	-0-	45,746	-0-	45,746
49,037	-0-	-0-	49,037	-0-	49,037
3,052	-0-	-0-	3,052	-0-	3,052
40,609	1,598	-0-	42,207	-0-	42,207
4,911	-0-	625	5,536	-0-	5,536
22,368	-0-	-0-	22,368	5,467	27,835
27,538	-0-	354	27,892	6,731	34,623
27,530	-0-	-0-	27,530	6,728	34,258
14,575	-0-	-0-	14,575	-0-	14,575
-0-	882	755	1,637	-0-	1,637
11,942	4,931	540	17,413	-0-	17,413
33,410	-0-	4,376	37,786	8,165	45,951
35,268	5,466	21,424	62,158	8,315	70,473
2,472	-0-	-0-	2,472	604	3,076
5,438	-0-	6,600	12,038	-0-	12,038
-0-	-0-	-0-	-0-	25,507	25,507
$ 798,869	$ 34,931	$ 38,365	$ 872,165	$ 220,919	$1,093,084

STEPPING STONES, INC.
SCHEDULE OF EXPENDITURES OF FEDERAL AND STATE AWARDS
YEAR ENDED JUNE 30, 2008

Federal Funds Pass-Through Grantor Program Title	Federal CFDA Number	Program From	Period To
Department of Health and Human Services			
Pass Through-State of West Virginia, West Virginia Department of Health and Human Resources			
Foster Care - Title IV-E	93.658	07/01/07	06/30/08
Community Based Teams	93.556	07/01/07	06/30/08
Department of Agriculture			
Pass Through-State of West Virginia, West Virginia Department of Education			
School Breakfast Program	10.553	07/01/07	06/30/08
National School Lunch Program	10.555	07/01/07	06/30/08
Total Federal Awards			
State Funds			
WV Department of Health & Human Resources			
Youth Transition to Independence	93.958	07/01/07	06/30/08
Total State Awards			

Program or Award Amount	Receipts or Revenue Recognized	Disbursement/ Expenditures	
$ 809,382	$ 809,382	$ 691,237	
$ 15,000	$ 15,000	$ 2,913	
$ 5,157	$ 5,157	$ 5,157	
$ 9,755	$ 9,955	$ 9,755	
	$ 839,294	$ 709,062	
$ 498,661	$ 313,498	$ 293,369	*
	$ 313,498	$ 293,369	

* In accordance with the grant award budget, expenditures for property and equipment are expensed in the period in which the expenditure is made as opposed to being capitalized and depreciated over the assets estimated useful lives.

INDEPENDENT AUDITOR'S REPORTS ON COMPLIANCE AND ON INTERNAL CONTROL

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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*

Board of Directors
Stepping Stones, Inc.
Lavalette, West Virginia

We have audited the financial statements of Stepping Stones, Inc. (a nonprofit organization) as of and for the year ended June 30, 2008, and have issued our report thereon dated December 5, 2008. 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 Stepping Stones, Inc.'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 Stepping Stones, Inc.'s internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Organizations internal control over financial reporting.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the organization's ability to initiate, authorize, record, process, or report financial data reliability in accordance with generally accepted accounting principals, such that there is more than a remote likelihood that a misstatement of the organization's financial statements that is more than inconsequential will not be prevented or detected by the organization's internal controls. We consider the deficiencies described in the accompanying schedule of findings and questioned costs to be significant deficiencies in internal control over financial reporting. See findings 08-1 and 08-2.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the organization's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we consider item 08-1to be a material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Stepping Stones, Inc.'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 that are required to be reported under *Government Auditing Standards*.

Stepping Stones, Inc.'s response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit Stepping Stones, Inc.'s response, and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the 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 the specified parties.

Ware & Hall PLLC

Huntington, West Virginia
December 5, 2008

Ware & Hall, PLLC

Certified Public Accountants

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

Board of Directors
Stepping Stones, Inc.
Lavalette, West Virginia

Compliance

We have audited the compliance of Stepping Stones, Inc. (a nonprofit organization) with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2008. Stepping Stones, Inc.'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 Stepping Stones, Inc.'s management. Our responsibility is to express an opinion on Stepping Stones, Inc.'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 Stepping Stones, Inc.'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 Stepping Stones, Inc.'s compliance with those requirements.

In our opinion, Stepping Stones, Inc. complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2008.

Internal Control Over Compliance

The management of Stepping Stones, Inc. 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 Stepping Stones, Inc.'s internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, 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 Stepping Stones, Inc.'s internal control over compliance.

A control deficiency in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely effects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiency's that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be 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 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.

Ware & Hall PLLC

Ware and Hall, PLLC
Huntington, West Virginia
December 5, 2008

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

STEPPING STONES, INC.
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2008

2007 FINDING NO: 07-1

Condition: Several audit entries were required at year-end and in the interim, thus management was unable to produce financial statements presented in accordance with generally accepted accounting principals.

Recommendation: Strengthen review procedures that would reconcile general ledger accounts with supporting documentation to ensure that transactions are recorded completely, timely, and accurately.

Status: Management has not implemented the recommendation. The finding has been repeated as 08-1.

2007 FINDING NO: 07-2

Condition: The accounting functions lack a proper segregation of duties in regard to receiving and disbursing of funds.

Recommendation: Review current duties of management staff and make changes where possible or develop compensating controls.

Status: Management has implemented several compensating controls and has partially complied with the recommendation. The finding has been repeated as 08-2.

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

STEPPING STONES, INC.
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2008

A. SUMMARY OF AUDITOR'S RESULTS

1) The independent auditor's report expresses an unqualified opinion on the financial statements of Stepping Stones, Inc. for the year ended June 30, 2008.

2) Two significant deficiencies were noted during the audit of the financial statements of Stepping Stones, Inc. for the year ended June 30, 2008. Significant deficiency 08-1 was considered to be a material weakness.

3) No instance of noncompliance which may be material to the financial statements of Stepping Stones, Inc. for the year ended June 30, 2008 was noted during the audit.

4) No significant deficiencies were identified during the audit of the major federal award programs of Stepping Stones, Inc. for the year ended June 30, 2008.

5) The independent auditor's report on compliance for the major federal award programs for Stepping Stones, Inc. for the year ended June 30, 2008 expresses an unqualified opinion.

6) No audit findings were identified which are required to be reported under §510(a) of OMB Circular A-133.

7) The following programs were tested as a major program:

Program	CFDA#
Department of Health and Human Services	
Foster Care - Title IV-E	93.658
West Virginia Department of Health and Human Resources	
Youth Transition to Independence	93.958

8) The threshold for distinguishing type A and B programs was the greater of $300,000 or 3% of total federal awards expended by Stepping Stones, Inc. for the year ended June 30, 2008.

9) Stepping Stones, Inc. has not qualified as a low risk auditee under §.530 of OMB Circular A-133 for the year ended June 30, 2008.

STEPPING STONES, INC.
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2008

B. FINDINGS - FINANCIAL STATEMENT AUDIT

- **SIGNIFICANT DEFICIENCIES:**

08-1 Reconciliation of Accounting Records to Supporting Documentation

Condition: Several audit adjusting entries were required to be made to the Organization's accounting records to reflect accurate balances in the Organization's assets, liabilities, revenues and expenses. Adjusting entries were also required in the interim in order to prepare the semi-annual cost reports. Various general ledger balances were not properly reconciled to the supporting documentation.

Criteria: One of the objectives of an internal control system is to provide management with reasonable assurance that transactions are recorded properly to permit the preparation of financial statements in accordance with accounting principals generally accepted in the United States of America. In addition, timely, accurate and complete financial reporting is an essential management tool in monitoring and controlling operations.

Effect: This results in an inaccurate and incomplete presentation of the financial position, results of operations, and cash flows of the Organization. Management therefore, is unable to produce financial statements presented in accordance with generally accepted accounting principals.

Recommendation: Review procedures should be strengthened which would include reconciliation of the general ledger accounts with supporting documentation to ensure that transactions are recorded completely, timely, and accurately in order to prepare financial statements in accordance with generally accepted accounting principals. This finding was also noted in the prior year's audit.

07-2 Segregation of Duties

Condition: Although various compensating controls and oversight has been implemented, the Organization lacks actual segregation of duties within the accounting department.

Criteria: Proper internal controls require separation of duties between the recording of the transaction and the custody of the related assets.

Cause: The Organization has a limited number of employees which makes segregation of duties difficult.

Recommendation: Review current duties of administrative staff and make changes where possible or strengthen compensating controls where segregation is not possible.

- **Noncompliance Findings**

None

C. FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAM

Department of Health and Human Services

None