

ESPERANÇA, INC.

Financial Statements
and
Independent Auditors' Report

Year Ended September 30, 2018

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Independent Auditors' Report

To the Board of Directors of
Esperança, Inc.
Phoenix, Arizona

Report on the Financial Statements

We have audited the accompanying financial statements of Esperança, Inc. (a nonprofit Organization), which comprise the statement of financial position as of September 30, 2018, and the related statements of activities, functional expenses and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Esperança, Inc. as of September 30, 2018, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Fester & Chapman, PLLC

January 15, 2019

ESPERANÇA, INC.
STATEMENT OF FINANCIAL POSITION
September 30, 2018

ASSETS

| | |
|-----------------------------|----------------------------|
| Current assets: | |
| Cash | \$ 353,901 |
| Prepaid expenses | <u>21,327</u> |
| Total current assets | 375,228 |
| Investments | 3,101,948 |
| Property and equipment, net | <u>165,398</u> |
| Total assets | <u><u>\$ 3,642,574</u></u> |

LIABILITIES AND NET ASSETS

| | |
|----------------------------------|----------------------------|
| Current liabilities: | |
| Accounts payable | \$ 2,961 |
| Accrued expenses | <u>22,176</u> |
| Total current liabilities | 25,137 |
| Net assets: | |
| Unrestricted | 479,871 |
| Board designated | <u>2,139,553</u> |
| Total unrestricted net assets | 2,619,424 |
| Temporarily restricted | 138,333 |
| Permanently restricted | <u>859,680</u> |
| Total net assets | <u>3,617,437</u> |
| Total liabilities and net assets | <u><u>\$ 3,642,574</u></u> |

The accompanying notes are an integral part of these statements.

ESPERANÇA, INC.
STATEMENT OF ACTIVITIES
For the Year Ended September 30, 2018

| | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>Permanently Restricted</u> | <u>Totals</u> |
|---|---------------------|-----------------------------------|-----------------------------------|---------------------|
| Support and revenue: | | | | |
| Contributions | \$ 1,275,686 | \$ 163,969 | | \$ 1,439,655 |
| Donated services | 2,875,362 | | | 2,875,362 |
| Donated materials | 1,802,447 | | | 1,802,447 |
| Interest and dividends | 44,671 | | | 44,671 |
| Net gains on investments | 120,008 | | | 120,008 |
| Net assets released from restrictions | <u>105,085</u> | <u>(105,085)</u> | | |
| | <u>6,223,259</u> | <u>58,884</u> | | <u>6,282,143</u> |
| Special event revenue | 108,762 | | | 108,762 |
| Less: Costs of direct benefits to donors | <u>(23,346)</u> | | | <u>(23,346)</u> |
| Net revenues from special events | <u>85,416</u> | | | <u>85,416</u> |
| Total support and revenue | <u>6,308,675</u> | <u>58,884</u> | | <u>6,367,559</u> |
| Expenses: | | | | |
| Public health and medical program services | 5,706,836 | | | 5,706,836 |
| Supporting services: | | | | |
| Management and general | 228,872 | | | 228,872 |
| Fundraising | <u>272,062</u> | | | <u>272,062</u> |
| Total supporting services | <u>500,934</u> | | | <u>500,934</u> |
| Total expenses | <u>6,207,770</u> | | | <u>6,207,770</u> |
| Change in net assets | 100,905 | 58,884 | | 159,789 |
| Net assets, beginning of year | <u>2,518,519</u> | <u>79,449</u> | <u>\$ 859,680</u> | <u>3,457,648</u> |
| Net assets, end of year | <u>\$ 2,619,424</u> | <u>\$ 138,333</u> | <u>\$ 859,680</u> | <u>\$ 3,617,437</u> |

The accompanying notes are an integral part of these statements.

ESPERANÇA, INC.
STATEMENT OF FUNCTIONAL EXPENSES
For the Year Ended September 30, 2018

| | Public Health and Medical Program Services | Supporting Services | | | Total |
|------------------------------------|---|---------------------------|-------------------|---------------------------------|---------------------|
| | | Management and General | Fundraising | Total Supporting Services | |
| Payroll and related expenses: | | | | | |
| Salaries | \$ 247,988 | \$ 136,116 | \$ 100,776 | \$ 236,892 | \$ 484,880 |
| Employee benefits | 41,213 | 22,627 | 16,970 | 39,597 | 80,810 |
| Payroll taxes | 20,107 | 11,040 | 8,280 | 19,320 | 39,427 |
| Total payroll and related expenses | 309,308 | 169,783 | 126,026 | 295,809 | 605,117 |
| Donated services | 2,875,362 | | | | 2,875,362 |
| Donated materials | 1,815,982 | | | | 1,815,982 |
| Grants to other organizations | 515,855 | | | | 515,855 |
| Supplies | 2,818 | 1,562 | 1,458 | 3,020 | 5,838 |
| Professional fees | 30,527 | 27,471 | 67,500 | 94,971 | 125,498 |
| Printing and copying | 2,746 | 1,694 | 29,249 | 30,943 | 33,689 |
| Travel | 56,807 | 49 | 11,734 | 11,783 | 68,590 |
| Postage and shipping | 26,580 | 703 | 6,640 | 7,343 | 33,923 |
| Domestic events and services | 19,553 | | | | 19,553 |
| Repairs and maintenance | 6,519 | 3,579 | 2,684 | 6,263 | 12,782 |
| Insurance | 5,797 | 3,183 | 2,387 | 5,570 | 11,367 |
| Telecommunications | 2,431 | 1,334 | 6,614 | 7,948 | 10,379 |
| Conferences and meetings | 3,611 | 918 | 1,228 | 2,146 | 5,757 |
| Utilities | 4,213 | 2,313 | 1,735 | 4,048 | 8,261 |
| Dues and subscriptions | 1,786 | 1,221 | 3,500 | 4,721 | 6,507 |
| Board | | 1,500 | | 1,500 | 1,500 |
| Banking fees | 8,312 | 4,557 | 3,561 | 8,118 | 16,430 |
| Other | 15,614 | 7,349 | 6,504 | 13,853 | 29,467 |
| Depreciation | 3,015 | 1,656 | 1,242 | 2,898 | 5,913 |
| Total expenses | <u>\$ 5,706,836</u> | <u>\$ 228,872</u> | <u>\$ 272,062</u> | <u>\$ 500,934</u> | <u>\$ 6,207,770</u> |

The accompanying notes are an integral part of these statements.

ESPERANÇA, INC.
STATEMENT OF CASH FLOWS
For the Year Ended September 30, 2018

| | |
|---|--------------------------|
| Cash flows from operating activities: | |
| Change in net assets | \$ 159,789 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | |
| Depreciation | 5,913 |
| Net gains on investments | (120,008) |
| Distributions of donated inventory | 13,535 |
| Change in: | |
| Prepaid expenses | 1,400 |
| Accounts payable | (12,821) |
| Accrued expenses | <u>(3,249)</u> |
| Net cash provided by operating activities | <u>44,559</u> |
| | |
| Cash flows from investing activities: | |
| Proceeds from sales of investments | 255,000 |
| Purchases of investments | <u>(50,549)</u> |
| Net cash provided by investing activities | <u>204,451</u> |
| | |
| Change in cash | 249,010 |
| | |
| Cash, beginning of year | <u>104,891</u> |
| | |
| Cash, end of year | <u><u>\$ 353,901</u></u> |

The accompanying notes are an integral part of these statements.

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018

NOTE 1 - BACKGROUND AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Esperança, Inc. (the Organization) is an international 501(c)(3) nonprofit organization incorporated in Arizona, which provides sustainable public health programs and volunteer surgical missions that reach more than 100,000 people annually in Bolivia, Mozambique, Nicaragua, Peru, and the United States of America. Major funding sources are from direct public contributions, bequests, and grants.

The significant accounting policies of the Organization follow:

Basis of Accounting: The financial statements of the Organization have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP). Under this method of accounting, revenue and expenses are identified with specific periods of time and are recorded as earned and incurred, respectively, without regard to the date of receipt or payment.

Basis of Presentation: Financial statement presentation follows the recommendations of the Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) topic of *Not-for-Profit Entities*, requiring the Organization to report 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.

Use of Estimates: In preparing financial statements in conformity with GAAP, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Investments: The Organization follows the provisions of FASB ASC's topic of *Not-for-Profit Entities* regarding its investments. Management has estimated the fair value of its investments using available market information and other valuation methodologies as described in Note 3. The estimates are based on pertinent information available to management as of September 30, 2018. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, current estimates of fair value may differ significantly from the amounts in the financial statements.

Property and Equipment: Property and equipment are stated at cost, or at their estimated fair value at the date of donation. Property and equipment costing \$5,000 or more is capitalized. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets as follows:

| | |
|------------------------------------|----------|
| Buildings | 25 years |
| Furniture, fixtures, and equipment | 5 years |

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018

NOTE 1 - BACKGROUND AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES -
Continued

Donated Services: Donated services are recognized at fair value as contributions and expenses if the services (a) create or enhance nonfinancial assets, or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased by the Organization. Many individuals during the year volunteered their time in support of the Organization's programs, but did not meet the above criteria, so no donated services were recorded for their efforts. However, the medical professionals who provided free services on volunteer surgical missions do meet that criteria, and the fair value of those services are based on rates that would have been charged to paying patients.

Donated Materials: Donated materials are recognized in the financial statements on the date received at their estimated fair value. Donated materials received by the Organization were recorded as an in-kind contributions and as program expenses.

Income Taxes: The Organization is exempt from federal and state income taxes as an organization other than a private foundation under Section 501(c)(3) of the Internal Revenue Code and similar state provisions.

Contributions: Contributions are reported in accordance with the FASB ASC topic of *Not-for-Profit Entities*. Contributions are recognized when the donor makes a pledge to give that is, in substance, an unconditional promise. Contributions are recorded as unrestricted, temporarily restricted, or permanently restricted depending on the nature of donor restrictions and depending on whether the restrictions are met in the current fiscal period. Restricted contributions are reported as increases in unrestricted net assets if the restrictions have been met in the current fiscal period. If the restriction has not been met by fiscal year end, the amount is reported as an increase in temporarily restricted net assets. When the restriction is met on a contribution received in a prior fiscal period, the amount is shown as a reclassification of restricted net assets to unrestricted net assets.

Expense Allocation: The costs of providing various programs and other activities have been summarized on a functional basis in the Statement of Activities, and allocated among program and supporting services benefited in the Statement of Functional Expenses.

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018

NOTE 2 - CONCENTRATION OF CREDIT RISK

The Organization maintains its cash and investment accounts at financial institutions that may at times exceed the limits insured by the Federal Deposit Insurance Corporation (FDIC), or covered under Securities Investor Protection Corporation (SIPC). The Organization has not incurred losses related to uninsured balances, and manages this risk by maintaining its deposits in multiple financial institutions.

NOTE 3 - INVESTMENTS AND FAIR VALUE MEASUREMENTS

Fair value measurements are determined based on assumptions that market participants would use in pricing assets and liabilities. GAAP establishes a fair value hierarchy that distinguishes between market participant assumptions and the Organization's own assumptions about market participant assumptions. Observable inputs are assumptions based on market data obtained from independent sources; while unobservable inputs are the Organization's own assumptions about what market participants would assume based on the best information available in the circumstance.

Level 1 inputs – A quoted price in an active market for an identical asset or liability is considered to be the most reliable evidence of fair value.

Level 2 inputs – These are observable inputs, either directly or indirectly, other than quoted prices included within Level 1. The Organization does not currently have any investments valued based on Level 2 inputs.

Level 3 inputs – These inputs are unobservable and are used to measure fair value only when observable inputs are not available. The Organization does not currently have any investments valued based on Level 3 inputs.

The Organization's interest and dividends are presented in the Statement of Activities for the year ended September 30, 2018. The Organization's net gains on investments included the following for the year ended September 30, 2018:

| | |
|--------------------------|--------------------------|
| Realized gains | \$ 227,174 |
| Unrealized losses | <u>(107,166)</u> |
| Net gains on investments | <u><u>\$ 120,008</u></u> |

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018

NOTE 3 - INVESTMENTS AND FAIR VALUE MEASUREMENTS - Continued

The fair value of assets measured as Level 1 inputs on a recurring basis at September 30, 2018 were as follows:

| | <u>Level 1</u> |
|------------------------------|--------------------|
| Investments: | |
| Money market | \$ 26,009 |
| Certificates of deposit | 1,053,072 |
| Exchange-traded funds: | |
| Diversified emerging markets | 163,385 |
| Foreign large blend | 461,448 |
| Large blend | 708,300 |
| Small blend | 157,426 |
| Mutual funds: | |
| Diversified emerging markets | 45,575 |
| Foreign large blend | 59,717 |
| Foreign large growth | 61,075 |
| Large growth | 97,261 |
| Large value | 94,078 |
| Mid-cap value | 10,913 |
| Money market - taxable | 130,832 |
| Small growth | 21,728 |
| Small value | 11,129 |
| Total investments | <u>\$3,101,948</u> |

NOTE 4 - PROPERTY AND EQUIPMENT, NET

Property and equipment consisted of the following at September 30, 2018:

| | |
|-----------------------------------|-------------------|
| Land | \$ 32,918 |
| Buildings | 325,722 |
| Furniture, fixtures and equipment | 21,601 |
| | 380,241 |
| Accumulated depreciation | (214,843) |
| | <u>\$ 165,398</u> |

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018

NOTE 5 - TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consisted of the following at September 30, 2018:

| | |
|---------------------------|-------------------|
| Peru Medical Restrictions | \$ 43,069 |
| Nicaragua Restrictions | 20,000 |
| Nicaragua Medical | 10,000 |
| Domestic Programs | <u>65,264</u> |
| | <u>\$ 138,333</u> |

Temporarily restricted net assets released from purpose restrictions consisted of the following for year ended September 30, 2018:

| | |
|---------------------------|-------------------|
| Peru Medical Restrictions | \$ 22,957 |
| Nicaragua Restrictions | 10,261 |
| Domestic Programs | <u>71,867</u> |
| | <u>\$ 105,085</u> |

NOTE 6 - ENDOWMENTS

The Organization's endowments include board-designated (unrestricted) net assets totaling \$2,139,553, and permanently restricted net assets totaling \$859,680, at September 30, 2018. The board-designated endowment includes amounts that the Organization's Board of Directors has set aside for various domestic and international programs.

Permanently restricted net assets consisted of resources that must be invested in perpetuity. The income from the resources can be used to support the Organization's activities. Permanently restricted net assets consisted of the following at September 30, 2018:

| | |
|-------------------|-------------------|
| Domestic programs | \$ 470,913 |
| General endowment | 363,574 |
| Wargel endowment | <u>25,193</u> |
| | <u>\$ 859,680</u> |

Interpretation of Relevant Law: The Organization's endowment funds are subject to compliance with the State of Arizona's version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) which provides standards for managing investments of institutional funds and spending from endowments. The Organization's Board of Directors has interpreted UPMIFA as requiring the classification of the original value of gifts donated to permanent donor-restricted endowments, and the original value of subsequent gifts to those permanent endowments as permanently restricted net assets.

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018

NOTE 6 - ENDOWMENTS - Continued

Return Objectives and Risk Parameters: The Organization's endowment funds are invested with Morgan Stanley in long-term investment pools in order to achieve return objectives and to maintain appropriate risk parameters approved by the Organization's Board of Directors.

Strategies Employed for Achieving Objectives: The Organization's Board of Directors has appointed a finance committee to oversee the management of the Organization's endowments. The finance committee meets with management periodically to review asset allocations, manager and investment entity performance, anticipated additions to or transfers of funds, and future investment strategies.

Spending Policy: In accordance with the Organization's policy, income earned from the permanently restricted net assets may be used for operations unless otherwise restricted. From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or UPMIFA requires the Organization to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature would be reported as unrestricted net assets.

Activity of the endowment funds for the year ended September 30, 2018 is as follows:

| | Unrestricted Net Assets | Temporarily Restricted Net Assets | Permanently Restricted Net Assets | Total |
|--|----------------------------|---|---|---------------------|
| Endowment net assets, beginning of year | \$ 2,139,553 | | \$ 859,679 | \$ 2,999,232 |
| Investment income | | \$ 45,627 | | 45,627 |
| Distributions appropriated for expenditure | 45,627 | (45,627) | | |
| Expenditures of investment income | (45,627) | | | (45,627) |
| Endowment net assets, end of year | <u>\$ 2,139,553</u> | | <u>\$ 859,679</u> | <u>\$ 2,999,232</u> |

NOTE 7 - RETIREMENT PLAN

The Organization established a 401(k) plan in 2002, which covers substantially all permanent full-time employees. Plan contributions are discretionary and determined annually by the Board of Directors. Contribution costs for the plan are expensed when incurred and funded annually. Plan contributions for the year ended September 30, 2018 were \$21,891 and are included in employee benefits expense on the Statement of Functional Expenses.

NOTE 8 - SUBSEQUENT EVENTS

The Organization has evaluated subsequent events through January 15, 2019, the date which the financial statements were available to be issued, and has concluded that no events have occurred since September 30, 2018, that would require an adjustment to or disclosure in the financial statements.