

ESPERANÇA, INC.

Financial Statements
and
Independent Auditors' Report

Year Ended September 30, 2016

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Independent Auditors' Report

To the Board of Directors
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, 2016, 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, 2016, 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 P.C.

January 18, 2017

ESPERANÇA, INC.
STATEMENT OF FINANCIAL POSITION
September 30, 2016

ASSETS

Current assets:	
Cash	\$ 37,515
Contributions receivable	25,000
Prepaid expenses	15,988
Inventory	<u>246,843</u>
Total current assets	325,346
Investments	3,308,481
Loan receivable	158,640
Property and equipment, net	<u>178,234</u>
Total assets	<u><u>\$ 3,970,701</u></u>

LIABILITIES AND NET ASSETS

Current liabilities:	
Accounts payable	\$ 8,290
Accrued expenses	32,444
Deferred revenue	<u>1,000</u>
Total current liabilities	41,734
Net assets:	
Unrestricted	866,744
Board designated	<u>1,200,001</u>
Total unrestricted net assets	2,066,745
Temporarily restricted	25,000
Permanently restricted	<u>1,837,222</u>
Total net assets	<u>3,928,967</u>
Total liabilities and net assets	<u><u>\$ 3,970,701</u></u>

The accompanying notes are an integral part of these statements.

ESPERANÇA, INC.
STATEMENT OF ACTIVITIES
For the Year Ended September 30, 2016

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Totals</u>
Support and revenue:				
Contributions	\$ 952,177	\$ 25,000		\$ 977,177
Donated services	2,020,080			2,020,080
Donated materials	2,377,782			2,377,782
Interest and dividends	58,624			58,624
Gains on investments	231,178			231,178
Net assets released from restrictions	<u>102,589</u>	<u>(102,589)</u>		
	<u>5,742,430</u>	<u>(77,589)</u>		<u>5,664,841</u>
Special event revenue	72,814			72,814
Less: Costs of direct benefits to donors	<u>(14,763)</u>			<u>(14,763)</u>
Net revenues from special events	<u>58,051</u>			<u>58,051</u>
Total support and revenue	<u>5,800,481</u>	<u>(77,589)</u>		<u>5,722,892</u>
Expenses:				
Public health and medical program services	5,061,309			5,061,309
Supporting services:				
Management and general	221,343			221,343
Fundraising	<u>288,876</u>			<u>288,876</u>
Total supporting services	<u>510,219</u>			<u>510,219</u>
Total expenses	<u>5,571,528</u>			<u>5,571,528</u>
Change in net assets	228,953	(77,589)		151,364
Net assets, beginning of year	<u>1,837,792</u>	<u>102,589</u>	<u>\$ 1,837,222</u>	<u>3,777,603</u>
Net assets, end of year	<u>\$ 2,066,745</u>	<u>\$ 25,000</u>	<u>\$ 1,837,222</u>	<u>\$ 3,928,967</u>

The accompanying notes are an integral part of these statements.

ESPERANÇA, INC.
STATEMENT OF FUNCTIONAL EXPENSES
For the Year Ended September 30, 2016

	Public Health and Medical Program Services	Supporting Services			Total
		Management and General	Fundraising	Total Supporting Services	
Payroll:					
Salaries	\$ 279,822	\$ 147,156	\$ 140,777	\$ 287,933	\$ 567,755
Employee benefits	64,422	33,976	32,276	66,252	130,674
Payroll taxes	22,509	11,871	11,278	23,149	45,658
Total payroll	366,753	193,003	184,331	377,334	744,087
Donated services	2,020,080				2,020,080
Donated materials	2,148,172				2,148,172
Grants to other organizations	377,069				377,069
Supplies	2,885	1,088	2,128	3,216	6,101
Professional fees	5,466	2,461	20,873	23,334	28,800
Printing and copying	22,525	528	7,903	8,431	30,956
Travel	50,968	454	9,430	9,884	60,852
Postage and shipping	2,332	1,186	32,470	33,656	35,988
Domestic events and services	9,090				9,090
Repairs and maintenance	6,977	3,679	3,495	7,174	14,151
Insurance	6,093	3,213	3,053	6,266	12,359
Telecommunications	2,051	1,082	7,047	8,129	10,180
Conferences and meetings	4,098	995	2,699	3,694	7,792
Utilities	4,259	2,246	2,134	4,380	8,639
Dues and subscriptions	2,776	1,625	3,648	5,273	8,049
Board	8,762	4,621	4,410	9,031	17,793
Contract labor	10,917				10,917
Banking fees	6,682	3,524	3,347	6,871	13,553
Other	1,054	425	756	1,181	2,235
Depreciation	2,300	1,213	1,152	2,365	4,665
	<u>\$ 5,061,309</u>	<u>\$ 221,343</u>	<u>\$ 288,876</u>	<u>\$ 510,219</u>	<u>\$ 5,571,528</u>

The accompanying notes are an integral part of these statements.

ESPERANÇA, INC.
STATEMENT OF CASH FLOWS
For the Year Ended September 30, 2016

Cash flows from operating activities:	
Change in net assets	\$ 151,364
Adjustments to reconcile change in net assets to net cash used for operating activities:	
Depreciation	4,665
Gains on investments	(231,178)
Donated inventory	(229,610)
Change in:	
Contributions receivable	33,682
Prepaid expenses	1,842
Accounts payable	(33,610)
Accrued expenses	11,753
Deferred revenue	<u>(3,250)</u>
Net cash used for operating activities	<u>(294,342)</u>
Cash flows from investing activities:	
Proceeds from sales of investments	509,447
Purchases of investments	(58,615)
Purchases of property and equipment	(80,272)
Net advances on loan receivable	<u>(105,759)</u>
Net cash provided by investing activities	<u>264,801</u>
Change in cash	(29,541)
Cash, beginning of year	<u>67,056</u>
Cash, end of year	<u><u>\$ 37,515</u></u>

The accompanying notes are an integral part of these statements.

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2016

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.

Inventory: Inventory, which consists primarily of donated medical supplies and equipment, is stated at the estimated fair value on the date received.

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, 2016. 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 statements presented.

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2016

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

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

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 contribution and as a program expense, except for donated materials that were in the possession of the Organization as of September 30, 2016. Those donated materials are reported as inventory on the statement of financial position as of September 30, 2016.

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, 2016

NOTE 2 - CONCENTRATION OF CREDIT RISK

The Organization maintains its cash accounts at a financial institution that may at times exceed the limits insured by the Federal Deposit Insurance Corporation (FDIC). The Organization has not incurred losses related to uninsured balances, and manages this risk by maintaining its deposits in a national financial institution.

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, 2016. The Organization's gains on investments included the following for the year ended September 30, 2016:

Realized gains	\$ 73,620
Unrealized gains	<u>157,558</u>
Total gains on investments	<u><u>\$ 231,178</u></u>

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2016

NOTE 3 - INVESTMENTS AND FAIR VALUE MEASUREMENTS - Continued

The following were the fair value of assets measured as Level 1 inputs on a recurring basis at September 30, 2016:

	<u>Level 1</u>
Investments:	
Money market	\$ 121,345
Certificates of deposit	1,177,033
Exchange-traded funds:	
Diversified emerging mkts	84,291
Foreign large blend	466,063
Global real estate	68,527
Large blend	746,233
Real estate	67,397
Small blend	165,323
Mutual funds:	
Large blend	76,981
Large growth	186,065
Large value	103,641
Mid growth	11,049
Mid value	11,119
Small growth	12,123
Small value	11,291
Total investments	<u>\$3,308,481</u>

NOTE 4 - LOAN RECEIVABLE

During the year ended September 30, 2016, the Organization made cash advances of \$105,759 to Esperanza Bolivia, a non-related charitable organization located in Bolivia. The total amount advanced to Esperanza Bolivia at September 30, 2016 was \$158,640. There is no written note or agreement and there is no interest charged on this advance.

NOTE 5 - PROPERTY AND EQUIPMENT, NET

Property and equipment consisted of the following at September 30, 2016:

Land	\$ 32,918
Buildings	325,722
Furniture, fixtures and equipment	21,601
	380,241
Accumulated depreciation	(202,007)
	<u>\$ 178,234</u>

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2016

NOTE 6 - TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consisted of the following at September 30, 2016:

Aetna grant - time restriction	\$ 25,000
	<u>\$ 25,000</u>

Net assets were released from purpose restrictions as follows for the year ended September 30, 2016:

Domestic programs	\$ 90,089
Bolivia programs	<u>12,500</u>
Total temporarily restricted net assets released from restrictions	<u>\$ 102,589</u>

NOTE 7 - PERMANENTLY RESTRICTED NET ASSETS

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, 2016:

Domestic programs	\$ 470,913
General endowment	363,574
Mozambique programs	977,542
Wargel endowment	<u>25,193</u>
	<u>\$1,837,222</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.

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.

ESPERANÇA, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2016

NOTE 7 - PERMANENTLY RESTRICTED NET ASSETS - Continued

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, 2016 is as follows:

	<u>Permanently Restricted Net Assets</u>
Endowment net assets, beginning of year	\$ 1,837,222
Investment income	156,584
Expenditures	<u>(156,584)</u>
Endowment net assets, end of year	<u>\$ 1,837,222</u>

NOTE 8 - 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, 2016 were \$24,194 and are included in employee benefits expense on the Statement of Functional Expenses.

NOTE 9 - SUBSEQUENT EVENTS

The Organization has evaluated subsequent events through January 18, 2017, the date which the financial statements were available to be issued, and has concluded that no events have occurred since September 30, 2016, that would require an adjustment to or disclosure in the financial statements.