

MENDING KIDS INTERNATIONAL

FINANCIAL STATEMENTS

DECEMBER 31, 2014

CONTENTS

Independent Auditors' Report	1-2
Statement of Financial Position	3
Statement of Activities	4
Statement of Functional Expenses	5
Statement of Cash Flows	6
Notes to Financial Statements	7-14

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Mending Kids International

Report on the Financial Statements

We have audited the accompanying financial statements of Mending Kids International (a nonprofit organization), which comprise the Statement of Financial Position as December 31, 2014, 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.

INDEPENDENT AUDITORS' REPORT

continued

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Mending Kids International as of December 31, 2014, 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.

Other Matter

Summarized Comparative Information

We have previously audited Mending Kids International's 2013 financial statements, and we expressed an unmodified opinion on those audited financial statements in our report dated November 10, 2014. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2013, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Harrington Group

Pasadena, California
November 6, 2015

MENDING KIDS INTERNATIONAL

STATEMENT OF FINANCIAL POSITION

December 31, 2014

With comparative totals at December 31, 2013

	2014	2013
Assets		
Current assets		
Cash	\$ 11,777	\$ 267,649
Contributions receivable (Note 2)	59,595	86,850
Investments (Note 3)	2,318,520	2,625,727
Inventory (Note 4)	253,831	-
Artwork held for sale (Note 5)	400,000	-
Other assets	14,500	6,000
	3,058,223	2,986,226
Fixed assets, net (Note 6)	27,470	12,606
Total assets	\$ 3,085,693	\$ 2,998,832
Liabilities and net assets		
Current Liabilities		
Accounts payable	\$ 213,369	\$ 178,580
Accrued liabilities	13,864	41,655
Deferred revenue	60,000	42,000
	287,233	262,235
Total liabilities	287,233	262,235
Commitments (Note 7)		
Net assets		
Unrestricted:		
Undesignated	\$ 1,813,400	\$ 1,802,786
Board-designated (Note 11)	245,733	134,143
Equity in fixed assets - net	27,470	12,606
	2,086,603	1,949,535
Temporarily restricted (Note 8)	711,857	787,062
Total net assets	2,798,460	2,736,597
Total liabilities and net assets	\$ 3,085,693	\$ 2,998,832

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

MENDING KIDS INTERNATIONAL

STATEMENT OF ACTIVITIES

For the year ended December 31, 2014

With comparative totals for the year ended December 31, 2013

	Unrestricted	Temporarily Restricted	2014	2013
Revenue and support				
In-kind contributions (Note 2)	\$ 4,553,456	\$ -	\$ 4,553,456	\$ 3,864,399
Special events income	1,194,755		1,194,755	1,176,174
Contributions	365,576	80,301	445,877	308,340
Investment income (Note 3)	74,969		74,969	79,694
Mission team fees	18,779		18,779	21,200
Other income	6,357		6,357	2,233
Net assets released from program restrictions	155,506	(155,506)	-	-
Total revenue and support	6,369,398	(75,205)	6,294,193	5,452,040
Expenses				
Program services	\$ 5,445,133	\$ -	\$ 5,445,133	\$ 5,356,501
Support services				
Management and general	279,796		279,796	138,855
Fundraising	507,401		507,401	372,806
Total expenses	6,232,330	-	6,232,330	5,868,162
Change in net assets	137,068	(75,205)	61,863	(416,122)
Net assets, beginning of year	1,949,535	787,062	2,736,597	3,152,719
Net assets, end of year	\$ 2,086,603	\$ 711,857	\$ 2,798,460	\$ 2,736,597

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

MENDING KIDS INTERNATIONAL

STATEMENT OF FUNCTIONAL EXPENSES

For the year ended December 31, 2014

With comparative totals for the year end December 31, 2013

	Program Services	Management and General	Fundraising	Total Expenses	
				2014	2013
Surgical expenses					
Surgical missions	\$ 2,107,966	\$ -	\$ -	\$ 2,107,966	\$ 2,154,599
United States surgeries	1,104,143			1,104,143	1,410,631
International surgeries	975,070			975,070	655,722
Hometown missions	568,191			568,191	591,006
	4,755,370	-	-	4,755,370	4,811,958
Salaries and employee benefits	343,336	72,536	67,700	483,572	480,503
Events and outreach	88,136		352,853	440,989	263,572
Professional fees	29,562	133,642	7,390	170,594	51,412
Advertising and marketing	81,607		20,402	102,009	53,896
Consultants	28,090	15,029	27,096	70,215	52,620
Rent	48,364	10,088	9,416	67,868	58,670
Supplies	15,587	3,293	3,074	21,954	21,911
Insurance	13,600	2,874	2,682	19,156	9,466
Bank charges and merchant fees		18,836		18,836	13,454
Miscellaneous expenses	7,674	9,063	1,484	18,221	15,841
Communication	11,221	2,371	2,212	15,804	11,401
Conferences and meetings	12,460	2,689		15,149	3,759
Bad debt expense			11,096	11,096	-
Depreciation and amortization		7,236		7,236	6,285
Mileage and parking	3,857	815	760	5,432	8,259
Meals and entertainment	3,490	737	688	4,915	2,657
Postage	2,779	587	548	3,914	1,841
Corporate travel				-	657
	\$ 5,445,133	\$ 279,796	\$ 507,401	\$ 6,232,330	
Total 2014 functional expenses	\$ 5,445,133	\$ 279,796	\$ 507,401	\$ 6,232,330	
Total 2013 functional expenses	\$ 5,356,501	\$ 138,855	\$ 372,806		\$ 5,868,162

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

MENDING KIDS INTERNATIONAL

STATEMENT OF CASH FLOWS

For the year ended December 31, 2014

With comparative totals for the year ended December 31, 2013

	2014	2013
Cash flows from operating activities:		
Change in net assets	\$ 61,863	\$ (416,122)
Adjustments to reconcile change in net assets to net cash (used) by operating activities:		
Depreciation and amortization expense	7,236	6,285
Change in allowance for uncollectible accounts	(500)	(12,680)
Loss on disposal of property and equipment	-	2,486
Reinvested investment interest and dividends	(72,451)	(54,343)
Realized and unrealized (gain) on investments	(2,518)	(25,351)
Non-cash contribution of assets	(670,031)	-
Changes in operating assets and liabilities		
Decrease (increase) in contributions receivable	27,755	(30,933)
(Increase) decrease in other assets	(8,500)	6,731
Increase (decrease) in accounts payable	34,789	(54,621)
(Decrease) increase in accrued liabilities	(27,791)	21,256
Increase in deferred revenue	18,000	42,000
	(632,148)	(515,292)
Cash flows from investing activities:		
Purchase of investments	(400,000)	(201,000)
Proceeds from sale of investments	782,176	660,500
Purchase of property and equipment	(5,900)	(8,648)
	376,276	450,852
Net (decrease) in cash	(255,872)	(64,440)
Cash, beginning of year	267,649	332,089
Cash, end of year	\$ 11,777	\$ 267,649
Supplemental disclosure:		
Non-cash activities:		
Donated artwork held for sale	\$ 400,000	\$ -
Donated medical supplies (inventory)	253,831	-
Donated website development	16,200	-
	\$ 670,031	\$ -

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

MENDING KIDS INTERNATIONAL

NOTES TO FINANCIAL STATEMENTS

1. **Organization**

Mending Kids International (“MKI”) is a nonprofit public benefit corporation chartered by the State of California in 1993 to provide donated surgical services, in transportation, to sick and injured children worldwide who otherwise could not afford such treatment.

MKI provides the following areas of service:

International In-Bound Program – Transports foreign children with correctable surgical conditions to the United States of America where they can be treated by local physicians and medical facilities.

International Surgeries – Facilitates and funds the “matchmaking” between specialized surgeons and the children who need surgery.

Surgical Missions – Transports medical teams to developing countries where they are able to provide specialized surgical care to prescreened children.

Hometown Missions Program – Provides free surgical care to children all over the United States and abroad performed at domestic volunteer surgical centers with volunteer surgeons.

2. **Summary of Significant Accounting Policies**

A summary of the significant accounting policies applied in the preparation of the accompanying financial statements is as follows:

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting.

Accounting

To ensure observance of certain constraints and restrictions placed on the use of resources, the accounts of MKI are maintained in accordance with the principles of net asset accounting. This is the procedure by which resources for various purposes are classified for accounting and reporting purposes into net asset classes that are in accordance with specified activities or objectives. Accordingly, all financial transactions have been recorded and reported by net asset class as follows:

Unrestricted. These generally result from revenues generated by receiving unrestricted contributions, providing services, and receiving interest from investments less expenses incurred in providing program-related services, raising contributions, and performing administrative functions.

MENDING KIDS INTERNATIONAL

NOTES TO FINANCIAL STATEMENTS

2. Summary of Significant Accounting Policies, continued

Unrestricted – Board Designated and Equity in Fixed Net Assets. These are comprised of resources that the Board of Directors has established as being designated for future program operations and those resources invested in its fixed assets. For purposes of complying with net assets accounting, these assets are included in the unrestricted net assets at December 31, 2014 (see Note 11).

Temporarily Restricted. MKI reports gifts of cash and other assets as temporarily restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or the purpose of the restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Activities as net assets released from program or capital restrictions.

Permanently Restricted. These net assets are restricted by donors who stipulate that resources are to be maintained permanently, but permit MKI to expend all of the income (or other economic benefits) derived from the donated assets. MKI had no permanently restricted net assets at December 31, 2014.

Contributions Receivable

Contributions receivable are unconditional promises to give that are expected to be collected within one year. MKI uses the allowance method to reserve for potentially uncollectible contributions receivable. Conditional promises to give are not included as support until the conditions are substantially met. There was no allowance for uncollectible accounts reserved at December 31, 2014.

Investments

MKI values its investments at fair value. Unrealized gains or losses (including investments bought, sold, and held during the year) are reflected in the Statement of Activities as gain or loss on investments. Short-term, highly liquid money market deposits that are not used for operations are treated as an investment.

Concentration of Credit Risks

MKI places its temporary cash investments with high-credit, quality financial institutions. At times, such investments may be in excess of the Federal Deposit Insurance Corporation insurance limit. MKI has not incurred losses related to these investments.

Approximately 66% of the revenue and support generated by MKI for the year ended December 31, 2014 was derived from in-kind contributions.

MENDING KIDS INTERNATIONAL

NOTES TO FINANCIAL STATEMENTS

2. Summary of Significant Accounting Policies, continued

Property and Equipment

Property and equipment are recorded at cost if purchased or at fair value at the date of donation, if donated. Depreciation is computed on the straight-line basis over the estimated useful lives of the related assets which are:

Furniture and equipment	5 years
Computer software and website	3 years

Fair Value Measurements

Generally accepted accounting principles provide guidance on how fair value should be determined when financial statement elements are required to be measured at fair value. Valuation techniques are ranked in three levels depending on the degree of objectivity of the inputs used with each level:

Level 1 inputs - quoted prices in active markets for identical assets

Level 2 inputs - quoted prices in active or inactive markets for the same or similar assets

Level 3 inputs - estimates using the best information available when there is little or no market

MKI is required to measure certain investments and non-cash contributions at fair value. The specific techniques used to measure fair value for each element are described in the notes below that relate to each element.

Donated Materials and Services

MKI received significant contributions of materials and services from individuals, medical facilities, and other organizations. Contributions of donated non-cash assets are measured on a non-recurring basis and are recorded at fair value in the period received. Contributions of donated services that create or enhance non-financial assets or that require specialized skills are provided by individuals possessing those skills, and would typically need to be purchased, if not provided by donation, are recorded at fair value at the date of donation. Donated assets, services, materials, and medical facilities of \$4,553,456 for the year ended December 31, 2014 are reflected in these financial statements (see Note 9).

continued

MENDING KIDS INTERNATIONAL

NOTES TO FINANCIAL STATEMENTS

2. Summary of Significant Accounting Policies, continued

Income Taxes

MKI is exempt from taxation under Internal Revenue Code Section 501(c)(3) and California Revenue and Taxation Code Section 23701d.

Generally accepted accounting principles provide accounting and disclosure guidance about positions taken by an organization in its tax returns that might be uncertain. Management has considered its tax positions and believes that all of the positions taken by MKI in its federal and state exempt organization tax returns are more likely than not to be sustained upon examination. MKI's returns are subject to examination by federal and state taxing authorities, generally for three and four years, respectively, after they are filed.

Functional Allocation of Expenses

MKI allocates its expense on a functional basis among its various programs, management and general and fundraising services. Expenses that can be identified with a specific program or supporting services are allocated directly according to their natural expenditure classification. Other expenses common to several functions are allocated accordingly.

Use of 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 reported amounts of assets, liabilities, revenues, and expenses as of the date and for the period presented. Actual results may differ from those estimates.

Comparative Totals

The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with MKI's financial statements for the year ended December 31, 2013, from which the summarized information was derived.

Reclassification

Certain amounts from the December 31, 2013 financial statements have been reclassified to conform to the presentation for the year ended December 31, 2014.

Subsequent Events

Management has evaluated subsequent events through November 6, 2015, the date which the financial statements were available.

continued

MENDING KIDS INTERNATIONAL

NOTES TO FINANCIAL STATEMENTS

3. Investments

Investments at December 31, 2014 consist of the following:

Corporate bonds	\$ 892,043
Government bonds	865,465
Common stocks	262,984
Mutual funds	246,831
Money market funds	<u>51,197</u>
	<u>\$2,318,520</u>

Investment income consists of the following:

Interest and dividends	\$72,451
Net realized and unrealized gains	<u>2,518</u>
	<u>\$74,969</u>

4. Inventory

In 2014, MKI recognized medical supplies and equipment most of which were donated, and a small amount were purchased at a discounted rate. Inventory is based on physical counts as of December 31, 2014. The valuation of inventory held for program use is determined based on the replacement method using fair market values. At December 31, 2014, the value of inventory was \$253,831.

5. Artwork Held for Sale

During the year ended December 31, 2014, MKI received eight oil-on-canvas paintings. The collection was conservatively recorded at \$400,000, an amount less than its appraised value of \$800,000.

6. Fixed Assets

Property and equipment at December 31, 2014 consist of the following:

Leasehold improvements	\$ 14,548
Website design	12,918
Furniture and equipment	5,533
Work in progress – website	<u>16,200</u>
	49,199
Less: accumulated depreciation and amortization	<u>(21,729)</u>
	<u>\$ 27,470</u>

Depreciation and amortization expense for the year ended December 31, 2014 was \$7,236.

continued

MENDING KIDS INTERNATIONAL

NOTES TO FINANCIAL STATEMENTS

7. Commitments

Obligations Under Operating Leases

MKI leases certain facilities and equipment under operating leases with various terms. Future minimum payments, by year and in the aggregate, under these leases with initial or remaining terms of one year or more, consist of the following:

<u>Year ended December 31,</u>	
2015	\$ 75,042
2016	77,284
2017	79,597
2018	<u>20,079</u>
	<u>\$252,002</u>

Lease expense under operating leases for the year ended December 31, 2014 was \$67,868

8. Temporarily Restricted Net Assets

Temporarily restricted net assets at December 31, 2014 consist of the following:

International surgery	\$692,768
Hometown mission	12,500
HANS fund	3,761
Iraqi children	<u>2,828</u>
	<u>\$711,857</u>

continued

MENDING KIDS INTERNATIONAL

NOTES TO FINANCIAL STATEMENTS

9. Fair Value Measurements

The table below presents the balances of assets measured at fair value at December 31, 2014 on a recurring basis:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Mutual funds				
Fixed income	\$ 150,299	\$ -	\$ -	\$ 150,299
Large blend	54,503			54,503
Foreign large blend	15,908			15,908
Foreign stocks	10,195			10,195
Diversified emerging markets	9,155			9,155
Small growth	6,771			6,771
	<u>\$ 246,831</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 246,831</u>
Common stocks				
Technology	\$ 65,412	\$ -	\$ -	\$ 65,412
Consumer discretionary	52,742			52,742
Financial	46,647			46,647
Industrial	40,449			40,449
Energy	31,070			31,070
Health care	16,508			16,508
Materials	10,156			10,156
	<u>\$ 262,984</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 262,984</u>
Corporate bonds				
A- credit rating	\$ -	\$461,273	\$ -	\$ 461,273
A credit rating		371,419		371,419
BBB+ credit rating		30,191		30,191
AA+ credit rating		29,160		29,160
	<u>\$ -</u>	<u>\$892,043</u>	<u>\$ -</u>	<u>\$ 892,043</u>
U.S. government securities				
Municipal bonds	\$ 790,951	\$ -	\$ -	\$ 790,951
Federal agency bonds	74,514			74,514
	<u>\$ 865,465</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 865,465</u>
	<u>\$1,375,280</u>	<u>\$892,043</u>	<u>\$ -</u>	<u>\$2,267,323</u>

The fair values of mutual funds, common stocks and U.S. government securities have been measured on a recurring basis using quoted prices for identical assets in active markets (Level 1 inputs).

The fair values of corporate bonds have been measured on a recurring basis using quoted prices for identical assets in inactive markets (Level 2 inputs).

continued

MENDING KIDS INTERNATIONAL

NOTES TO FINANCIAL STATEMENTS

9. Fair Value Measurements, continued

The table below presents the balances of assets measured at fair value at December 31, 2014 on a non-recurring basis:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Donated physician services	\$ -	\$2,112,203	\$ -	\$2,112,203
Donated medical facilities		1,665,837		1,665,837
Donated assets held for sale		400,000		400,000
Donated medical supplies		271,278		271,278
Donated professional services		104,138		104,138
	<u>\$ -</u>	<u>\$4,553,456</u>	<u>\$ -</u>	<u>\$4,553,456</u>

The fair value of contributed assets, services, materials, and medical facilities has been measured on a non-recurring basis using quoted prices for similar assets in inactive markets (Level 2 inputs).

10. Related Party Transactions

For the year ended December 31, 2014, MKI paid immediate family members of employees or board members \$7,785 for website design, office remodeling, and general consulting projects.

11. Board Designated Funds

After receiving an unrestricted bequest in 2009, the board voluntarily started the Cris Embleton Fund, named after the organization's founder. The board agreed to not use the interest unless the board voted and to let the fund accrue interest and grow over time. The Cris Embleton fund is currently comprised exclusively of board-designated funds which are held in investments for the purpose of providing support to MKI programs over the long-term.

MKI utilizes a total return strategy that considers both capital appreciation and current income, focusing on overall fund returns. MKI targets a diversified asset allocation of recognized investments vehicles within prudent risk constraints.

Changes in the board designated funds for the year ended December 31, 2014 are as follows:

Board designated funds beginning of the year	\$134,143
Investment returns	<u>111,590</u>
	<u>\$245,733</u>