

STAR OF HOPE MISSION
FINANCIAL STATEMENTS
DECEMBER 31, 2017

C O N T E N T S

	Page
Independent Auditor’s Report.....	2-3
Statement of Financial Position.....	4
Statement of Activities	5
Statement of Functional Expenses	6
Statement of Cash Flows.....	7
Notes to Financial Statements	8-21



INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Star of Hope Mission

We have audited the accompanying financial statements of Star of Hope Mission (the Mission) (a Texas non-profit corporation), which comprise the statement of financial position as of December 31, 2017, 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; 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.

Auditor's 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 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 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 auditor's judgment, including the assessment of the risk 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 the Mission as of December 31, 2017, and the changes in its net assets and cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 4, 2018, on our consideration of the Mission'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* in considering the Mission's internal control over financial reporting and compliance.

Hoyer & Pearson Company, P.C.

Houston, Texas
June 4, 2018

STAR OF HOPE MISSION
STATEMENT OF FINANCIAL POSITION
DECEMBER 31, 2017

ASSETS

Cash and cash equivalents	\$ 3,557,832
Receivables	1,993,110
United Way receivable	911,032
Pledges receivable, net	5,557,435
Prepaid expenses and other assets	712,844
Land, buildings and equipment, net	70,199,518
Long-term investment securities	10,052,669
Beneficial interest in Trees of Hope	<u>250,649</u>
 TOTAL ASSETS	 <u>\$ 93,235,089</u>

LIABILITIES AND NET ASSETS

LIABILITIES

Accounts payable and accrued liabilities	\$ 4,411,112
Deferred revenues and rent	102,778
Notes payable	<u>11,780,541</u>

TOTAL LIABILITIES 16,294,431

NET ASSETS

Without donor restrictions	71,542,086
With donor restrictions	<u>5,398,572</u>

TOTAL NET ASSETS 76,940,658

TOTAL LIABILITIES AND NET ASSETS \$ 93,235,089

STAR OF HOPE MISSION
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2017

	Without Donor Restrictions	With Donor Restrictions	Total
Public support and revenues:			
Contributions and other grants	\$ 15,105,150	\$ 8,140,788	\$ 23,245,938
Special events, net	183,202	1,378,885	1,562,087
In-kind contributions	3,402,824	-	3,402,824
Fees and grants from government agencies	1,219,379	-	1,219,379
Client fees	85,629	-	85,629
Investment return, net	1,204,315	593	1,204,908
Net change in beneficial interest in Trees of Hope	(35,500)	-	(35,500)
Miscellaneous	217,689	-	217,689
Net assets released from restrictions	52,556,679	(52,556,679)	-
Total public support and revenues	73,939,367	(43,036,413)	30,902,954
Expenses:			
Program Services			
Men's Development Center	5,657,570	-	5,657,570
Women and Family Development Center	5,712,100	-	5,712,100
Women and Family Emergency Shelter	4,169,482	-	4,169,482
Transitional Living Center	4,018,662	-	4,018,662
Extended Services	2,487,125	-	2,487,125
Total program services	22,044,939	-	22,044,939
Management and general	2,941,112	-	2,941,112
Fundraising	4,091,191	-	4,091,191
Total expenses	29,077,242	-	29,077,242
Change in net assets	44,862,125	(43,036,413)	1,825,712
Net Assets, beginning of year	26,679,961	48,434,985	75,114,946
Net Assets, end of year	\$ 71,542,086	\$ 5,398,572	\$ 76,940,658

STAR OF HOPE MISSION
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED DECEMBER 31, 2017

	Men's Development Center	Women and Family Development Center	Women and Family Emergency Shelter	Transitional Living Center	Extended Services	Total Program Services	Management and General	Fundraising	Total
Salaries	\$ 2,470,592	\$ 2,457,213	\$ 1,763,174	\$ 1,827,120	\$ 757,690	\$ 9,275,789	\$ 1,495,758	\$ 1,028,715	\$ 11,800,262
Benefits	460,940	432,112	466,090	437,569	156,224	1,952,935	335,832	212,345	2,501,112
Payroll taxes	188,114	181,677	141,217	145,705	58,856	715,569	102,118	78,253	895,940
Workers compensation	16,725	1,193	16,196	16,185	2,755	53,054	2,315	1,316	56,685
Total salaries and related expenses	3,136,371	3,072,195	2,386,677	2,426,579	975,525	11,997,347	1,936,023	1,320,629	15,253,999
Temporary help services	20,597	125,368	134,470	40,733	-	321,168	168,006	53,158	542,332
Professional fees and contract services	120,718	209,677	151,856	129,082	10,228	621,561	283,360	432,562	1,337,483
Supplies	236,701	152,738	151,183	157,294	57,696	755,612	5,428	2,329	763,369
Telephone	43,742	73,519	33,036	34,684	24,611	209,592	31,385	23,081	264,058
Postage and handling	531	736	184	268	-	1,719	2,532	180,381	184,632
Occupancy	475,239	319,622	307,798	331,526	67,492	1,501,677	76,038	71,046	1,648,761
Equipment rent maintenance and purchase	118,061	101,972	78,232	54,569	10,841	363,675	74,413	229,129	667,217
Printing and publications	8,160	6,058	4,124	4,777	464	23,583	45,153	547,059	615,795
Travel and transportation	33,094	22,343	16,213	19,725	19,505	110,880	11,472	3,413	125,765
Conferences dues and certifications	2,290	626	319	5,267	90	8,592	19,124	390	28,106
Assistance to individuals and ministries	32,903	25,595	50,809	38,150	660,582	808,039	-	-	808,039
Donor acquisition	-	-	-	-	-	-	-	841,941	841,941
Bad debt expense	-	-	-	-	-	-	-	231,045	231,045
Bank charges and credit card fees	-	-	-	-	-	-	50,237	105,657	155,894
Miscellaneous expense	31,931	158,053	13,901	50,844	20,648	275,377	135,807	8,176	419,360
Total operating expenses	4,260,338	4,268,502	3,328,802	3,293,498	1,847,682	16,998,822	2,838,978	4,049,996	23,887,796
In-kind donations expense	1,133,096	601,836	671,192	692,368	639,443	3,737,935	96,531	14,535	3,849,001
Depreciation expense	264,136	841,762	31,326	32,796	-	1,170,020	5,603	26,660	1,202,283
Loss on sale of facility	-	-	138,162	-	-	138,162	-	-	138,162
Total expenses by function	5,657,570	5,712,100	4,169,482	4,018,662	2,487,125	22,044,939	2,941,112	4,091,191	29,077,242
Plus expenses netted against revenue on the statement of activities									
Cost of direct benefits to donors	-	-	-	-	-	-	-	622,669	622,669
Investment fees	-	-	-	-	-	-	67,857	-	67,857
Total expenses	\$ 5,657,570	\$ 5,712,100	\$ 4,169,482	\$ 4,018,662	\$ 2,487,125	\$ 22,044,939	\$ 3,008,969	\$ 4,713,860	\$ 29,767,768

See accompanying notes.

STAR OF HOPE MISSION
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2017

CASH FLOWS FROM OPERATING ACTIVITIES:	
Change in net assets	\$ 1,825,712
Adjustments to reconcile change in net assets to net cash used by operating activities:	
Net realized and unrealized gain on marketable securities	(975,714)
Depreciation	1,202,283
Contributions restricted to Cornerstone Community	(3,930,105)
Loss on sale of facility	138,162
Net change in beneficial interest in Trees of Hope	35,500
(Increase) decrease in operating assets:	
Receivables	(646,649)
United Way receivable	19,336
Pledges receivable, net	(816,667)
Prepaid expenses and other assets	476,781
Increase (decrease) in operating liabilities:	
Accounts payable and accrued liabilities	278,445
Deferred revenues and rent	<u>19,969</u>
Total adjustments	<u>(4,198,659)</u>
Net cash used by operating activities	<u>(2,372,947)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Purchase of investment securities	(1,293,278)
Proceeds from sale or maturity of investment securities	1,385,240
Purchase of land, buildings and equipment	(32,592,023)
Proceeds from sale of facility	<u>4,104,699</u>
Net cash used by investing activities	<u>(28,395,362)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:	
Proceeds from contributions restricted to Cornerstone Community	7,842,608
Debt issuance costs	(79,159)
Draws on notes payable	16,214,992
Payments on notes payable	<u>(4,355,292)</u>
Net cash provided by financing activities	<u>19,623,149</u>
NET DECREASE IN CASH, CASH EQUIVALENTS, AND RESTRICTED CASH	(11,145,160)
CASH, CASH EQUIVALENTS, AND RESTRICTED CASH AT BEGINNING OF YEAR	<u>14,702,992</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 3,557,832</u>
SUPPLEMENTAL DISCLOSURE OF SIGNIFICANT NONCASH ACTIVITIES:	
Cash paid for interest	<u>\$ 55,664</u>

See accompanying notes.

NOTE A SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Star of Hope Mission (the Mission) is a Christ-centered community dedicated to meeting the needs of homeless men, women and their children. Positive life changes are encouraged through structured programs which focus on spiritual growth, education, employment, life management and recovery from substance abuse. Residents are provided with individual counseling services, referrals and other assistance designed to obtain permanent housing and make lasting life changes. During the year, the Mission operated four facilities:

The Men's Development Center - a 328 bed facility which provides emergency shelter and life-recovery services to men at various stages of self-sufficiency.

The Women and Family Development Center - a 600 bed facility which provides emergency shelter and life-recovery services to single women and single-parent families at various stages of self-sufficiency, which began operations in August 2017.

The Women and Family Emergency Shelter - a 296 bed facility offering emergency shelter and services leading to stability for homeless single women and single-parent families in crisis. Residents at the facility were moved to the Women and Family Development Center in August 2017.

The Transitional Living Center - a facility that can house up to 66 single-parent families with children and as many as 45 single women. Residents pursue a self-supporting life through various life skills and substance abuse recovery programs. Residents at the facility were moved to the Women and Family Development Center in August 2017.

Additionally, the Mission's Extended Services program ministers to those on the brink of homelessness, the street homeless, and those who have exited homelessness by providing rent assistance, distribution of food and clothing, and operation of two supportive housing programs.

In February 2016, the Mission began construction of the Star of Hope Mission Cornerstone Community[®] campus (Cornerstone). This collaborative campus is anchored by the Mission's Women and Family Development Center, which opened in August 2017. It will also be occupied by other nonprofit organizations that provide permanent supportive housing, job readiness training and after school programs for children. The Mission will continue development of the campus in future years as demand for additional services materializes.

The Mission is supported primarily through donor contributions, the United Way, and government grants.

Concentration of Credit and Market Risk - Financial instruments which subject the Mission to concentrations of credit risk consist principally of cash, receivables and marketable securities. The Mission places its cash with a financial institution it believes to be creditworthy. At December 31, 2017, deposits with financial institutions exceed the amount of federal deposit insurance provided on such deposits by approximately \$3,300,000. These deposits typically may be redeemed upon demand and therefore, bear minimal risk. In monitoring this credit risk, the Mission periodically evaluates the stability of the financial institution.

NOTE A SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Mission's investments in marketable and nonmarketable securities subject the Mission to various levels of risk associated with economic, operating, and political events beyond management's control. Consequently, management's judgment as to the level of losses that currently exist or may develop in the future involves the consideration of current and anticipated conditions and their potential effects on the Mission's investments. Due to the level of risk associated with investments and the level of uncertainty related to changes in the value of investments, it is at least reasonably possible that changes in risks in the near term could materially impact the amounts reflected in the accompanying financial statements.

Use of Estimates - Management uses estimates and assumptions in preparing these financial statements in accordance with accounting principles generally accepted in the United States (GAAP). Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could vary from the estimates that were used.

Cash and Cash Equivalents - For purposes of the statement of cash flows, the Mission considers all unrestricted, highly liquid investments with a maturity of three months or less to be cash equivalents.

Donations in Transit - Contributions postmarked by December 31 and received in January are included in receivables as donations in transit and contributions revenue in the current year.

Pledges Receivables - Generally, no collateral or other security is required to support receivables. An allowance for doubtful accounts is established and accounts written off as needed based upon factors surrounding the credit risk of specific contributors. At December 31, 2017, pledges from six donors represented 72% of pledges.

Investment Securities - All marketable securities are measured at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Investment income or loss (including realized and change in unrealized gains and losses on marketable securities, interest, and dividends) is included in the statement of activities as increases or decreases in unrestricted net assets unless the income or loss is restricted by donor or law.

It is the policy of the Mission to promptly sell all donated securities.

Land, Buildings and Equipment - Purchased land, buildings and equipment are recorded at cost. Donated land, buildings and equipment are recorded at fair value at the date of donation. Buildings and equipment are depreciated using the straight-line method based on the estimated useful lives of the assets, generally as follows:

Buildings and improvements	5-40 years
Equipment, furniture, computers and software	5-12 years
Vehicles	5-6 years

NOTE A SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Change in Accounting Principle - The Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2016-14, Presentation of Financial Statements of Not-for-Profit Entities, on August 18, 2016. This new standard changes the manner in which net assets are classified and financial statements are prepared. The standard is effective for annual financial statements issued for fiscal years beginning after December 15, 2017. Early adoption of the standard is permitted. The Mission has elected to adopt the standard effective for the year ended December 31, 2017.

Financial Statement Presentation - Information regarding the financial position and activities of the Mission is reported in two categories as follows:

Net Assets Without Donor Restrictions - represent expendable funds available for operations which are not otherwise limited by donor restrictions.

Net Assets With Donor Restrictions - consist of (i) contributed funds subject to donor or grantor imposed restrictions related to a specific purpose or requiring a specific passage of time before the funds can be spent, and (ii) contributed funds subject to irrevocable donor restrictions requiring the assets be maintained in perpetuity for the purpose of generating investment income to fund current operations.

Contributions - Contributions are recognized when the donor makes a promise to give to the Mission that is, in substance, unconditional. Contributions that are restricted by the donor for future periods or a specific purpose are reported as increases in net assets with donor restrictions. When a restriction expires, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statement of activities as net assets released from donor restrictions.

Unconditional promises to give that are expected to be collected within one year are recorded at their realizable value. Unconditional promises to give that are expected to be collected after one year or more are recorded at the present value of estimated future cash flows. The discounts on those amounts are computed using a risk-free interest rate which was 2% at December 31, 2017. Amortization of the discount is included as contribution revenue. Conditional promises to give are not included as support until such time as the conditions are substantially met.

The Mission reports gifts of property and equipment as support without donor restrictions unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as support with donor restrictions.

If the only restriction on the unconditional promise to give is the construction or purchase of specified long-lived assets and absent explicit donor stipulations about how long those long-lived assets must be maintained, the Mission reports expirations of donor restrictions as the donated or acquired long-lived assets are placed in service.

NOTE A SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Gifts in Kind - Donations are recorded as in-kind contributions at the estimated fair value of the gift. Food is recorded at the time of receipt, based on pre-established standards. Donations of clothing are not recorded until distributed to clients or other relief organizations. At the time of distribution, both the contribution value and related program expense are computed using standards set by management and which approximate the fair value for second-hand clothing.

Donated Services - Donated services are reported as in-kind contributions at fair value if the service would typically need to be purchased by the Mission if they had not been provided by contribution, required specialized skills and were provided by individuals with those skills. For the year ended December 31, 2017, the Mission has recorded \$781,887 of donated professional services. In addition, many individuals also volunteer their time and perform a variety of tasks that assist the Mission with specific client assistance programs, general maintenance and other projects. The Mission received more than 26,922 (unaudited) volunteer hours during 2017, which are not reflected as revenues or expenses in the financial statements.

Functional Expenses - The financial statements report certain categories of expenses that are attributable to more than one program or supporting function. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include depreciation and amortization, office and occupancy which are allocated on a square footage basis, as well as salaries and related benefits which are allocated on the basis of the number of direct program staff combined with estimates of time and effort for certain executive and support staff. Joint costs of activities that include a fundraising appeal are allocated based on management's estimate of the content ratio of the promotional materials.

Income Taxes - The Mission is a not-for-profit organization that is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. However, the Mission is subject to taxes on unrelated business income. No unrelated business income tax was paid in 2017.

The Mission believes that all significant tax positions utilized by the Mission will more likely than not be sustained upon examination. As of December 31, 2017, the tax years that remain subject to examination by the major tax jurisdictions under the statute of limitations are from the fiscal year 2014 forward (with limited exceptions). Tax penalties and interest, if any, would be accrued as incurred and would be classified as management and general expense in the statement of activities.

Split Interest Agreements - In 2014, the Mission received fractional interests in several life insurance policies. These policies are irrevocable remainder interests and, as such, are recognized as investments on the statement of financial position, and valued at their fair value.

NOTE B LIQUIDITY AND AVAILABILITY

The Mission manages its liquidity by (i) developing a board approved annual budget that is cash neutral or reflects a surplus, (ii) monitoring liquidity with monthly cash flow projections, and (iii) when necessary, utilizing a \$3,000,000 Liquid Asset Line to assist with unanticipated liquidity needs. In addition, as discussed in Note I, the Mission's Board of Trustees has established a policy that 4% of the net asset value of the endowment funds, computed at the beginning of the year, shall be transferred to operations annually. This amount is included in the table of financial assets below. In the event of financial distress, the Mission may request to expend amounts in excess of 4% of the net value of the endowment fund for liquidity needs, but such a request requires a recommendation from the Finance and Endowment Committee and an affirmative vote of 75% of the Board of Trustees.

Financial assets available for general expenditures, that is, without donor or other restrictions limiting their use, within one year of the statement of financial position date, are comprised of the following:

Cash and cash equivalents	\$ 3,287,850
Receivables	1,993,110
United Way receivables	911,032
Pledges receivable, net	2,761,219
4% Endowment distribution	411,603
Prepaid expenses and other assets	<u>712,844</u>
	<u>\$ 10,077,658</u>

NOTE C RECEIVABLES

Receivables consist of the following at December 31, 2017:

Government grants	\$ 283,881
Donations in transit	<u>1,709,229</u>
	<u>\$ 1,993,110</u>

NOTE D PLEDGES RECEIVABLE

Pledges receivable consist of the following at December 31, 2017:

Receivables due in less than one year	\$ 2,820,835
Receivables due in one to five years	2,913,095
Less allowance for uncollectible pledges	(59,616)
Less discount on long-term pledges receivable at 2%	<u>(116,879)</u>
Total pledges receivable, net	<u>\$ 5,557,435</u>

NOTE E LAND, BUILDINGS AND EQUIPMENT

At December 31, 2017, the cost and accumulated depreciation of land, buildings and equipment were as follows:

Land	\$ 8,818,760
Land improvements	6,969,639
Buildings and improvements	53,756,053
Equipment and furniture	2,871,376
Vehicles	548,345
Computers and software	<u>3,083,160</u>
	76,047,333
Less accumulated depreciation	<u>(5,847,815)</u>
	<u>\$ 70,199,518</u>

NOTE F RETIREMENT PLAN

The Mission has established a defined contribution retirement plan commonly referred to as a 401(k) plan. Employees may choose to defer a portion of their compensation and the investments are selected by the employees. The Mission, at its discretion, may choose to make contributions to the plan. The Mission's contribution is vested on a graduated scale over six years. At the end of six years of service, the employee is fully vested. For the year ended December 31, 2017, the Mission's contributions to the plan were approximately \$381,000.

NOTE G NOTES PAYABLE

On April 12, 2016, the Mission entered into a Construction Loan Agreement to finance construction of improvements at Cornerstone. The loan agreement, as amended on September 1, 2017 consists of two loans: (i) a \$7,500,000 advancing term loan (Fixed Loan), and (ii) a \$12,500,000 advancing term loan (Floating Loan), as discussed further below. The Mission could request advances through March 31, 2018, and advances are made pro rata between the Fixed Loan and Floating Loan. The loans are secured by a first lien deed of trust on the Cornerstone property and improvements totaling approximately \$59,000,000 and Cornerstone pledges of approximately \$5,000,000. The Mission is under restrictive covenants limiting additional borrowings.

The two loans will reduce in combined availability based on the following schedule:

December 31, 2019	\$17,500,000
December 31, 2020	\$15,000,000
April 12, 2021	\$ -

NOTE G NOTES PAYABLE (CONTINUED)

Monthly interest payments only are required for the duration of the loans, based on the following:

Fixed Loan - The interest rate on outstanding borrowings is fixed at 3.25% for the duration of the loan.

Floating Loan - The interest rate on outstanding borrowings will be floating at 30-day LIBOR + 175 basis points (indicative rate of 3.12938% at the financial statement date).

There is a 0.25% unused commitment fee due quarterly once the total borrowings reach \$10,000,000. All capital campaign proceeds will be used to fund construction draws or reduce the principal balance of the loans.

Notes payable consist of the following at December 31, 2017:

Fixed Loan	\$ 4,743,880
Floating Loan	<u>7,115,820</u>
	11,859,700
Less unamortized debt issuance costs	<u>(79,159)</u>
	<u>\$ 11,780,541</u>

The Mission has a Liquid Asset Line (LAL) which is collateralized by the investments held with the financial institution that manages the endowment funds. The total amount available on this account is \$5,089,000 and any withdrawals must be preapproved by the Finance and Endowment Committee. Under the terms of the Construction Loan Agreement, as amended on September 1, 2017, outstanding borrowings under the LAL are limited to \$3,000,000. Interest on such withdrawals is charged at the corresponding LAL index plus 2.5% (indicative rate of 3.81375% at December 31, 2017). There were no outstanding borrowings on the LAL at December 31, 2017.

NOTE H NET ASSETS WITH DONOR RESTRICTIONS

Net assets with donor restrictions are restricted for the following purposes or periods:

Subject to expenditure for specific purpose:	
United Way receivable	\$ 891,696
Client programs	810,167
Land, buildings, and equipment	<u>1,267,824</u>
	2,969,687
Subject to passage of time:	
For periods after December 31, 2017	1,378,885
Subject to the Mission's spending policy and appropriation:	
Perpetual endowment fund	<u>1,050,000</u>
	<u>\$ 5,398,572</u>

In 2017, net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of events specified by the donors as follows:

Satisfaction of program restrictions	\$ 4,958,488
Satisfaction of equipment acquisition restrictions	46,981,765
Expiration of time restrictions	<u>616,426</u>
	<u>\$ 52,556,679</u>

NOTE I ENDOWMENT FUNDS

The Mission's Board of Trustees has established an endowment fund to provide funding for long-term needs, where the funds contributed by donors are not spent immediately, but are invested to provide a stream of earnings which can then be used or reinvested for later needs. Donations to the endowment are considered made without donor restrictions, unless restrictions are specified by the donor. The Mission has also established a Finance and Endowment Committee to administer the ongoing activities of the endowment and to ensure that proper records and controls are maintained to comply with donors' specific conditions.

The Mission's Board of Trustees has established a policy that at least 4% of the net asset value of this fund, computed at the beginning of the year, shall be transferred to operations annually. Expending any amount in excess of 4% of the net value of the endowment or expending any portion of the initial contributions (both donor contributions and Mission transfers) to the endowment requires Finance and Endowment Committee recommendation and the vote of 75% of the entire Board of Trustees.

NOTE I ENDOWMENT FUNDS (CONTINUED)

The endowment funds are invested in accordance with an investment policy. The primary objectives, as stated in the policy, are preservation of capital and to achieve returns in excess of the rate of inflation to preserve purchasing power of the funds, while controlling risk.

The Mission also has a perpetual endowment fund. The Mission has interpreted The Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date absent explicit donor stipulations to the contrary. As a result, the Mission classifies the original value of the gifts donated to the perpetual endowment as net assets with donor restrictions. The net appreciation or depreciation to the endowment fund investment accounts is classified as board designated net assets.

The composition of and changes in endowment net assets as of December 31 are as follows:

	Without Donor Restrictions	With Donor Restrictions	Total
Board-designated endowment funds	\$ 9,299,572	-	\$ 9,299,572
Donor restricted funds:			
Original donor restricted gift and amount required to be retained by donor	-	1,050,000	1,050,000
Total funds	<u>\$ 9,299,572</u>	<u>\$ 1,050,000</u>	<u>\$ 10,349,572</u>

Changes in endowment net assets were as follows for the year ended December 31, 2017:

	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, beginning of year	\$ 8,524,079	\$ 1,050,000	\$ 9,574,079
Investment returns, net	1,158,461	-	1,158,461
Appropriation of endowment net assets for expenditures	(382,968)	-	(382,968)
Endowment net assets, end of year	<u>\$ 9,299,572</u>	<u>\$ 1,050,000</u>	<u>\$ 10,349,572</u>

NOTE J JOINT COSTS OF ACTIVITIES THAT INCLUDE A FUNDRAISING APPEAL

The Mission engages in various activities, including advertising, public relations, and the production of newsletters, which include programmatic and administrative information, together with a request for contributions. During the year, the costs associated with these activities included joint costs not directly attributable to any single function. Those costs were allocated among the following functional expense categories as follows:

Fund Raising	\$ 948,807
Men's Development Center	44,937
Women & Family Emergency Shelter	19,359
Women & Family Development Center	38,875
Transitional Living Center	19,708
Management and general	141,218
	\$ 1,212,904

NOTE K FAIR VALUE DISCLOSURE

GAAP provides a framework for measuring fair value using a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value based upon whether the inputs to those valuation techniques are observable or unobservable. This hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical financial instruments and the lowest priority to unobservable inputs. Valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs. The financial instrument's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

These inputs are summarized in the three broad levels listed below:

Level 1 – Unadjusted quoted prices for identical financial instruments in active markets that the Mission has the ability to access.

Level 2 – Other significant observable inputs (including quoted prices in active or inactive markets for similar financial instruments), or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the financial instruments.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the financial instruments. The fair value of Level 3 financial instruments is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

NOTE K FAIR VALUE DISCLOSURE (CONTINUED)

The following is a description of the valuation techniques used for assets measured at fair value.

Equity securities, mutual funds, government securities, and the fund of funds are actively traded securities. Valuation inputs normally include quoted bid price in active markets for identical assets. They have no contractual investment period and are used to further diversify the investment portfolio.

The fair value of corporate bonds is determined using recently executed transactions, market price quotations (where observable), bond spreads or credit default swap spreads, at the money volatility and/or volatility skew obtained from independent external parties such as vendors and brokers adjusted for any basis difference between cash and derivative instruments. When position-specific external price data are not observable, fair value is determined based on either benchmarking to similar instruments or cash flow models with yield curves, bond or single-name credit default swap spreads and recovery rates as significant inputs.

Alternative investments at 2017 consist of a fund of funds which include investment vehicles such as equity securities and mutual funds listed on the NASDAQ stock exchange. The fair value of the alternative investment is determined by the fund's manager based on the fair value of the underlying assets.

The fair value of split interest agreements is estimated by management of the Mission based on actuarial assumptions and discount rates applied to projected future cash flows. The Mission has irrevocable rights to these investments and does not hold the assets; therefore, the Mission's interest in the assets and specified future distributions is recorded as a beneficial interest in split interest agreements.

There have been no changes in the techniques used during 2017. There were no significant transfers in and/or out of the fair value categories during 2017. The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Mission believes its valuation techniques are appropriate and consistent with other market participants, the use of different techniques or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

STAR OF HOPE MISSION
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017

NOTE K FAIR VALUE DISCLOSURE (CONTINUED)

The fair values of financial instruments are categorized as follows as of December 31, 2017:

	Level 1	Level 2	Level 3	Total
Equity securities:				
Common stock	\$ 5,358,203	\$ -	\$ -	\$ 5,358,203
Preferred stock	494,935	-	-	494,935
Mutual funds:				
Fixed income	1,965,516	-	-	1,965,516
Equity	1,211,113	-	-	1,211,113
Split interest agreements	-	-	33,355	33,355
Alternative investments:				
Fund of funds	-	989,547	-	989,547
	<u>\$ 9,029,767</u>	<u>\$ 989,547</u>	<u>\$ 33,355</u>	<u>\$ 10,052,669</u>

The table below sets forth a summary of the changes in the fair value of the Level 3 investments for the year ended December 31, 2017.

Balance, beginning of year	\$ 90,380
Distributions	(24,994)
Unrealized loss	<u>(32,031)</u>
Balance, end of year	<u>\$ 33,355</u>

NOTE L RELATED PARTIES

Trees of Hope is a charitable 501(c)(3) corporation that donates the net proceeds from its fundraising activities to the Mission. Trees of Hope is controlled by a Board of Directors separate from that of the Mission; therefore consolidated financial statements are not required. Instead, the Mission records its beneficial interest in the net assets of Trees of Hope. Contributions recorded during 2017 totaled \$200,000.

NOTE M COMMITMENTS AND CONTINGENCIES

The Mission leases office, warehouse and activity center space under operating leases with future commitments as follows:

2018		\$ 457,340
2019		449,877
2020		281,377
2021		127,978
2022		<u>63,285</u>
		<u>\$ 1,379,857</u>

Rent expense amounted to \$1,011,436 for 2017.

Amounts received from government and other grants require the fulfillment of certain conditions as set forth in the grant contracts. The Mission intends to fulfill the conditions of all grants, recognizing that the failure to fulfill the conditions could result in the return of the funds to the grantors. Amounts received or receivable from grantor agencies are subject to audit and adjustment by the grantor agencies. Any disallowed claims, including amounts already collected, could become a liability of the Mission. In management's opinion, disallowed claims, if any, would not have a material adverse effect on the Mission's financial position or results of operations.

In April, 2008, the Mission executed a Deed of Trust covering the Transitional Living Center (TLC) in favor of the Federal Home Loan Bank of Dallas (FHLBD) in exchange for funding in the amount of \$350,000. The funds were used to partially rehabilitate the TLC and, under the Agreement, the Mission must continue to use the facility to meet the needs of the homeless for a fifteen-year term. Repayment would be required if the Mission were to change the use or sell the property. The Mission also has certain annual reporting requirements under the Agreement. On April 27, 2016, the Mission sold the TLC and was required by the FHLBD to retain \$350,000 of the sale proceeds in escrow. Under the terms of the Escrow Agreement, the FHLBD released the Deed of Trust covering the TLC and the escrowed funds to the Mission on July 28, 2017. On October 6, 2017, the Mission executed a Deed of Trust covering the residential buildings at the Women and Family Development Center (WFDC) in favor of FHLBD for the remainder of the fifteen-year term.

In April, 2008, the Mission executed a Deed of Trust covering the Women & Family Emergency Shelter (W&F Shelter) in favor of FHLBD in exchange for funding of a grant in the amount of \$350,000. The funds were used to partially rehabilitate the shelter and under the agreement, the Mission must continue to use the facility to meet the needs of the homeless for a fifteen-year term. Repayment would be required if the Mission were to change the use or sell the property. The Mission also has certain annual reporting requirements under the Agreement. Prior to the sale of the W&F Shelter on September 15, 2017, FHLBD released the Deed of Trust. On October 6, 2017, the Mission executed a Deed of Trust covering the residential buildings at the WFDC in favor of FHLBD for the remainder of the fifteen-year term.

NOTE M COMMITMENTS AND CONTINGENCIES (CONTINUED)

In August, 2011, the Mission executed a Deed of Trust covering the Men's Development Center in favor of the FHLBD in exchange for funding of a grant in the amount of \$500,000. The funds were used to partially rehabilitate the shelter and under the Agreement, the Mission must continue to use the facility to meet the needs of the homeless for a fifteen-year term. Repayment would be required if the Mission were to change the use or sell the property. The Mission also has certain annual reporting requirements under the Agreement.

In March 2012, the City of Houston (City), under the Community Development Block Grant program, granted \$300,000 to help fund the upgrade of the HVAC system at the W&F Shelter. Under the terms of the agreement, the Mission could incur a liability if it sells, transfers or assigns its interest in the facility prior to July 16, 2018. This grant was amended on January 27, 2017, whereby the City agreed to allow the Mission to transfer the final year of the grant agreement to the residential buildings at WFDC, and not to incur any liability under the grant when the Mission sold the W&F Shelter.

On January 27, 2017, the Mission entered into a performance based loan in the amount of \$800,000 with the City for use in construction of certain residential buildings at Cornerstone. Under the terms of the agreement, the loan balance is automatically reduced by \$160,000 each year (at no liability to the Mission) until it expires in five years. The Mission would be required to pay off the unpaid principal balance if it sells, transfers or assigns its interest in the facility within the five-year period.

On January 8, 2018, the Mission executed a Deed of Trust covering the single women's residential building at Cornerstone in favor of the FHLBD in exchange for funding of a grant in the amount of \$500,000. The funds were used to partially finance construction of the building and under the agreement, the Mission must continue to use the facility to meet the needs of the homeless for a fifteen-year term. Repayment would be required if the Mission were to change the use or sell the property. The Mission also has certain annual reporting requirements under the agreement.

NOTE N SUBSEQUENT EVENTS

The Mission has evaluated subsequent events through June 4, 2018, the date the financial statements were available to be issued. No subsequent events occurred or require adjustment or additional disclosure to the financial statements.