

**The F.B. Heron Foundation**

Financial Statements

December 31, 2017 and 2016

## **Independent Auditors' Report**

### **Board of Directors The F.B. Heron Foundation**

We have audited the accompanying financial statements of The F.B. Heron Foundation, which comprise the statements of financial position as of December 31, 2017 and 2016, and the related statements of activities and cash flows for the years 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 audits. We conducted our audits 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 The F.B. Heron Foundation as of December 31, 2017 and 2016 and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

### ***Report on Supplementary Information***

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The schedules of program, administrative and investment expenses on page 13 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*PKF O'Connor Davies, LLP*

May 29, 2018

## The F.B. Heron Foundation

### Statements of Financial Position

	December 31	
	<u>2017</u>	<u>2016</u>
<b>ASSETS</b>		
Cash and cash equivalents	\$ 2,799,248	\$ 1,797,291
Investments allocated for mission	306,263,599	273,195,480
Prepaid Federal excise taxes	31,000	36,000
Other assets	<u>826,242</u>	<u>819,409</u>
	<u>\$ 309,920,089</u>	<u>\$ 275,848,180</u>
<b>LIABILITIES AND NET ASSETS</b>		
Liabilities		
Accounts payable and accrued expenses	\$ 568,873	\$ 468,053
Grants payable	39,750	16,000
Deferred rent	68,898	91,863
Deferred Federal excise tax	<u>1,149,857</u>	<u>538,660</u>
Total Liabilities	1,827,378	1,114,576
Unrestricted net assets	<u>308,092,711</u>	<u>274,733,604</u>
	<u>\$ 309,920,089</u>	<u>\$ 275,848,180</u>

See notes to financial statements

## The F.B. Heron Foundation

### Statements of Activities

	Year Ended	
	December 31	
	2017	2016
<b>INVESTMENTS ALLOCATED FOR MISSION</b>		
Revenue		
Interest, dividends and partnership earnings	\$ 7,179,221	\$ 4,349,436
Realized gain (loss)	6,644,093	(933,938)
Unrealized gain, net of deferred Federal excise tax	29,848,657	11,403,267
Program service fees (USCII license fee)	92,500	92,500
Current Federal excise tax	(201,000)	(55,740)
Net Revenue for Investments Allocated for Mission	43,563,471	14,855,525
Expenses		
Program expenses	3,540,073	3,546,481
Administrative expenses	946,547	1,044,633
Investment expenses	1,512,316	1,378,541
Total Expenses for Investments Allocated for Mission	5,998,936	5,969,655
Excess of Revenue over Expenses for Investments Allocated for Mission Before Grant Expense	37,564,535	8,885,870
Grants	4,205,428	8,207,495
Excess of Revenue over Expenses for Investments Allocated for Mission	33,359,107	678,375
<b>NON-MISSION INVESTMENTS</b>		
Revenue		
Interest, dividends and partnership earnings	-	2,017,524
Realized loss	-	(4,871,098)
Unrealized gain, net of deferred Federal excise tax	-	4,386,822
Current Federal excise tax	-	(35,327)
Net Revenue for Non-Mission Investments	-	1,497,921
Expenses		
Investment expenses	-	134,662
Excess of Revenue over Expenses for Non-Mission Investments	-	1,363,259
Change in Net Assets	33,359,107	2,041,634
<b>NET ASSETS</b>		
Beginning of year	274,733,604	272,691,970
End of year	\$ 308,092,711	\$ 274,733,604

See notes to financial statements

## The F.B. Heron Foundation

### Statements of Cash Flows

	Year Ended	
	December 31	
	2017	2016
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in net assets	\$ 33,359,107	\$ 2,041,634
Adjustments to reconcile change in net assets to net cash from operating activities		
Realized and unrealized gain on investments	(37,103,947)	(10,326,152)
Deferred Federal excise tax	611,197	341,099
Deferred rent	(22,965)	(22,965)
Net change in operating assets and liabilities		
Prepaid Federal excise taxes	5,000	51,067
Other assets	(6,833)	(9,987)
Accounts payable and accrued expenses	100,820	(127,034)
Grants payable	23,750	(43,250)
Net Cash from Operating Activities	(3,033,871)	(8,095,588)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of non-mission investments	-	(2,010,418)
Proceeds from non-mission investments sold	-	70,555,128
Purchases of investments allocated for mission	(55,067,351)	(111,669,097)
Proceeds from investments allocated for mission sold or repaid	59,103,179	46,487,861
Net Cash from Investing Activities	4,035,828	3,363,474
Net Change in Cash and Cash Equivalents	1,001,957	(4,732,114)
<b>CASH AND CASH EQUIVALENTS</b>		
Beginning of year	1,797,291	6,529,405
End of year	\$ 2,799,248	\$ 1,797,291
<b>SUPPLEMENTAL DISCLOSURE</b>		
Federal excise tax paid	\$ 196,000	\$ 40,000

See notes to financial statements

## The F.B. Heron Foundation

Notes to Financial Statements  
December 31, 2017 and 2016

### 1. Organization

The F.B. Heron Foundation (doing business as “Heron” and referred to herein as the “Foundation”) is a not-for-profit, charitable corporation formed in December 1991 under the General Corporation Law of the State of Delaware. The Foundation is exempt from income tax under Section 501(c)(3) of the Internal Revenue Code (the Code) and is classified as a private foundation under Section 509(a) of the Code.

To advance its mission of helping people and communities to help themselves out of poverty, the Foundation makes grants and loans and takes equity stakes in organizations and funds that advance systemic improvements to help communities be resilient to the changing nature of the economy.

### 2. Summary of Significant Accounting Policies

#### *Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (US GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingencies at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

#### *Cash Equivalents*

Cash equivalents include short-term investments with maturities of three months or less at the time of purchase, which are intended to be used for payment of expenses and grants and exclude those amounts used by investment managers for long-term investment strategies.

#### *Fair Value Measurements*

The Foundation follows US GAAP guidance on *Fair Value Measurements* which defines fair value and establishes a fair value hierarchy organized into three levels based upon the input assumptions used in pricing assets. Level 1 inputs have the highest reliability and are related to assets with unadjusted quoted prices in active markets. Level 2 inputs relate to assets with other than quoted prices in active markets which may include quoted prices for similar assets or liabilities or other inputs which can be corroborated by observable market data. Level 3 inputs are unobservable inputs and are used to the extent that observable inputs do not exist.

The Foundation follows US GAAP guidance which removes the requirements to categorize within the fair value hierarchy alternative investments where fair value is measured using the Net Asset Value (“NAV”) per share as a practical expedient.

## **The F.B. Heron Foundation**

Notes to Financial Statements  
December 31, 2017 and 2016

### **2. Summary of Significant Accounting Policies (continued)**

#### ***Investments Valuation***

Investments with the exception of program related investments, are stated at fair value. For insured deposits, fair value is the amount of the deposit.

#### ***Program Related Investments***

Program related investments (PRIs) defined in IRC 4944(c), have a primary purpose of advancing the mission of the Foundation without a significant purpose for the production of income or the appreciation of property. PRIs are treated as charitable distributions on Internal Revenue Service Form 990-PF, the tax and information return filed by private foundations for minimum-distribution requirement purposes. The Foundation's PRIs are considered below market rate loans and equities. They are stated at cost, less any valuation allowance for discount or uncollectable amounts.

#### ***Property and Equipment***

Property and equipment are stated at cost. The Foundation capitalizes property and equipment costing more than \$100,000. Depreciation was computed using the straight-line method over the estimated useful life of the assets. The estimated useful lives ranged from five to seven years. Leasehold improvements were amortized over the life of the original lease. There was no capitalized property and equipment at December 31, 2017 and 2016.

#### ***Net Asset Presentation***

Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the Foundation's net assets are classified as permanently restricted, temporarily restricted or unrestricted. There were no temporarily or permanently restricted net assets at December 31, 2017 and 2016.

#### ***Investment Income Recognition***

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis and dividends are recorded on the ex-dividend date. Realized and unrealized gains and losses are included in the determination of the change in net assets.

#### ***Grants***

Once a grant has been approved by the Board of Directors and/or President, and once any conditions imposed on the grantee have been fulfilled, the grant becomes payable and is recorded by the Foundation.



## The F.B. Heron Foundation

Notes to Financial Statements  
December 31, 2017 and 2016

### 2. Summary of Significant Accounting Policies (*continued*)

#### ***Accounting for Uncertainty in Income Taxes***

The Foundation recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Management has determined that the Foundation had no uncertain tax positions that would require financial statement recognition of disclosure.

#### ***Subsequent Events Evaluation by Management***

Management has evaluated subsequent events for disclosure and/or recognition in the financial statements through the date that the financial statements were available to be issued, which is May 29, 2018.

#### ***Reclassifications***

Certain 2016 amounts have been reclassified to conform to the current year presentation.

### 3. Investments Allocated for Mission

Investments allocated for mission advance the mission of the Foundation using the strategies articulated in Note 1. These include both risk-adjusted, market-rate investments that advance the mission as well as PRIs.

The Foundation's PRI loans bear interest at below-market rates from 1% to 6% and are generally payable on March 31 and September 30 of each year. PRI loans are individually monitored to determine net realizable value based on an evaluation of recovery. Management has reviewed the collectability of all PRI loans and deemed an allowance to be unnecessary at December 31, 2017 and 2016.

PRI equities consist of eight PRIs in LP and LLC interests in community development ventures and real estate funds, one PRI in preferred stock in a regulated community bank and one direct equity investment. PRI equity balances are net of a \$4,000,000 and \$3,900,000 valuation reserve at December 31, 2017 and 2016.

## The F.B. Heron Foundation

Notes to Financial Statements  
December 31, 2017 and 2016

### 3. Investments Allocated for Mission *(continued)*

The following are major categories of investments allocated for mission measured at fair value on a recurring basis at December 31, grouped by the fair value hierarchy, for those investments subject to categorization within such hierarchy:

	2017			Total
	(Level 1)	(Level 2)	(Practical Expedient) *	
At Fair Value				
Common and Preferred Stocks				
Information technology	\$ 22,269,200	\$ -	\$ -	\$ 22,269,200
Consumer discretionary	8,991,366	-	-	8,991,366
Health care	14,472,361	-	-	14,472,361
Other	49,434,586	-	-	49,434,586
Commingled Funds	-	44,348,758	-	44,348,758
Ishares MSCI	69,336,530	-	-	69,336,530
Fixed-Income Securities				
US agency	-	30,859,061	-	30,859,061
Municipals	-	17,965,776	-	17,965,776
Corporate	-	25,960,518	-	25,960,518
Limited partnership interests	-	-	10,592,115	10,592,115
Total at Fair Value	<u>\$ 164,504,043</u>	<u>\$ 119,134,113</u>	<u>\$ 10,592,115</u>	294,230,271
Program related investments, at cost (net of \$4,000,000 valuation reserve)				9,580,640
Invested cash and cash equivalents, at cost				2,452,688
Total Investments Allocated for Mission				<u>\$ 306,263,599</u>
	2016			
	(Level 1)	(Level 2)	(Practical Expedient) *	Total
At Fair Value				
Common and Preferred Stocks				
Information technology	\$ 16,579,499	\$ -	\$ -	\$ 16,579,499
Consumer discretionary	9,266,397	-	-	9,266,397
Health care	11,769,995	-	-	11,769,995
Other	44,194,257	-	-	44,194,257
Commingled Funds	-	27,659,795	-	27,659,795
Ishares MSCI	64,357,540	-	-	64,357,540
Fixed-Income Securities				
US agency	-	27,310,303	-	27,310,303
Municipals	-	19,382,489	-	19,382,489
Corporate	-	23,384,052	-	23,384,052
Limited partnership interests	-	-	10,610,441	10,610,441
Total at Fair Value	<u>\$ 146,167,688</u>	<u>\$ 97,736,639</u>	<u>\$ 10,610,441</u>	254,514,768
Program related investments, at cost (net of \$3,900,000 valuation reserve)				12,791,504
Invested cash and cash equivalents, at cost				5,889,208
Total Investments Allocated for Mission				<u>\$ 273,195,480</u>

\* As discussed in Note 2, investments that are measured using the practical expedient are not classified within the fair value hierarchy.

## The F.B. Heron Foundation

Notes to Financial Statements  
December 31, 2017 and 2016

### 3. Investments Allocated for Mission *(continued)*

The following is a reconciliation of the beginning and ending balances for preferred stock assets (Level 3):

	2017	2016
Beginning balance	\$ -	\$ 250,000
Unrealized loss	-	(250,000)
Purchases, issuances and settlements	-	-
Ending balance	\$ -	\$ -

Information regarding limited partnership interests at December 31, 2017 is as follows:

	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Limited partnership interests	\$ 10,592,115	\$ 6,753,312	*	*

\* Limited partnership interests are illiquid assets.

The following summarizes changes in PRIs for 2017 and 2016:

	2017			2016		
	PRI Loans	PRI Equities	Total	PRI Loans	PRI Equities	Total
Balance at beginning of year	\$10,484,522	\$2,306,982	\$12,791,504	\$11,932,232	\$2,356,401	\$14,288,633
Additions						
Disbursements	117,431	1,071,499	1,188,930	2,344,517	1,013,867	3,358,384
Deductions						
Repayments	(3,230,183)	(1,069,611)	(4,299,794)	(3,792,227)	(163,286)	(3,955,513)
Writeoffs	-	-	-	-	-	-
	7,371,770	2,308,870	9,680,640	10,484,522	3,206,982	13,691,504
Valuation adjustment	-	(100,000)	(100,000)	-	(900,000)	(900,000)
Balance at end of year	\$ 7,371,770	\$ 2,208,870	\$ 9,580,640	\$10,484,522	\$ 2,306,982	\$ 12,791,504

There is an additional \$3,318,448 of unfunded commitments for equity PRI investments.

## The F.B. Heron Foundation

Notes to Financial Statements  
December 31, 2017 and 2016

### 3. Investments Allocated for Mission (*continued*)

PRI loan principal repayments at December 31, 2017 are projected as follows:

2018	\$ 1,437,886
2019	580,119
2020	2,470,758
2021	-
2022	1,500,000
Thereafter	<u>1,383,007</u>
	<u>\$ 7,371,770</u>

PRI equity investments will be redeemed over the next ten years depending on investment performance and activity.

### 4. Grants Payable

The following summarizes changes in grants payable for the years ended December 31:

	<u>2017</u>	<u>2016</u>
Balance at beginning of year	\$ 16,000	\$ 59,250
Grants authorized	4,205,428	8,207,495
Grants paid	<u>(4,181,678)</u>	<u>(8,250,745)</u>
Balance at end of year	<u>\$ 39,750</u>	<u>\$ 16,000</u>

There are an additional \$2,185,000 of conditional grant payments at December 31, 2017 which will become payable once the appropriate conditions have been met.

### 5. Federal Excise Tax

As a private foundation, the Foundation is normally subject to a Federal excise tax equal to 2% of its net investment income. However, under Section 4940(e) of the Code, this tax is reduced to 1% if certain conditions are met. Current taxes are estimated at 2% of net investment income, as defined in the Code.

The Foundation records a liability for deferred Federal excise taxes using the 2% rate. For 2017 and 2016 the deferred excise tax provision amounted to \$611,197, and \$341,099.

For Federal excise tax purposes, realized gains and losses from the sale of securities are determined on the specific-identification basis. Net realized gain or loss is based on the Foundation's allocated share, and, on sale, average cost is used.

## **The F.B. Heron Foundation**

Notes to Financial Statements  
December 31, 2017 and 2016

### **6. Lease Commitment**

The Foundation's office lease was set to expire on December 31, 2020, however, the Foundation entered into a lease termination agreement which accelerated the expiration date to May 31, 2018. Subsequent to year-end, the Foundation entered into a new lease on January 15, 2018, which expires on December 31, 2018.

Rent expense for 2017 and 2016 was \$360,935 and \$350,155.

### **7. Retirement Plans**

The Foundation sponsors a defined contribution retirement plan under IRC Section 401(a). Under the current plan, the Foundation contributes 12% of the basic compensation for all eligible employees subject to IRS and ERISA limitations. The Foundation also sponsors a 401(k) savings plan. Eligible participants, as defined, may make voluntary contributions into the savings plan. The Foundation is obligated to match 50% of participant contributions, not to exceed 3% of base compensation. For 2017 and 2016, retirement and savings plan expense was \$332,728 and \$312,483.

\* \* \* \* \*

**The F.B. Heron Foundation**

Supplementary Information

Years Ended December 31, 2017 and 2016

## The F.B. Heron Foundation

### Schedules of Program, Administrative and Investment Expenses Year Ended December 31

	2017					2016				
	Investments Allocated for Mission			Non-Mission Investments	Total	Investments Allocated for Mission			Non-Mission Investments	Total
	Program	Administrative	Investment	Investment		Program	Administrative	Investment	Investment	
Salary and related costs	\$ 2,251,937	\$ 558,203	\$ 506,576	\$ -	\$ 3,316,716	\$ 1,880,022	\$ 608,522	\$ 644,333	\$ 21,801	\$ 3,154,678
Consulting fees	499,534	15,656	54,634	-	569,824	609,110	16,591	26,943	593	653,237
Occupancy	260,733	64,630	58,652	-	384,015	220,897	71,500	75,707	2,562	370,666
Investment monitoring and advisory	103,746	-	242,074	-	345,820	244,498	67,048	70,994	2,402	384,942
Outsourced functions	-	206,550	-	-	206,550	-	181,248	-	-	181,248
Market data	101,610	-	48,870	-	150,480	145,152	-	-	-	145,152
Travel, meetings, and conferences	189,829	20,376	20,376	-	230,581	229,415	16,111	-	-	245,526
Office expenses	62,296	6,325	5,740	-	74,361	155,540	44,646	47,274	1,600	249,060
Legal fees	-	53,924	22,967	-	76,891	-	15,784	29,873	-	45,657
Audit expenses	24,052	5,962	5,411	-	35,425	21,112	6,833	7,235	245	35,425
Equipment expenses	24,758	6,137	5,569	-	36,464	21,821	7,063	7,478	253	36,615
Insurance	21,578	5,349	4,854	-	31,781	18,914	6,122	6,482	219	31,737
Bank fees	-	3,435	-	-	3,435	-	3,165	-	-	3,165
Custody fees	-	-	90,406	-	90,406	-	-	60,369	-	60,369
Asset management	-	-	446,187	-	446,187	-	-	401,853	104,987	506,840
	<u>\$ 3,540,073</u>	<u>\$ 946,547</u>	<u>\$ 1,512,316</u>	<u>\$ -</u>	<u>\$ 5,998,936</u>	<u>\$ 3,546,481</u>	<u>\$ 1,044,633</u>	<u>\$ 1,378,541</u>	<u>\$ 134,662</u>	<u>\$ 6,104,317</u>

See independent auditors' report