The F.B. Heron Foundation

Financial Statements

December 31, 2018 and 2017

PKF O'CONNOR DAVIES
ACCOUNTANTS AND ADVISORS

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, 2018 and 2017, and the related statements of activities, functional expenses 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.

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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, 2018 and 2017 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.

Change in Accounting Principle

As discussed in note 2 to the financial statements, during the year ended December 31, 2018 The F.B. Heron Foundation adopted new accounting guidance resulting in a change in the manner in which it presents net assets and reports certain aspects of its financial statements. Our opinion is not modified with respect to this matter.

PKF O'Connor Davies, LLP

June 24, 2019

The F.B. Heron Foundation

Statements of Financial Position

	December 31	
	2018	2017
ASSETS		
Cash and cash equivalents	$ 1,616,720	$ 2,799,248
Investments, net	281,412,730	306,263,599
Prepaid Federal excise taxes	2,000	31,000
Other assets	847,378	826,242
	$ 283,878,828	$ 309,920,089
LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable and accrued expenses	$ 617,611	$ 568,873
Grants payable	-	39,750
Deferred rent	-	68,898
Deferred Federal excise tax	642,025	1,149,857
Total Liabilities	1,259,636	1,827,378
Net assets, without donor restrictions	282,619,192	308,092,711
	$ 283,878,828	$ 309,920,089

See notes to financial statements

The F.B. Heron Foundation

Statements of Activities

	Year Ended December 31	
	2018	2017
REVENUE		
Net return on investments	$ (11,913,774)	$ 42,681,160
Program service fees (USCII license fee)	72,570	92,500
Current Federal excise tax	(249,000)	(201,000)
Total Revenue	(12,090,204)	42,572,660
EXPENSES		
Program (including grants of $8,903,545 and $4,205,428)	12,151,372	7,745,501
Administrative	736,941	946,547
Indirect Investment	495,002	521,505
Total Expenses	13,383,315	9,213,553
Change in Net Assets	(25,473,519)	33,359,107
NET ASSETS, WITHOUT DONOR RESTRICTIONS		
Beginning of year	308,092,711	274,733,604
End of year	$ 282,619,192	$ 308,092,711

See notes to financial statements

The F.B. Heron Foundation

Statements of Functional Expenses
Year Ended December 31

	2018						2017					
	Program	Administrative	Indirect Investment	Sub Total	Direct Investment	Total	Program	Administrative	Indirect Investment	Sub Total	Direct Investment	Total
Salary and related costs	$ 2,270,539	$ 492,308	$ 207,808	$ 2,970,655	$ 184,396	$ 3,155,051	$ 2,251,937	$ 558,203	$ 268,408	$ 3,078,548	$ 238,168	$ 3,316,716
Consulting fees	205,538	885	374	206,797	51,718	258,515	499,534	15,656	7,528	522,718	47,106	569,824
Occupancy	273,588	59,321	25,040	357,949	22,219	380,168	245,062	60,745	29,209	335,016	25,918	360,934
Investment monitoring and advisory	42,638	-	120,806	163,444	120,806	284,250	103,746	-	121,037	224,783	121,037	345,820
Outsourced functions	-	139,448	-	139,448	-	139,448	-	206,550	-	206,550	-	206,550
Market data	108,027	-	113,418	221,445	-	221,445	101,610	-	48,870	150,480	-	150,480
Travel, meetings, and conferences	179,922	9,981	4,846	194,749	14,538	209,287	189,829	20,376	10,188	220,393	10,188	230,581
Office expenses	93,886	10,241	4,323	108,450	3,836	112,286	77,967	10,210	4,908	93,085	4,357	97,442
Legal fees	-	7,114	11,643	18,757	-	18,757	-	53,924	22,967	76,891	-	76,891
Audit expenses	27,653	5,996	2,531	36,180	2,246	38,426	24,052	5,962	2,867	32,881	2,544	35,425
Equipment expenses	25,089	5,440	2,296	32,825	2,038	34,863	24,758	6,137	2,951	33,846	2,618	36,464
Insurance	20,947	4,542	1,917	27,406	1,701	29,107	21,578	5,349	2,572	29,499	2,282	31,781
Bank fees	-	1,665	-	1,665	-	1,665	-	3,435	-	3,435	-	3,435
Custody fees	-	-	-	-	93,354	93,354	-	-	-	-	90,406	90,406
Asset management	-	-	-	-	469,423	469,423	-	-	-	-	446,187	446,187
Grants	8,903,545	-	-	8,903,545	-	8,903,545	4,205,428	-	-	4,205,428	-	4,205,428
	$ 12,151,372	$ 736,941	$ 495,002	$ 13,383,315	$ 966,275	$ 14,349,590	$ 7,745,501	$ 946,547	$ 521,505	$ 9,213,553	$ 990,811	$ 10,204,364

See notes to financial statements

The F.B. Heron Foundation

Statements of Cash Flows

	Year Ended December 31 2018	Year Ended December 31 2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	$ (25,473,519)	$ 33,359,107
Adjustments to reconcile change in net assets to net cash from operating activities		
Realized and unrealized loss (gain) on investments	17,196,838	(37,103,947)
Deferred Federal excise tax	(507,832)	611,197
Deferred rent	(68,898)	(22,965)
Net change in operating assets and liabilities		
Prepaid Federal excise taxes	29,000	5,000
Other assets	(21,136)	(6,833)
Accounts payable and accrued expenses	48,738	100,820
Grants payable	(39,750)	23,750
Net Cash from Operating Activities	(8,836,559)	(3,033,871)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(49,672,328)	(55,067,351)
Proceeds from investments	57,326,359	59,103,179
Net Cash from Investing Activities	7,654,031	4,035,828
Net Change in Cash and Cash Equivalents	(1,182,528)	1,001,957
CASH AND CASH EQUIVALENTS		
Beginning of year	2,799,248	1,797,291
End of year	$ 1,616,720	$ 2,799,248
SUPPLEMENTAL DISCLOSURE		
Federal excise tax paid	$ 220,000	$ 196,000

See notes to financial statements

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.

Change in Accounting Principle

On January 1, 2018, the Foundation adopted new guidance regarding the Presentation of Financial Statements for Not-for-Profit Entities. This guidance requires the Foundation to collapse the three-category (unrestricted, temporarily restricted, and permanently restricted) classification of net assets into two categories: with donor restrictions and without donor restrictions. In addition, the new guidance requires the Foundation to make certain expanded disclosures relating to (1) the liquidity of financial assets, and (2) expenses by both their natural and functional classification in one location in the financial statements.

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.

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

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.

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, 2018 and 2017.

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 without donor restrictions or with donor restrictions. There were no net assets with donor restrictions at December 31, 2018 and 2017.

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

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.

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 June 24, 2019.

Reclassifications

Certain 2017 amounts have been reclassified to conform to the current year presentation.

3. Investments

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 3.5% 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, 2018 and 2017.

PRI equities consist of seven 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 two direct equity investments. PRI equity balances are net of a $3,800,000 and $4,000,000 valuation reserve at December 31, 2018 and 2017.

3. Investments *(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:

2018	(Level 1)	(Level 2)	(Level 3)	(Practical Expedient) *	Total
At Fair Value					
Common and Preferred Stocks					
Information technology	$ 25,397,834	$ -	$ -	$ -	$ 25,397,834
Consumer discretionary	7,032,964	-	-	-	7,032,964
Health care	18,689,489	-	-	-	18,689,489
Other	47,643,700	-	500,000	-	48,143,700
Commingled funds	-	32,598,160	-	-	32,598,160
Ishares MSCI	50,247,740	-	-	-	50,247,740
Fixed-Income Securities					
US agency	-	28,151,560	-	-	28,151,560
Municipals	-	16,269,089	-	-	16,269,089
Corporate	-	27,948,883	-	-	27,948,883
Limited partnership interests	-	-	-	12,877,365	12,877,365
Total at Fair Value	$ 149,011,727	$ 104,967,692	$ 500,000	$ 12,877,365	267,356,784
Program related investments, at cost (net of $3,800,000 valuation reserve)					8,456,346
Invested cash and cash equivalents, at cost					5,599,600
Total Investments Allocated for Mission					$ 281,412,730

2017	(Level 1)	(Level 2)	(Level 3)	(Practical Expedient) *	Total
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	$ 164,504,043	$ 119,134,113	$ -	$ 10,592,115	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					$ 306,263,599

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

3. Investments *(continued)*

Net return on investments consists of the following:

	2018	2017
Interest, dividends and partnership earnings	$ 5,741,507	$ 7,179,221
Realized gain	7,994,774	6,644,093
Unrealized (loss) gain, net of deferred Federal excise tax	(24,683,780)	29,848,657
Direct investment expenses	(966,275)	(990,811)
	$ (11,913,774)	$42,681,160

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

	2018	2017
Beginning balance	$ -	$ -
Purchases, issuances and settlements	500,000	-
Ending balance	$ 500,000	$ -

Information regarding limited partnership interests and preferred stock at December 31, 2018 is as follows:

	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Limited partnership interests	$ 12,877,365	$ 7,526,100	*	*
Preferred stock	500,000	-	*	*
	$ 13,377,365	$ 7,526,100		

* Limited partnership interests and preferred stock are illiquid assets.

The Foundation invests across a broad spectrum of investment vehicles, strategies, and asset classes in order to both achieve a financial return, and achieve a social return consistent with the Foundation’s mission of helping people and communities help themselves out of poverty. The Foundation does not invest its assets exclusively for financial return. Investments include a range of opportunities, including risk-adjusted, market-rate investments as well as PRIs.

3. Investments *(continued)*

The following summarizes changes in PRIs for 2018 and 2017:

	2018			2017		
	PRI Loans	PRI Equities	Total	PRI Loans	PRI Equities	Total
Balance at beginning of year	$ 7,371,770	$ 2,208,870	$ 9,580,640	$ 10,484,522	$ 2,306,982	$ 12,791,504
Additions						
Disbursements	616,992	1,759,197	2,376,189	117,431	1,071,499	1,188,930
Deductions						
Repayments	(3,434,091)	(4,660)	(3,438,751)	(3,230,183)	(1,069,611)	(4,299,794)
Writeoffs	-	(261,732)	(261,732)	-	-	-
	4,554,671	3,701,675	8,256,346	7,371,770	2,308,870	9,680,640
Valuation adjustment	-	200,000	200,000	-	(100,000)	(100,000)
Balance at end of year	$ 4,554,671	$ 3,901,675	$ 8,456,346	$ 7,371,770	$ 2,208,870	$ 9,580,640

There is an additional $3,559,251 of unfunded commitments for equity PRI investments.

PRI loan principal repayments at December 31, 2018 are projected as follows:

2019	$ 54,671
2020	1,000,000
2021	-
2022	1,500,000
2023	2,000,000
	$ 4,554,671

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:

	2018	2017
Balance at beginning of year	$ 39,750	$ 16,000
Grants authorized	8,903,545	4,205,428
Grants paid	(8,943,295)	(4,181,678)
Balance at end of year	$ -	$ 39,750

There are an additional $1,800,000 of conditional grant payments at December 31, 2018 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 2018 and 2017 the deferred excise tax (benefit) provision amounted to $(507,832), and $611,197.

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, upon sale, average cost is used.

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. The Foundation entered into a new lease on January 15, 2018, which expired on December 31, 2018 and was renewed to December 31, 2019.

Rent expense for 2018 and 2017 was $380,168 and $360,934.

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 2018 and 2017, retirement and savings plan expense was $323,168 and $332,728.

8. Liquidity and Availability of Financial Assets

The following reflects the Foundation's financial assets and resources available to meet cash needs within the next twelve months:

Financial Assets	
Cash and cash equivalents	$ 1,616,720
Interest receivable	619,144
Investments	281,412,730
Total Financial Assets	283,648,594
Less:	
Contractual or donor imposed restriction amounts	
Funds held for long term investment	21,779,040
Financial assets available to meet general expenditures over the next twelve months	$ 261,869,554

The Foundation monitors its cash needs and availability on a regular basis, meeting weekly to review forecasted cash needs for investment capital calls, regular operations, and grant making. Regular operating expenses are approved annually during the annual budget process and monitored closely throughout the year. Grants are generally approved on a monthly basis. Following grant approvals, the Foundation reviews its cash forecasts and liquidates investments as needed. The majority of its investments are liquid and easily accessible and do not require more than 3 days' notice. The Foundation will generally attempt to draw first from investments that are seen as less mission-aligned.

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