

Sustainable Communities Fund

Financial Statements

December 31, 2020



TABLE OF CONTENTS

	<u>Page No.</u>
Independent Auditor's 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 AUDITOR'S REPORT

To the Board of Directors
Sustainable Communities Fund
Los Angeles, California

We have audited the accompanying financial statements of Sustainable Communities Fund (a California nonprofit corporation) ("SCF"), which comprise the statement of financial position as of December 31, 2020, 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.

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 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 auditor's 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 Sustainable Communities Fund as of December 31, 2020, 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.

Emphasis of Matter

As discussed in Note 8 to the financial statements, on March 11, 2020, the World Health Organization declared the novel strain of coronavirus (COVID-19) a global pandemic and recommended containment and mitigation measures worldwide. The total financial impact and duration cannot be reasonably estimated at this time. Our opinion is not modified with respect to that matter.

A handwritten signature in black ink that reads "Armanino LLP". The signature is written in a cursive, flowing style.

Armanino^{LLP}
Los Angeles, California

July 2, 2021

Sustainable Communities Fund
Statement of Financial Position
December 31, 2020

ASSETS

Cash and cash equivalents	\$ 2,056,407
Contributions receivable, net	732,419
Program-related investment assets, net, including interest receivable of \$25,389	1,900,139
Mission-related investment assets, net	<u>450,963</u>
Total assets	<u><u>\$ 5,139,928</u></u>

LIABILITIES AND NET ASSETS

Liabilities	
Accounts payable and accrued expenses	<u>\$ 32,801</u>
Total liabilities	<u>32,801</u>
Net assets	
Without donor restrictions	
Operating reserve	138,500
Designated for future funding commitments (Note 5)	283,000
General	<u>3,953,208</u>
Total without donor restrictions	4,374,708
With donor restrictions	<u>732,419</u>
Total net assets	<u><u>5,107,127</u></u>
Total liabilities and net assets	<u><u>\$ 5,139,928</u></u>

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

Sustainable Communities Fund
Statement of Activities
For the Year Ended December 31, 2020

	Without Donor Restrictions	With Donor Restrictions	Total
Revenues, gains, and other support			
Contributions			
Contributions, net	\$ 14,000	\$ 44,242	\$ 58,242
Net assets released from restriction	<u>457,858</u>	<u>(457,858)</u>	<u>-</u>
Total contributions	471,858	(413,616)	58,242
Interest income	<u>77,562</u>	<u>-</u>	<u>77,562</u>
Total revenues, gains, and other support	<u>549,420</u>	<u>(413,616)</u>	<u>135,804</u>
Functional expenses			
Program services	<u>250,950</u>	<u>-</u>	<u>250,950</u>
Support services			
Management and general	84,846	-	84,846
Fundraising	<u>36,943</u>	<u>-</u>	<u>36,943</u>
Total support services	<u>121,789</u>	<u>-</u>	<u>121,789</u>
Total functional expenses	<u>372,739</u>	<u>-</u>	<u>372,739</u>
Change in net assets from operations	176,681	(413,616)	(236,935)
Allowance for doubtful contributions receivable	<u>-</u>	<u>(49,286)</u>	<u>(49,286)</u>
Change in net assets	176,681	(462,902)	(286,221)
Net assets, beginning of year	<u>4,198,027</u>	<u>1,195,321</u>	<u>5,393,348</u>
Net assets, end of year	<u><u>\$ 4,374,708</u></u>	<u><u>\$ 732,419</u></u>	<u><u>\$ 5,107,127</u></u>

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

Sustainable Communities Fund
Statement of Functional Expenses
For the Year Ended December 31, 2020

	Program services	Management and general	Fundraising	Total
Accounting services	\$ -	\$ 22,525	\$ -	\$ 22,525
Allowance for loan losses	104,633	-	-	104,633
Bank charge	-	351	-	351
Conference, convention and meetings	451	-	-	451
Grant expenses	5,330	-	-	5,330
Insurance	1,320	1,107	-	2,427
Legal fees	493	1,650	-	2,143
Office expenses and supplies	2,152	2,251	-	4,403
Membership dues	1,000	75	-	1,075
Overhead fee	884	1,020	-	1,904
Payroll administration	18,184	6,350	4,329	28,863
Salaries	96,195	33,592	22,904	152,691
Staff and other consulting	15,768	13,595	7,500	36,863
Telephone and telecommunications	120	120	-	240
Website and marketing	4,420	2,210	2,210	8,840
	<u>\$ 250,950</u>	<u>\$ 84,846</u>	<u>\$ 36,943</u>	<u>\$ 372,739</u>

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

Sustainable Communities Fund
Statement of Cash Flows
For the Year Ended December 31, 2020

Cash flows from operating activities	
Change in net assets	\$ (286,221)
Adjustments to reconcile change in net assets to net cash provided by operating activities	
Increase in allowance for doubtful contributions receivable	49,286
Decrease in discounts on contributions receivable	(44,241)
Increase in allowance for doubtful program-related investments	75,250
Increase in allowance for doubtful mission-related investments	29,383
Changes in operating assets and liabilities	
Contributions receivable	457,857
Program-related investment assets	384,055
Mission-related investment assets	(87,912)
Accounts payable and accrued expenses	<u>8,533</u>
Net cash provided by operating activities	<u>585,990</u>
Net increase in cash and cash equivalents	585,990
Cash and cash equivalents, beginning of year	<u>1,470,417</u>
Cash and cash equivalents, end of year	<u><u>\$ 2,056,407</u></u>

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

Sustainable Communities Fund
Notes to Financial Statements
December 31, 2020

1. NATURE OF OPERATIONS

Sustainable Communities Fund ("SCF") has been established to alleviate poverty by supporting financial, economic and social inclusion strategies that empower people and strengthen low-income communities.

SCF is a private operating foundation which operates as a revolving investment fund capitalized by funds originating from investment activities generated primarily by National New Markets Fund ("NNMF"), a joint venture partnership between Strategic Development Solutions, LLC ("SDS") and Economic Innovations International ("EII"). SCF was created to revolve donations coming from NNMF's investment projects as well as other sources, into a new generation of investments benefiting very high-poverty communities or individuals. SCF achieves its mission by investing in organizations with innovative prototype lending or investing models that create significant social and environmental impacts. SCF particularly seeks organizations with new financing models that may need early stage seed funding where its investment can help them "prove" their model – and thus spur follow-on investors to bring additional resources to the effort.

SCF filed to terminate its foundation status and transition to a public charity on December 23, 2019, triggering the start of a five-year transition process. SCF will continue to be a private operating foundation through 2024. SCF has also filed for and received an advance ruling letter with the IRS to allow SCF to fundraise as a public charity during the five-year transition period.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Income tax status

SCF is exempt from federal income taxes under Section 501(c)(3) and is classified as a private operating foundation under Section 509(a) of the Internal Revenue Code. SCF is subject to federal excise taxes on its net investment income.

Basis of accounting and financial statement presentation

The financial statements of SCF have been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles ("GAAP") in the United States of America.

SCF reports information regarding its financial position and activities based on the existence or absence of donor imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

- *Without donor restrictions, operating reserve* - Includes net assets designated as an operating reserve.
- *Without donor restrictions, designated for future funding commitments* - Includes net assets designated for approved program-related investment assets ("PRIs") and mission-related investment assets ("MRIs") that have not yet been funded (see Note 5).

Sustainable Communities Fund
Notes to Financial Statements
December 31, 2020

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of accounting and financial statement presentation (continued)

- *Without donor restrictions, general* - Includes contributions, interest income, and other forms of revenue that are not restricted by the donor or grantor as well as expenditures related to the general operations of SCF.
- *With donor restrictions* - Includes net assets subject to donor (or certain grantor) imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both. At December 31, 2020, net assets with donor restrictions consisted of contributions receivable net of an allowance for uncollectible contributions and present value discount and are being reclassified to net assets without donor restrictions when paid.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and those differences could be material.

Cash and cash equivalents

SCF considers all cash and highly liquid financial instruments with original maturities of three months or less, which are neither held for nor restricted by donors for long-term purposes, to be cash and cash equivalents. Cash and highly liquid financial instruments restricted to building projects, endowments that are perpetual in nature, or other long-term purposes are excluded from this definition. There were no cash equivalents at December 31, 2020.

Program-related investment assets (PRIs)

SCF makes PRIs to other organizations to achieve its charitable purposes in alignment with SCF's strategies. At December 31, 2020, SCF had seven outstanding PRIs: one in the form of equity and six loans. Five of the PRI investments have been made with not-for-profit entities and two with for-profit entities.

PRIs are evaluated annually for impairment and no impairment losses were recorded during the year ended December 31, 2020. However, an allowance for loan losses was established given the general economic conditions.

Sustainable Communities Fund
Notes to Financial Statements
December 31, 2020

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Mission-related investment assets (MRIs)

SCF makes MRIs to other organizations to achieve its charitable purposes in alignment with SCF's strategies. MRIs are market-rate investments and, unlike PRIs, are not considered to be qualified distributions for tax purposes. At December 31, 2020, SCF had three outstanding MRIs in the form of two certificates of deposit and one equity investment. Two of the MRI investments have been made with not-for-profit entities and one with a for-profit entity.

MRIs are evaluated annually for impairment and no impairment losses were recorded during the year ended December 31, 2020. However, an allowance for loan losses was established given the general economic conditions.

PRI and MRI allowance for loan losses

SCF has the following process in determining its allowance for loan losses: SCF assesses each individual investment on its own to determine its individual contribution to the overall PRI or MRI allowance for loan losses.

Initial investment - At the time of reviewing a prospective investment, SCF underwriters assess organizational and project-level risks and assign a risk rating score of 1-5 (1= lowest risk). Each of these risk-rating scores has been assigned a percentage range of the dollar amount of the loan to be allocated to the allowance for loan losses. Underwriters assign this dollar amount for the allowance for loan losses as is deemed appropriate based on the specific perceived investment risk rating, and SCF will set aside this dollar amount into its respective PRI or MRI allowance for loan losses account as the investment funds deploy.

Annual re-assessment - Each investment is assessed annually for its level of risk during its annual asset management review or during an interim assessment if SCF learns of additional investment risks during the course of on-going borrower communications. Based on the new risk assessment, the allowance for loan losses may be increased or decreased as appropriate.

At the end of 2020, there was \$125,250 in the PRI allowance for loan losses which account for the seven PRI investments. Four of the PRI investments have been rated as Risk Level 1 and have 100% payment guarantees, and therefore SCF has not provided an allowance for the four Risk Level 1 investments. Three of the PRI investments have been rated as Risk Level 2 and SCF has provided an allowance equal to 5% - 10% of capital deployed.

At the end of 2020, there was \$34,543 in the MRI allowance for loan losses which account for the three MRI investments. Two of the MRI investments have been rated as Risk Level 1 and have 100% payment guarantees, and therefore SCF has not provided an allowance for the two Risk Level 1 investments. The third MRI investment has been rated as Risk Level 2 and SCF has provided an allowance equal to 15% of capital deployed.

Sustainable Communities Fund
Notes to Financial Statements
December 31, 2020

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

PRI and MRI allowance for loan losses (continued)

The PRI and MRI allowances also include a general allowance equal to 3.5% of capital deployed. This general allowance reflects management's best estimate of potential investment losses due to volatile financial market conditions related to the global pandemic experienced in 2020 (see Note 8).

Contributions receivable

SCF records unconditional promises to give that are expected to be collected within one year at net realizable value. Unconditional promises to give expected to be collected in future years are recorded as contributions receivable and are initially recorded at fair value using present value techniques incorporating risk-adjusted discount rates designed to reflect the assumptions market participants would use in pricing the asset. In subsequent years, amortization of the discounts is included in contribution revenue in the statement of activities. SCF determines the allowance for uncollectible promises to give based on historical experience, an assessment of economic conditions, and a review of subsequent collections. Promises to give are written off when deemed uncollectible. At December 31, 2020, management has recorded an allowance in the amount of \$49,286 for one specific contributions receivable balance. All other contributions receivable balances are considered to be fully collectible.

Revenue recognition

Contributions are recognized when cash, securities or other assets, an unconditional promise to give, or notification of a beneficial interest is received. Grant revenue is recognized consistent with the terms of the grant agreement. Deferred revenue represents cash received in excess of costs incurred on cost reimbursement grants.

Functional expenses

The costs of program and supporting services activities have been summarized on a functional basis in the statement of activities. The statement of functional expenses present the natural classification detail of expenses by function. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Subsequent events

SCF has evaluated events subsequent to December 31, 2020, to assess the need for potential recognition or disclosure in the financial statements. Such events were evaluated through July 2, 2021, the date the financial statements were available to be issued. Based upon this evaluation it was determined no subsequent events occurred that require recognition or additional disclosure in the financial statements.

Sustainable Communities Fund
Notes to Financial Statements
December 31, 2020

3. CONTRIBUTIONS RECEIVABLE AND NET ASSETS WITH DONOR RESTRICTIONS

Contributions receivable and net assets with donor restrictions consisted of the following:

Khan Family Office	\$ 340,000
Detroit Manufacturing Systems, LLC	53,571
Pizitz, LLC	197,143
American Tubing Arkansas, LLC	43,750
CMC Steel Oklahoma, LLC	78,750
The Westervelt Company	<u>80,000</u>
	793,214
Less: allowance for doubtful contributions receivable	(49,286)
Less: discount to present value	<u>(11,509)</u>
	<u><u>\$ 732,419</u></u>

Contributions receivable by year are as follows:

Due in less than 1 year	\$ 414,464
Due in 1 to 5 years	<u>378,750</u>
	793,214
Less: allowance for doubtful contributions receivable	(49,286)
Less: discount to present value	<u>(11,509)</u>
	<u><u>\$ 732,419</u></u>

SCF uses .55% as its present value discount factor which is based on an average of 5-year U.S. Treasury rates.

Donor-restricted net assets consist solely of contributions receivable, which are restricted as to time.

4. FEDERAL EXCISE TAXES

Beginning January 2020, Congress modified the excise tax on net investment income from a two-tier 1%/2% rate to a flat rate of 1.39%. The excise tax is imposed on net investment income, as defined under federal law, which includes interest, dividends, and net related gains on the sale of investments. Management records excise tax expense on the cash basis as the amount due is estimated to be de minimis.

5. INVESTMENT ASSETS

PRIs and MRIs are strategic investments, beyond grants, made by SCF for the specific objective of furthering SCF's charitable purpose. The production of income is not the primary objective of a PRI or an MRI.

Sustainable Communities Fund
Notes to Financial Statements
December 31, 2020

5. INVESTMENT ASSETS (continued)

Deployed

SCF's portfolio consists of ten investments at December 31, 2020, the majority of which are in support of economic development activities in low-income communities in the United States. They enable partner organizations to invest in small business development and entrepreneurship in select communities. Interest payments are due on the outstanding loan and certificate of deposit amounts at interest rates generally ranging between 1% and 4%.

Deployed investment assets are summarized in the table below as follows:

	<u>PRI</u> s	<u>MRI</u> s	<u>Total</u>
Beginning of year	\$ 2,382,027	\$ 397,594	\$ 2,779,621
Additional investments	-	610,237	610,237
Maturities and repayments	<u>(382,027)</u>	<u>(522,325)</u>	<u>(904,352)</u>
	2,000,000	485,506	2,485,506
Less: allowance for loan losses	(125,250)	(34,543)	(159,793)
Add: Interest receivable	<u>25,389</u>	<u>-</u>	<u>25,389</u>
End of year, net	<u><u>\$ 1,900,139</u></u>	<u><u>\$ 450,963</u></u>	<u><u>\$ 2,351,102</u></u>

Committed/Undeployed

SCF has one unfunded commitment at December 31, 2020 totaling \$283,000. This unfunded commitment consists of one MRI in the amount of \$400,000. Funding for the MRI requires formal capital calls from the investee. During 2020, the investee submitted capital calls totaling \$82,600 which SCF funded.

The future repayments of the program-related and mission-related investments are as follows:

Year ending December 31,

2021	\$ 612,048
2022	756,458
2023	300,000
2025	700,000
Thereafter	<u>117,000</u>
	<u><u>\$ 2,485,506</u></u>

Sustainable Communities Fund
Notes to Financial Statements
December 31, 2020

6. RELATED PARTY TRANSACTIONS

SCF has entered into a shared services agreement with SDS. SDS is owned by individuals that serve on the board of directors of SCF and are therefore considered disqualified persons under the Internal Revenue Code. SCF has determined that this arrangement qualifies as reimbursement for reasonable and necessary costs. Under the agreement, SCF will reimburse SDS for direct costs of services provided by SDS personnel (which includes a 7.5% overhead charge applied to this total), up to \$40,000 in 2020. Any services provided directly by disqualified persons are not charged to SCF. During 2020, costs reimbursable to SDS totaled \$31,269, of which \$5,602 was included in accounts payable and accrued expenses at December 31, 2020.

7. LIQUIDITY AND AVAILABILITY

SCF is significantly supported by contributions. SCF's liquidity management policy is designed to provide that its remaining financial assets are available for operations as its general expenditures, liabilities, and other obligations come due.

The following reflects SCF's financial assets reported on the statement of financial position, reduced by amounts not available for general use within one year because of contractual or time restrictions, or commitments to provide funding to identified investments. PRIs and MRIs have been excluded from this analysis, since they are not generally available for use in SCF's operations.

Liquidity of financial assets as of December 31, 2020 is as follows:

Financial assets	
Cash and cash equivalents	\$ 2,056,407
Contributions receivable, net	<u>732,419</u>
	<u>2,788,826</u>
Less: assets unavailable for general use	
Contributions receivable due past one year	(378,750)
Operating reserve	(138,500)
Designated for future funding commitments	<u>(283,000)</u>
	<u>(800,250)</u>
	<u>\$ 1,988,576</u>

Sustainable Communities Fund
Notes to Financial Statements
December 31, 2020

8. RISKS AND UNCERTAINTIES

On March 11, 2020, the World Health Organization declared the novel strain of coronavirus (COVID-19) a global pandemic and recommended containment and mitigation measures worldwide. By the end of 2020, there was still uncertainty regarding the impact the pandemic would have on the operations of SCF and the operations of SCF's investees. Since the end of 2020, the level of uncertainty has been significantly reduced and SCF's understanding of the impacts of the pandemic on its investees has been expanded. However, it is at least reasonably possible that this matter will negatively impact SCF, the ultimate financial impact and duration cannot be reasonably estimated at this time.