

SOSTENICA, INC.

REPORT ON AUDIT OF
FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2010

SOSTENICA, INC.

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INDEPENDENT AUDITOR'S REPORT

April 11, 2011

Board of Directors
SOSTENICA, INC.
West Chester, PA 19382

I have audited the accompanying statement of financial position of *SOSTENICA, INC.* (the Organization) as of December 31, 2010, and the related statements of activities and changes in net assets, functional expenses and cash flows for the year then ended. These financial statements are the responsibility of the Organization's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. I believe that my audit provides a reasonable basis for my opinion.

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Organization as of December 31, 2010 and the results of its activities and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Steven J. Handzel

SOSTENICA, INC.
STATEMENT OF FINANCIAL POSITION
DECEMBER 31, 2010

ASSETS

	Unrestricted	Temporarily Restricted	Total
CURRENT ASSETS			
Cash	\$ 92,864	13,572	106,436
Interest Receivable	78,725	-	78,725
Notes Receivable	536,543	-	536,543
Total Current Assets	708,132	13,572	721,704
 NON-CURRENT PORTION OF NOTES RECEIVABLE	 1,614,738	 -	 1,614,738
 PROPERTY, PLANT AND EQUIPMENT			
Furniture and Equipment	2,584	-	2,584
	2,584	-	2,584
Less: Accumulated Depreciation	(2,178)	-	(2,178)
	406	-	406
Total Assets	\$ 2,323,276	13,572	2,336,848

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES			
Accounts Payable	\$ 2,256	-	2,256
Accrued Interest Payable	29,815	-	29,815
Current Portion of Notes Payable	496,043	-	496,043
Total Current Liabilities	528,114	-	528,114
 NON-CURRENT PORTION OF NOTES PAYABLE	 1,422,738	 -	 1,422,738
 NET ASSETS			
Unrestricted	372,424	-	372,424
Temporarily Restricted	-	13,572	13,572
Total Net Assets	372,424	13,572	385,996
Total Liabilities and Net Assets	\$ 2,323,276	13,572	2,336,848

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

SOSTENICA, INC.
STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS
YEAR ENDED DECEMBER 31, 2010

	Unrestricted	Temporarily Restricted	Total
Income			
Contributions	\$ 26,849	-	26,849
Interest from Notes Receivable	146,418	-	146,418
Interest from Cash Deposits	369	-	369
Net Assets Released from Restrictions	-	-	-
Total	<u>173,636</u>	<u>-</u>	<u>173,636</u>
Expenses			
Program Services			
Micro-Lending Activities	87,830	-	87,830
Sustainable Agriculture Research & Training	37,224	-	37,224
Management and General	16,467	-	16,467
Fund Raising	4,171	-	4,171
Total	<u>145,692</u>	<u>-</u>	<u>145,692</u>
Net Operating Income	27,944	-	27,944
Net Assets, Beginning of Year	344,480	13,572	358,052
Net Assets, End of Year	<u>\$ 372,424</u>	<u>\$ 13,572</u>	<u>385,996</u>

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

SOSTENICA, INC.
STATEMENT OF FUNCTIONAL EXPENSES
YEAR ENDED DECEMBER 31, 2010

	<u>Program Expenses</u>				<u>Total</u>
	<u>Micro Lending Activities</u>	<u>Sustainable Development Research & Training</u>	<u>Management and General</u>	<u>Fund Raising</u>	
Salaries	\$ 21,000	7,600	9,000	3,000	40,600
Payroll Taxes	1,615	590	683	218	3,106
Employee Benefits	877	438	-	438	1,753
Interest on Notes and Loan Payable	57,886	-	-	-	57,886
Grants	-	27,807	-	-	27,807
Professional Fees (Accounting)	-	-	5,400	-	5,400
Seminars, Conference and Training	-	201	78	-	279
Printing	1,018	132	155	-	1,305
Insurance	-	-	251	-	251
Dues	125	-	-	-	125
Communications	795	291	107	336	1,529
Postage and Shipping	555	34	100	26	715
Travel	3,599	-	-	-	3,599
Bank Charges and Fees	-	-	474	-	474
Supplies	204	74	28	86	392
Licenses and Permits	-	-	170	-	170
	<u>87,674</u>	<u>37,167</u>	<u>16,446</u>	<u>4,104</u>	<u>145,391</u>
Depreciation	156	57	21	67	301
Total Expenses	<u>\$ 87,830</u>	<u>37,224</u>	<u>16,467</u>	<u>4,171</u>	<u>145,692</u>

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

SOSTENICA, INC.
STATEMENT OF CASH FLOWS
YEAR ENDED DECEMBER 31, 2010

Operating Cash Flows:	
Cash Received from:	
Contributions	\$ 26,849
Interest from Notes Receivable	144,549
Interest from Cash Deposits	369
Cash Paid to Employees and Suppliers	-
Cash Paid to Grantees	(27,807)
Interest Paid on Notes Payable	(55,927)
Net Operating Cash Flows	<u>88,033</u>
Financing Cash Flows:	
Cash Received from Issuance of Notes Payable	424,768
Cash Paid to Redeem Notes Payable	(329,558)
Cash Received from Redemption of Notes Receivable	366,558
Cash Paid to Acquire Notes Receivable	(455,768)
Net Financing Cash Flows	<u>6,000</u>
Investing Cash Flows	
Additions to Furniture and Equipment	-
Net Increase in Cash Balance	<u>94,033</u>
Cash: Beginning of Year	71,134
Cash: End of Year	<u>\$ 165,167</u>

Reconciliation of Operating Incomes to Net Cash Provided by Operations

Operating Income	\$ 27,944
Adjustments to Reconcile Operating Loss to Net Cash Utilized by Operations:	
Depreciation	301
Changes in Assets and Liabilities:	
Increase in Interest Receivable	(1,869)
Decrease in Prepaid Expense	690
Increase in Accounts Payable	277
Increase in Interest Payable	1,959
	<u>\$ 29,302</u>

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

SOSTENICA, INC.

NOTES TO FINANCIAL STATEMENTS

A. PURPOSE OF THE ORGANIZATION

The primary purpose of SOSTENICA, INC. (the Organization) is to link social investors in the United States and Europe with the micro-lending expertise of the *Center for the Promotion of Local Development (CEPRODEL)* in Nicaragua.

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accrual Basis

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

Basis of Presentation

The resources of the Organization are classified for accounting and reporting purposes into three net asset categories according to externally (donor) imposed restrictions. Unconditional promises to give (pledges) are recorded as receivables and revenues and are distinguished for each net asset category in accordance with donor-imposed restrictions. For the year ended December 31, 2010, the Organization had accounting transactions in only two of the net asset categories, as follows:

Unrestricted net assets - Net assets that are not subject to donor-imposed restrictions.

Temporarily restricted net assets - Net assets subject to donor-imposed restrictions that will be met by the passage of time or which will be fulfilled by actions of the Organization.

Cash and Cash Equivalents

For financial statement purposes, the Organization considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Cash overdrafts, if any, in operating bank accounts of the Organization are reclassified to accounts payable.

SOSTENICA, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, continued

Revenue and Support Recognition

Contributions are recognized as revenue when they are received or unconditionally pledged. The Organization reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and are reported in the statement of activities as net assets are released from restrictions.

The Organization accounts for grant and contract revenues, which are exchange transactions, in the statement of activities to the extent that expenses have been incurred for the purpose specified by the grantor during the period. In applying this concept, the legal and contractual requirements of each individual program are used as guidance. All moneys not expended in accordance with the grant or contract is recorded as a liability to the grantor as the Organization does not maintain any equity in the grant or contract. Additionally, funds received in advance of their proper usage are accounted for as deferred revenue in the statement of financial position.

Use of Estimates

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

Functional Allocation of Expenses

The costs of providing the various programs and activities have been summarized on a functional basis in the statement of activities. Accordingly, costs such as depreciation and certain administrative and maintenance expenses have been allocated among the programs and supporting services benefited. The majority of costs, however, are specifically allocable to program and support service functions.

SOSTENICA, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

C. MARKETABLE SECURITIES

The Organization occasionally receives contributions in the form of marketable securities. The Board of Directors has adopted a policy whereby such donations are liquidated upon receipt. Accordingly, there are no such assets reflected on the statement of financial position.

D. NOTES RECEIVABLE

Notes receivable are due from *CEPRODEL*. No allowance for uncollectible notes receivable is presented because *CEPRODEL* has not previously defaulted on its debt. However, *SOSTENICA* informs its lenders/investors that:

- *CEPRODEL* borrowers may present no collateral
- *CEPRODEL* borrowers may be under-collateralized
- *CEPRODEL* borrowers may be inexperienced and operate in a volatile economic environment
- The Nicaraguan economic environment has been very volatile
- There is no banking insurance in Nicaragua
- There is no guarantee that the loan loss reserve maintained by *CEPRODEL* will be adequate to cover all potential defaults
- The *SOSTENICA* Board and Staff are not professionals trained in managing a community development loan fund
- All notes receivable of *SOSTENICA* are held in Nicaragua and controlled by *CEPRODEL*
- Both the Organization and *CEPRODEL* maintain a combined equity capital share of not less than 15% of the total loan portfolio as a reserve against defaults by borrowers.

Notes receivable from *CEPRODEL* are denominated in United States dollars and accrue simple interest payable annually on each note. The entire portfolio earns interest at the rate of 7%.

Notes receivable are due throughout the year. Accordingly, while payments on each note are paid annually, the staggered due dates result in a regular stream of interest payments to the Organization.

SOSTENICA, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

D. NOTES RECEIVABLE, continued

It is the practice of the Organization to turn over funds to *CEPRODEL* for the purpose of issuing micro-loans in the form of notes receivable concurrent with the receipt of funds from lenders.

In addition to the notes receivable representing funds provided by Organization investors, an additional \$250,000 in notes receivable represents equity loans provided by donations and interest earnings.

E. PROPERTY, PLANT, EQUIPMENT AND DEPRECIATION

Property, plant and equipment are stated at cost if purchased. Expenditures of less than \$50.00 are expensed when incurred. Donated facilities and equipment are recorded at their fair market value at the date of receipt. When such assets are sold or otherwise disposed of, the cost and accumulated depreciation are removed from their respective accounts and any gain or loss on such disposition is recognized in the statement of activities.

Depreciation is provided on a straight-line basis over the estimated useful lives of the assets. One half year's depreciation is taken in the year of acquisition. Furniture and equipment are depreciated utilizing useful lives of 3-10 years.

F. NOTES PAYABLE

SOSTENICA issues notes that range in value from \$400 to \$100,000. The term of the notes range from 1 to 10 years with interest ranging from 0% to 5.50%. Simple interest is paid annually. Principal payment is due in full at the expiration of the term of the note. As of December 31, 2010 the notes carried a weighted average interest rate of 3.1% and mature as follows:

2011	\$496,043
2012	470,627
2013	287,231
2014	195,209
2015	191,168
Thereafter	278,503

SOSTENICA, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

G. DONATED MATERIALS AND SERVICES

Donated materials, equipment and furnishings are reflected as contributions in the accompanying statements at their estimated fair market value at date of receipt.

Donated services are those provided by individuals with specialized skills on a complimentary or discounted basis related to functions that would have to be purchased in the absence of the contributor.

No amounts have been reflected in the accompanying statements for donated services because officers, members of the Board of Directors or volunteers provided services not requiring specialized skills as defined by professional standards.

Office space for the Organization is contributed by the Board President. No amounts have been reflected in the accompanying financial statements for this in-kind contribution.

H. INCOME TAXES

The Organization is exempt from Federal income taxes under Section 501 (c) (3) of the Internal Revenue Code of 1986, as amended. The Organization is exempt from income and capital stock taxes from the Commonwealth of Pennsylvania under the Commonwealth Act of May 5, 1933, known as the Non-Profit Corporation Law.

I. RELATED PARTY TRANSACTIONS

The Organization loan portfolio includes twenty three notes payable to members of the Board of Directors, members of their immediate families and three employees. Further, it includes six additional notes from organizations over which individual board member have significant influence. The notes range in size from \$2,000 to \$52,000 and carry interest rates that range from 0% to 5%. The notes carry a weighted average interest rate of 4.14% and total \$365,900. The terms of the notes are all within parameters described in the Organization loan prospectus.

SOSTENICA, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

I. RELATED PARTY TRANSACTIONS, continued

The Board President serves as one of four paid staff members with an annual salary of \$12,000. In his salaried capacity, he administers the loan portfolio and investor relations and oversees the sustainable agriculture development program element of the Organization.