Small Steps Nurturing Center

Financial Statements
and Independent Auditors' Report
for the years ended December 31, 2012 and 2011

Small Steps Nurturing Center

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Blazek & Vetterling
CERTIFIED PUBLIC ACCOUNTANTS

Independent Auditors' Report

To the Board of Directors of
Small Steps Nurturing Center:

We have audited the accompanying financial statements of Small Steps Nurturing Center, which comprise the statements of financial position as of December 31, 2012 and 2011 and the related statements of activities, of functional expenses, and of 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 our audits 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 Small Steps Nurturing Center as of December 31, 2012 and 2011 and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Blazek & Vetterling

October 28, 2013

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Small Steps Nurturing Center

Statements of Financial Position as of December 31, 2012 and 2011

	2012	2011
ASSETS		
Cash	$ 152,577	$ 420,381
Prepaid expenses and other assets	25,412	21,299
Pledges receivable *(Note 2)*	843,905	551,784
Cash designated or restricted for long-term purposes *(Note 3)*	864,335	1,174,533
Investments *(Note 4)*	520,898	466,996
Property, net *(Note 5)*	3,292,972	2,178,801
TOTAL ASSETS	$ 5,700,099	$ 4,813,794
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable	$ 23,351	$ 33,592
Construction payable	116,700	
Total liabilities	140,051	33,592
Net assets:		
Unrestricted:		
Operating	2,199,462	2,455,199
Board-designated reserve funds	406,184	379,115
Total unrestricted net assets	2,605,646	2,834,314
Temporarily restricted *(Notes 6 and 7)*	2,954,402	1,945,888
Total net assets	5,560,048	4,780,202
TOTAL LIABILITIES AND NET ASSETS	$ 5,700,099	$ 4,813,794

See accompanying notes to financial statements.

Small Steps Nurturing Center

Statement of Activities for the year ended December 31, 2012

	UNRESTRICTED	TEMPORARILY RESTRICTED	TOTAL
REVENUE:			
Contributions	$ 492,575	$ 1,192,951	$ 1,685,526
Golf tournament	779,750		779,750
Sporting clay tournament	471,053		471,053
Wine Classic event	458,374		458,374
Luncheon event	190,467		190,467
Cost of direct donor benefits	(394,219)		(394,219)
Investment return *(Note 4)*	32,636	27,104	59,740
Total revenue	2,030,636	1,220,055	3,250,691
Net assets released from restrictions:			
Program expenditures	206,541	(206,541)	
Expiration of time restrictions	5,000	(5,000)	
Total	2,242,177	1,008,514	3,250,691
EXPENSES:			
Program services	2,027,290		2,027,290
Management and general	153,645		153,645
Fundraising	289,910		289,910
Total expenses	2,470,845		2,470,845
CHANGES IN NET ASSETS	(228,668)	1,008,514	779,846
Net assets, beginning of year	2,834,314	1,945,888	4,780,202
Net assets, end of year	$ 2,605,646	$ 2,954,402	$ 5,560,048

See accompanying notes to financial statements.

Small Steps Nurturing Center

Statement of Activities for the year ended December 31, 2011

	UNRESTRICTED	TEMPORARILY RESTRICTED	TOTAL
REVENUE:			
Contributions	$ 389,783	$ 1,421,369	$ 1,811,152
Golf tournament	778,150		778,150
Sporting clay tournament	424,130		424,130
Wine Classic event	368,458		368,458
Luncheon event	313,446		313,446
Cost of direct donor benefits	(357,109)		(357,109)
Investment return *(Note 4)*	3,068	2,550	5,618
Total revenue	1,919,926	1,423,919	3,343,845
Net assets released from restrictions:			
Program expenditures	212,136	(212,136)	
Expiration of time restrictions	5,000	(5,000)	
Total	2,137,062	1,206,783	3,343,845
EXPENSES:			
Program services	1,798,723		1,798,723
Management and general	94,944		94,944
Fundraising	288,934		288,934
Total expenses	2,182,601		2,182,601
CHANGES IN NET ASSETS	(45,539)	1,206,783	1,161,244
Net assets, beginning of year	2,879,853	739,105	3,618,958
Net assets, end of year	$ 2,834,314	$ 1,945,888	$ 4,780,202

See accompanying notes to financial statements.

Small Steps Nurturing Center

Statement of Functional Expenses for the year ended December 31, 2012

	PROGRAM SERVICES	MANAGEMENT AND GENERAL	FUNDRAISING	TOTAL
Salaries	$ 1,341,978	$ 77,539	$ 156,770	$ 1,576,287
Employee benefits	116,449	5,404	10,399	132,252
Depreciation	120,566	1,841	2,761	125,168
Employer payroll taxes	100,387	5,577	11,536	117,500
Professional services	30,653	45,688	1,290	77,631
Repairs and maintenance	63,061	1,356	2,149	66,566
Utilities	48,820	3,186	4,167	56,173
Insurance	44,484	2,970	3,953	51,407
Supplies	38,178	1,324	8,811	48,313
Food	47,518			47,518
Printing, publications and postage	7,998	614	32,348	40,960
Equipment rental	254		29,798	30,052
Extended day program	20,000			20,000
Transportation	17,696	1,090	301	19,087
Bank and credit card fees		618	16,794	17,412
Continuing education	14,694		245	14,939
Software and website	1,686		5,553	7,239
Clothing and toys	6,456			6,456
Other	6,412	6,438	3,035	15,885
Total expenses	$ 2,027,290	$ 153,645	$ 289,910	2,470,845
Cost of direct donor benefits				394,219
Total				$ 2,865,064

See accompanying notes to financial statements.

Small Steps Nurturing Center

Statement of Functional Expenses for the year ended December 31, 2011

	PROGRAM SERVICES	MANAGEMENT AND GENERAL	FUNDRAISING	TOTAL
Salaries	$ 1,189,959	$ 53,018	$ 121,371	$ 1,364,348
Employee benefits	116,453	2,450	11,401	130,304
Depreciation	109,613	1,815	2,722	114,150
Employer payroll taxes	89,281	3,615	8,735	101,631
Professional services	32,576	22,205	18,765	73,546
Repairs and maintenance	36,520	1,503	1,340	39,363
Utilities	45,232	3,420	5,192	53,844
Insurance	33,015	2,966	2,729	38,710
Supplies	24,568	450	8,023	33,041
Food	41,737			41,737
Printing, publications and postage	1,291	942	44,163	46,396
Equipment rental	3,095		25,633	28,728
Extended day program	20,000			20,000
Transportation	15,466			15,466
Bank and credit card fees		1,005	15,156	16,161
Continuing education	16,490		342	16,832
Software and website	2,197		10,879	13,076
Clothing and toys	9,000			9,000
Other	12,230	1,555	12,483	26,268
Total expenses	$ 1,798,723	$ 94,944	$ 288,934	2,182,601
Cost of direct donor benefits				357,109
Total				$ 2,539,710

See accompanying notes to financial statements.

Small Steps Nurturing Center

Statements of Cash Flows for the years ended December 31, 2012 and 2011

	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	$ 779,846	$ 1,161,244
Adjustments to reconcile changes in net assets to net cash provided (used) by operating activities:		
Contributions restricted for long-term purposes	(932,004)	(938,600)
Depreciation	125,168	114,149
Net realized and unrealized (gain) loss on investments	(38,496)	1,924
Changes in operating assets and liabilities:		
Pledges receivable (operating)	(65,169)	(20,000)
Prepaid expenses and other assets	(4,113)	(3,980)
Accounts payable	(10,241)	(17,114)
Net cash provided (used) by operating activities	(145,009)	297,623
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments	(15,406)	(468,920)
Purchases of property	(1,122,639)	(104,828)
Net change in cash held for long-term purposes	310,198	(74,204)
Net cash used by investing activities	(827,847)	(647,952)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from contributions restricted for long-term purposes	705,052	406,816
NET CHANGE IN CASH	(267,804)	56,487
Cash, beginning of year	420,381	363,894
Cash, end of year	$ 152,577	$ 420,381

See accompanying notes to financial statements.

NOTE 1 – ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

Organization – Small Steps Nurturing Center (Small Steps) is a Texas nonprofit corporation located in Houston, Texas, providing a comprehensive early childhood development program aimed at giving at-risk, pre-school-age children and their parents the opportunity to grow socially, emotionally, physically, intellectually, and spiritually. Small Steps serves approximately 120 students at its Jensen and DePelchin campuses. Small Steps relies on charitable contributions for support of its program and does not solicit or accept governmental funding.

Federal income tax status – Small Steps is exempt from federal income tax under §501(c)(3) of the Internal Revenue Code and is classified as a public charity under §509(a)(1). Small Steps files annual federal information returns that are subject to routine examination; however, there are no examinations for any tax periods currently in progress. Small Steps believes it is no longer subject to examinations of returns for tax years ended before December 31, 2009.

Cash concentration – Bank deposits exceed the federally insured limit per depositor per institution.

Pledges receivable that are expected to be collected within one year are reported at net realizable value. Pledges receivable that are expected to be collected in future years are discounted, if material, to estimate the present value of future cash flows.

Investments are reported at fair value. Investment return is reported in the statement of activities as an increase in unrestricted net assets unless the use of the income is limited by donor-imposed restrictions. Investment return whose use is restricted by the donor is reported as an increase in temporarily restricted net assets until expended in accordance with donor-imposed restrictions.

Property with an original value of at least $1,000 is reported at cost if purchased and at fair value at the date of gift if donated. Property is depreciated using the straight-line method over estimated useful lives of three to seven years for furniture, equipment and supplies, and 10 to 30 years for buildings and improvements.

Net asset classification – Contributions and the related net assets are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Unrestricted net assets* include those net assets whose use is not restricted by donor-imposed stipulations, even though their use may be limited in other respects, such as by contract or board designation.
- *Temporarily restricted net assets* include contributions restricted by the donor for specific purposes or time periods. When a purpose restriction is accomplished or a time restriction ends, temporarily restricted net assets are released to unrestricted net assets.

Contributions are recognized as revenue at fair value when an unconditional commitment is received from the donor. Contributions received with donor stipulations that limit their use are classified as restricted support. Conditional contributions are recognized in the same manner when the conditions are substantially met.

In-kind contributions – Donated materials, use of facilities and services are recognized at fair value as contributions when an unconditional commitment is received from the donor. The related expense is recognized as the item is used. Contributions of services are recognized when services received (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts of reported revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

NOTE 2 – PLEDGES RECEIVABLE

Pledges receivable consist of the following:

	2012	2011
Capital campaign	$ 758,736	$ 531,784
Operating	85,169	20,000
Pledges receivable, net	$ 843,905	$ 551,784

Pledges receivable at December 31, 2012 are expected to be collected as follows:

Due within one year	$ 515,255
Due in one to five years	328,650
Total pledges receivable	$ 843,905

NOTE 3 – CASH DESIGNATED OR RESTRICTED FOR LONG-TERM PURPOSES

Cash whose use has been limited or restricted for long-term purposes consist of the following:

	2012	2011
Donor-restricted for capital campaign	$ 564,452	$ 871,979
Board-designated for future operations	151,601	151,469
Donor-restricted for higher education	148,282	151,085
Total	$ 864,335	$ 1,174,533

NOTE 4 – INVESTMENTS AND FAIR VALUE MEASUREMENTS

Generally accepted accounting principles require that certain assets and liabilities be reported at fair value and establish a hierarchy that prioritizes inputs used to measure 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. The three levels of the fair value hierarchy are as follows:

- *Level 1* – Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date.
- *Level 2* – Inputs are other than quoted prices included in Level 1, which are either directly observable or can be derived from or corroborated by observable market data at the reporting date.

- *Level 3* – Inputs are not observable and are based on the reporting entity's assumptions about the inputs market participants would use in pricing the asset or liability.

Assets measured at fair value at December 31, 2012 are as follows:

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Open-ended mutual funds:				
Balanced index	$ 266,315			$ 266,315
Moderate growth	254,583			254,583
Total assets measured at fair value	$ 520,898	$ 0	$ 0	$ 520,898

Assets measured at fair value at December 31, 2011 are as follows:

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Open-ended mutual funds:				
Balanced index	$ 239,211			$ 239,211
Moderate growth	227,785			227,785
Total assets measured at fair value	$ 466,996	$ 0	$ 0	$ 466,996

Open-ended mutual funds are valued at the closing price reported on the active market in which the individual securities are traded. This valuation method may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while Small Steps believes its valuation method is appropriate, the use of different methods or assumptions could result in a different fair value measurement at the reporting date.

Investments are exposed to various risks such as interest rate, market, and credit risks. Because of these risks, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position and statement of activities.

Investment return includes earnings on cash and consists of the following:

	2012	2011
Interest and dividends	$ 21,244	$ 7,542
Net realized and unrealized gain (loss)	38,496	(1,924)
Total investment return	$ 59,740	$ 5,618

NOTE 5 – PROPERTY

Property consists of the following:

	2012	2011
Land	$ 367,748	$ 307,978
Buildings and improvements	2,404,664	2,398,646
Office furniture and equipment	81,663	82,562
Classroom equipment and supplies	171,057	149,553
Vans	168,748	139,537
Construction in progress	1,174,121	85,837
Property, at cost	4,368,001	3,164,113
Accumulated depreciation	(1,075,029)	(985,312)
Property, net	$ 3,292,972	$ 2,178,801

NOTE 6 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes:

	2012	2011
Capital improvements	$ 2,466,251	$ 1,489,600
Term endowment to support school operations	266,315	239,211
Higher education	148,282	151,085
For use in future years	65,000	20,000
Other	8,554	45,992
Total temporarily restricted net assets	$ 2,954,402	$ 1,945,888

NOTE 7 – ENDOWMENT FUND

Small Steps maintains a term endowment fund that is restricted by the donor until 2020 to provide consistent, long-term funding for educational operations by annually distributing 4% to 5% of the fund's average quarterly value. This fund has no permanently restricted component, but was established to function similar to an endowment. At the end of the term of the endowment, any remaining unspent funds may be used at the discretion of the Small Steps' Board of Directors.

Changes in net assets of the term endowment fund are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
Net assets, December 31, 2010	$ 0	$ 0	$ 0	$ 0
Contributions		250,000		250,000
Investment return:				
Interest and dividends		951		951
Net realized and unrealized gain		760		760
Net investment return		1,711		1,711
Distributions		(12,500)		(12,500)
Net assets, December 31, 2011	0	239,211	0	239,211
Investment return:				
Interest and dividends		5,279		5,279
Net realized and unrealized gain		21,825		21,825
Net investment return		27,104		27,104
Net assets, December 31, 2012	$ 0	$ 266,315	$ 0	$ 266,315

The Board of Directors of Small Steps has interpreted the Texas Uniform Prudent Management of Institutional Funds Act (TUPMIFA) as requiring the classification of the entire market value of the term endowment fund, as of the date of the financial statements, as temporarily restricted net assets. Annually, in accordance with the donor's wish as expressed in the gift instrument, Small Steps appropriates for expenditure an amount of money determined by a formula based on average net assets over a period of twelve quarters. In determining the specific amount of money to be appropriated for expenditure, the Small Steps Board of Directors considers the following factors:

- The duration and preservation of the funds
- The purposes of the organization and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the organization
- The investment policies of the organization

Investment Policy

Small Steps has adopted an investment policy for term endowment investments and other invested funds of Small Steps. The general purpose of the policy is to preserve and enhance the real value of the principal and to provide Small Steps with a dependable source of revenue to support its facilities and programs. More specifically, with respect to the donor-restricted term endowment fund, the purpose of the policy is to provide a relatively stable annual income whose real value will remain consistent over the next ten years.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, Small Steps relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). Small Steps targets a diversified asset allocation that varies based on the objectives of the specific fund. Asset allocation targets are determined by the Board of Directors based on the recommendations of the Finance Committee of the Board of Directors.

NOTE 8 – CONCENTRATION OF CONTRIBUTIONS

During the year ended December 31, 2012, contributions from two foundations comprised approximately $600,000 or 19% of total contributions. During the year ended December 31, 2011, contributions from five donors, two of which were foundations, comprised approximately $625,000 or 19% of total contributions.

NOTE 9 – IN-KIND CONTRIBUTIONS

The following in-kind contributions are included in revenue as unrestricted contributions and capitalized as fixed assets or expensed and reported in their respective functional categories:

	2012	2011
Building fire system and design services	$ 44,647	
Program supplies and food	13,300	$ 16,300
Printing and publications	4,000	4,000
Other	4,000	4,000
Total in-kind contributions	$ 65,947	$ 24,300

NOTE 10 – COMMITMENTS

Small Steps entered into a construction management agreement to coordinate and facilitate the construction of an addition to the school. At December 31, 2012, the unpaid commitment on this contract was approximately $296,000.

NOTE 11 – RELATED PARTY TRANSACTIONS

During 2012, Small Steps purchased vans from a related party for approximately $54,000.

NOTE 12 – SUBSEQUENT EVENTS

Management has evaluated subsequent events through October 28, 2013, which is the date that the financial statements were available for issuance. As a result of this evaluation, no events were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.