

SOLE4SOULS, INC. AND SUPPORTING ORGANIZATION

CONSOLIDATED FINANCIAL STATEMENTS

AND

INDEPENDENT AUDITOR'S REPORT

JUNE 30, 2013 AND 2012

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Soles4Souls, Inc.
Nashville, Tennessee

REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

We have audited the accompanying consolidated financial statements of Soles4Souls, Inc. and supporting organization, which comprise the consolidated statements of financial position as of June 30, 2013 and 2012, and the related consolidated statements of activities, cash flows and functional expenses, for the years then ended, and the related notes to the financial statements.

MANAGEMENT'S RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Soles4Souls, Inc. and supporting organization as of June 30, 2013 and 2012, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Ygraff CPAs PLLC

Nashville, Tennessee
March 7, 2014

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

JUNE 30, 2013 AND 2012

	<u>2013</u>	<u>2012</u>
<u>ASSETS</u>		
Cash	\$ 69,570	\$ 9,827
Accounts receivable	19,965	17,132
Prepaid expenses and other assets	21,043	16,832
Inventories	14,042,222	9,667,601
Investments	800,224	5,347,740
Property and equipment, net	3,364,491	3,493,820
Mortgage loan costs, net	29,345	32,938
TOTAL ASSETS	<u>\$ 18,346,860</u>	<u>\$ 18,585,890</u>
<u>LIABILITIES AND NET ASSETS</u>		
<u>LIABILITIES</u>		
Accounts payable and accrued expenses	\$ 666,855	\$ 1,302,981
Deposits	246,081	218,292
Investment margin loan	-	1,980,000
Obligation under line of credit	-	466,011
Notes payable	2,386,778	2,492,847
TOTAL LIABILITIES	<u>3,299,714</u>	<u>6,460,131</u>
<u>NET ASSETS</u>		
Unrestricted net assets		
Invested in property and equipment, less related debt	977,713	1,000,973
Unrestricted donated inventory	10,701,975	4,785,566
Undesignated	267,936	1,701,050
Total unrestricted net assets	11,947,624	7,487,589
Temporarily restricted net assets	3,099,522	4,638,170
TOTAL NET ASSETS	<u>15,047,146</u>	<u>12,125,759</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 18,346,860</u>	<u>\$ 18,585,890</u>

See accompanying notes to consolidated financial statements.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

CONSOLIDATED STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2013

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
SUPPORT AND REVENUE			
In-kind contributions			
Shoes:			
Corporate shoe donations	\$ 16,860,883	\$ 3,099,522	\$ 19,960,405
Retail store shoe drives	10,782,378	-	10,782,378
Community shoe drives	5,795,895	-	5,795,895
Clothing donations	7,347,631	-	7,347,631
Other relief item donations	<u>667,631</u>	<u>-</u>	<u>667,631</u>
Total in-kind contributions	41,454,418	3,099,522	44,553,940
Micro-enterprise program fees	2,018,506	-	2,018,506
Contributions	1,329,012	-	1,329,012
International volunteer travel fees	412,805	-	412,805
Investment income	230,204	-	230,204
Other income	31,692	-	31,692
Net assets released from restriction	<u>4,638,170</u>	<u>(4,638,170)</u>	<u>-</u>
TOTAL SUPPORT AND REVENUE	<u>50,114,807</u>	<u>(1,538,648)</u>	<u>48,576,159</u>
EXPENSES			
Program services	43,675,235	-	43,675,235
Management and general	1,065,728	-	1,065,728
Fundraising	<u>913,809</u>	<u>-</u>	<u>913,809</u>
TOTAL EXPENSES	<u>45,654,772</u>	<u>-</u>	<u>45,654,772</u>
CHANGE IN NET ASSETS	4,460,035	(1,538,648)	2,921,387
NET ASSETS, BEGINNING OF YEAR	<u>7,487,589</u>	<u>4,638,170</u>	<u>12,125,759</u>
NET ASSETS, END OF YEAR	<u>\$ 11,947,624</u>	<u>\$ 3,099,522</u>	<u>\$ 15,047,146</u>

See accompanying notes to consolidated financial statements.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

CONSOLIDATED STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2012

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
SUPPORT AND REVENUE			
In-kind contributions			
Shoes:			
Corporate shoe donations	\$ 14,555,968	\$ 4,638,170	\$ 19,194,138
Retail store shoe drives	5,579,545	-	5,579,545
Community shoe drives	6,897,422	-	6,897,422
Clothing donations	13,649,562	-	13,649,562
Other relief item donations	<u>1,603,963</u>	<u>-</u>	<u>1,603,963</u>
 Total in-kind contributions	 42,286,460	 4,638,170	 46,924,630
 Micro-enterprise program fees	 2,492,749	 -	 2,492,749
Contributions	1,528,066	-	1,528,066
International volunteer travel fees	586,861	-	586,861
Investment loss	(181,318)	-	(181,318)
Other income	18,200	-	18,200
Net assets released from restriction	<u>1,478,908</u>	<u>(1,478,908)</u>	<u>-</u>
 TOTAL SUPPORT AND REVENUE	 <u>48,209,926</u>	 <u>3,159,262</u>	 <u>51,369,188</u>
 EXPENSES			
Program services	50,165,415	-	50,165,415
Management and general	1,510,051	-	1,510,051
Fundraising	<u>1,069,048</u>	<u>-</u>	<u>1,069,048</u>
 TOTAL EXPENSES	 <u>52,744,514</u>	 <u>-</u>	 <u>52,744,514</u>
 CHANGE IN NET ASSETS	 (4,534,588)	 3,159,262	 (1,375,326)
 NET ASSETS, BEGINNING OF YEAR	 <u>12,022,177</u>	 <u>1,478,908</u>	 <u>13,501,085</u>
 NET ASSETS, END OF YEAR	 <u>\$ 7,487,589</u>	 <u>\$ 4,638,170</u>	 <u>\$ 12,125,759</u>

See accompanying notes to consolidated financial statements.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED JUNE 30, 2013 AND 2012

	<u>2013</u>	<u>2012</u>
OPERATING ACTIVITIES		
Change in net assets	\$ 2,921,387	\$ (1,375,326)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Realized and unrealized losses (gains) on investments, net	(206,335)	271,825
Depreciation	178,176	197,994
Gain on sale of property and equipment	-	(5,846)
Amortization on mortgage loan costs	3,593	2,994
(Increase) decrease in:		
Accounts receivable	(2,833)	(8,535)
Prepaid expenses and other assets	(4,211)	77,948
Inventories	(4,374,621)	(38,161)
Increase (decrease) in:		
Accounts payable and accrued expenses	(636,126)	716,075
Deposits	27,789	(135,960)
Inventory promised for distribution	-	(1,579,200)
TOTAL ADJUSTMENTS	<u>(5,014,568)</u>	<u>(500,866)</u>
NET CASH USED IN OPERATING ACTIVITIES	<u>(2,093,181)</u>	<u>(1,876,192)</u>
INVESTING ACTIVITIES		
Purchase of investments	(1,169,392)	(2,318,866)
Proceeds from sale of investments	5,923,243	2,607,227
Purchase of property and equipment	(48,847)	(77,626)
Proceeds from sale of property and equipment	-	30,000
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>4,705,004</u>	<u>240,735</u>
FINANCING ACTIVITIES		
Repayments of notes payable	(106,069)	(93,572)
Net borrowings (payments) on investment margin loan	(1,980,000)	1,230,000
Net borrowings (payments) on line of credit	(466,011)	421,814
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	<u>(2,552,080)</u>	<u>1,558,242</u>
NET (DECREASE) INCREASE IN CASH	59,743	(77,215)
CASH - BEGINNING OF YEAR	<u>9,827</u>	<u>87,042</u>
CASH - ENDING OF YEAR	<u>\$ 69,570</u>	<u>\$ 9,827</u>
NONCASH INVESTING AND FINANCING ACTIVITIES		
Note payable obligation incurred in refinancing	<u>\$ -</u>	<u>\$ 2,527,000</u>
Increase in line of credit incurred in refinancing	<u>\$ -</u>	<u>\$ 50,197</u>
Note payable paid-off with refinanced loan	<u>\$ -</u>	<u>\$ (2,442,187)</u>
Mortgage loan costs incurred on refinanced loan	<u>\$ -</u>	<u>\$ (35,932)</u>
Line of credit paid-off with refinanced loan	<u>\$ -</u>	<u>\$ (99,078)</u>
SUPPLEMENTAL CASH FLOW DISCLOSURE		
Cash paid during the year for interest	<u>\$ 140,412</u>	<u>\$ 159,950</u>

See accompanying notes to consolidated financial statements.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

FOR THE YEAR ENDED JUNE 30, 2013

	<u>Program Services</u>	<u>Management and General</u>	<u>Fundraising</u>	<u>Total</u>
Salaries	\$ 1,456,567	\$ 483,324	\$ 221,398	\$ 2,161,289
Employee benefits and payroll taxes	<u>221,244</u>	<u>64,847</u>	<u>35,609</u>	<u>321,700</u>
 Total personnel costs	 <u>1,677,811</u>	 <u>548,171</u>	 <u>257,007</u>	 <u>2,482,989</u>
 In-kind distributions:				
Shoes	13,993,630	-	-	13,993,630
Clothing	1,081,979	-	-	1,081,979
Other relief items	581,470	-	-	581,470
Items to the micro-enterprise programs	<u>24,522,240</u>	<u>-</u>	<u>-</u>	<u>24,522,240</u>
 Total in-kind distributions	 40,179,319	 -	 -	 40,179,319
 Other distribution expenses	 299,761	 -	 -	 299,761
Advertising and promotion	201,838	-	23,269	225,107
Auto expenses	25,193	-	-	25,193
Bank fees	-	90,359	-	90,359
Depreciation and amortization	136,327	27,265	18,177	181,769
Direct mail	-	-	266,712	266,712
Events	18,301	-	43,732	62,033
Insurance	102,400	20,480	13,653	136,533
Interest	92,769	35,274	12,369	140,412
Miscellaneous	7,554	43,857	6,905	58,316
Supplies and equipment	38,778	2,111	1,325	42,214
Postage, shipping and delivery	141,464	1,664	23,300	166,428
Professional fees	114,643	265,111	221,376	601,130
Rent	31,177	-	-	31,177
Repairs and maintenance	24,174	2,138	1,552	27,864
Telephone and utilities	72,985	14,597	9,731	97,313
Travel	<u>510,741</u>	<u>14,701</u>	<u>14,701</u>	<u>540,143</u>
 TOTAL EXPENSES	 <u>\$ 43,675,235</u>	 <u>\$ 1,065,728</u>	 <u>\$ 913,809</u>	 <u>\$ 45,654,772</u>

See accompanying notes to consolidated financial statements.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

FOR THE YEAR ENDED JUNE 30, 2012

	Program Services	Management and General	Fundraising	Total
Salaries	\$ 1,845,932	\$ 733,269	\$ 296,228	\$ 2,875,429
Employee benefits and payroll taxes	259,482	103,041	41,650	404,173
Total personnel costs	2,105,414	836,310	337,878	3,279,602
In-kind distributions:				
Shoes	13,521,446	-	-	13,521,446
Clothing	2,806,496	-	-	2,806,496
Other relief items	1,059,485	-	-	1,059,485
Items to the micro-enterprise programs	27,919,506	-	-	27,919,506
Total in-kind distributions	45,306,933	-	-	45,306,933
Other distribution expenses	498,059	-	-	498,059
Advertising and promotion	267,677	695	44,254	312,626
Auto expenses	39,598	3,274	3,274	46,146
Bank fees	-	65,673	-	65,673
Depreciation and amortization	151,489	29,699	19,800	200,988
Direct mail	-	-	336,172	336,172
Events	118,913	-	150,697	269,610
Insurance	69,731	13,946	9,297	92,974
Interest	98,675	48,118	13,157	159,950
Miscellaneous	28,651	29,137	507	58,295
Supplies and equipment	53,091	3,146	2,097	58,334
Postage, shipping and delivery	138,658	1,631	22,838	163,127
Professional fees	458,150	436,262	94,152	988,564
Rent	47,191	-	-	47,191
Repairs and maintenance	31,972	2,788	2,113	36,873
Telephone and utilities	98,399	19,680	13,120	131,199
Travel	652,814	19,692	19,692	692,198
TOTAL EXPENSES	\$ 50,165,415	\$ 1,510,051	\$ 1,069,048	\$ 52,744,514

See accompanying notes to consolidated financial statements.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

JUNE 30, 2013 AND 2012

NOTE 1 - ORGANIZATION AND NATURE OF ACTIVITIES

Soles4Souls, Inc. ("Soles4Souls") was founded in 2006 as an Alabama not-for-profit corporation. Soles4Souls is a global not-for-profit institution dedicated to fighting the devastating impact and perpetuation of poverty. The organization advances its anti-poverty mission by collecting new and used shoes and clothes from individuals, schools, faith-based institutions, civic organizations and corporate partners, then distributing those shoes and clothes both via direct donations to people in need and by provisioning qualified micro-enterprise programs designed to create jobs in poor and disadvantaged communities.

In February 2009, Changing the World Foundation, Inc. ("CTWF") was formed as a supporting organization as a Tennessee not-for-profit corporation to support and further the charitable purposes of Soles4Souls. Soles4Souls has an economic interest in CTWF combined with control through a majority voting interest of the Board of CTWF.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation and Basis of Presentation

The consolidated financial statements include the accounts of Soles4Souls, Inc. and Changing the World Foundation, Inc. (collectively the "Organization"). The accompanying consolidated financial statements are presented on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America ("GAAP"). All significant intercompany accounts and transactions have been eliminated in consolidation.

Resources are classified as unrestricted, temporarily restricted or permanently restricted net assets, based on the existence or absence of donor-imposed restrictions, as follows:

- *Unrestricted net assets* are free of donor-imposed restrictions. All revenues, gains and losses that are not temporarily or permanently restricted by donors are included in this classification. All expenditures are reported in the unrestricted class of net assets, since the use of restricted contributions in accordance with the donors' stipulations results in the release of the restriction.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Consolidation and Basis of Presentation (Continued)

- *Temporarily restricted net assets* are limited as to use by donor-imposed restrictions that expire with the passage of time or that can be satisfied by use for the specific purpose. Temporarily restricted net assets in 2013 and 2012 consisted entirely of donated inventory restricted for distribution outside the United States of America.
- *Permanently restricted net assets* are amounts required by donors to be held in perpetuity, including gifts requiring that the principal be invested and the income or specific portions thereof be used for operations. The Organization had no permanently restricted net assets as of June 30, 2013 and 2012.

Contributions and Support

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are restricted by the donor for future periods or for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset classes. When a restriction is fulfilled (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted and reported in the Consolidated Statement of Activities as net assets released from restrictions. However, if a restriction is fulfilled in the same time period in which the contribution is received, the support is reported as unrestricted.

The Organization reports any gifts of equipment or materials as unrestricted support unless explicit donor restrictions specify how the assets must be used. Gifts of long-lived assets with explicit restrictions as to how the assets are to be used or funds restricted for the acquisition of long-lived assets are reported as restricted support. Expirations of donor restrictions are recognized when the donated or acquired long-lived assets are placed in service.

Cash

Cash consists of checking account balances.

Accounts Receivable

Accounts receivable are from micro-enterprise distributors related to cost of shipping and handling. The Organization does not charge interest on past due accounts. Accounts receivable are deemed to be fully collectible by management and no allowance for bad debts is considered necessary at June 30, 2013 and 2012.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Inventories

Inventories consist primarily of donated new and used footwear, purchased footwear, clothing, DVDs, books, and other relief items. Items are assigned an estimated fair value by management at the time of donation. Management assigns an estimated fair value based on previous experience in the shoe industry and the donor's product, which approximates a range between cost and wholesale. Most donations of new product consist of mixed styles and types, for which management assigns an average fair value as follows: \$30 for men's shoes, \$27 for women's shoes and \$16 for children's shoes. Used shoes obtained through retail stores and community shoe drives are valued at \$4 per pair, which is measured in poundage assuming an average weight of 1.25 lbs. per pair.

Donated clothing, DVDs, books and other relief supplies are recorded at their estimated fair value as provided by the donor or, in the absence of donors' valuations, based on the Organization's estimate of wholesale values considering their condition and utility for use, at the time the goods are received from the donor. Beginning in 2013, the Organization valued donated new clothing at an average fair value of \$12 per item. Prior to 2013, the fair value was determined on the specific clothing item received.

Purchased inventory is valued at the lower of cost or market, determined by the first-in first-out (FIFO) method. Provision is made to reduce any excess, obsolete or slow moving inventory to net realizable value.

Investments

Investments consist of cash, tax managed fund, mutual funds, equities, equity funds and fixed income funds. Cash is carried at cash value plus any accrued interest. Mutual funds, equities, equity funds and fixed income funds are carried at their quoted market value on the last business day of the reporting period. Changes in unrealized gains and losses are recognized currently in the Consolidated Statement of Activities.

Property and Equipment and Depreciation

Property and equipment are reported at cost, net of accumulated depreciation, and include improvements that significantly add to productive capacity or extend useful lives. It is the Organization's policy to capitalize expenditures for assets with a cost of \$1,000 or greater and an estimated useful life of at least one year. Costs of maintenance and repairs are charged to expense. When depreciable assets are disposed of, the cost and related accumulated depreciation are removed from the accounts, and any gain (except trade-ins) or loss is recognized. Gains on trade-ins are applied to reduce the cost of the new acquisition.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property and Equipment and Depreciation (Continued)

Depreciation is computed under the straight-line method over the estimated useful lives of depreciable assets, as follows:

Building and improvements	10 - 30 years
Vehicles	5 years
Equipment	3 - 5 years
Furniture and fixtures	7 years

Mortgage Loan Costs

Mortgage loan costs are capitalized and amortized on a straight-line basis over a period of 10 years, the life of the related loan. Amortization of the loan costs will be \$3,593 for the years 2013 through 2021, respectively and \$601 in 2022.

Fair Value Measurements

The Organization classifies its assets and liabilities measured at fair value based on a hierarchy consisting of: Level 1 (valued using quoted prices from active markets for identical assets), Level 2 (not traded on an active market but for which observable market inputs are readily available), and Level 3 (valued based on significant unobservable inputs).

An asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value on a recurring basis:

Investments - Where quoted prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include highly liquid securities and certain other products, such as mutual funds. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics, or discounted cash flows and are classified within Level 2.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fair Value Measurements (Continued)

No changes in the valuation methodologies have been made since the prior year.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Organization believes its valuation methods are appropriate and consistent with that of other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in different fair value measurements at the reporting date.

Donated Goods and Services

Donated goods, including donated shoes, clothing, DVDs, books and other relief items, are recorded as in-kind gifts in the period received at their estimated fair value, if there is an objective and measurable basis for determining such value.

Donated services are recognized if they create or enhance nonfinancial assets or the donated service requires specialized skills, was performed by a donor who possesses such skills, and would have been purchased by the Organization if not donated. Such services are recognized at fair value as support and expense in the period the services were performed.

A number of unpaid volunteers have made significant contributions of their time to assist the Organization in implementing various programs. The value of contributed time is not reflected in these financial statements since it is not susceptible to objective measurement or valuation.

Micro-enterprise Program Fees / Deposits

Micro-enterprise ("MBE") program handling fees are charged to certain recipient organizations that receive used footwear for redistribution. Such fees are recognized as revenue at the time the product is shipped to the recipient organization. Amounts collected in advance of shipment are classified initially as deposits in the Consolidated Statement of Financial Position and recognized in the period the product is shipped.

Advertising

The Organization uses advertising to promote its programs and raise awareness. All advertising costs are expensed when incurred.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Program and Supporting Services

The following program and supporting services are included in the accompanying consolidated financial statements:

Program Services - facilitates the donation and collection of new and used shoes, new and used clothing and other relief supplies (including diapers, DVD's, books, toys for children, and other relief supplies.) from footwear, clothing and other manufacturers, retailers and individuals. These items are distributed to people in need locally, nationally and internationally through a network of volunteer organizations and in cooperation with other charitable organizations, referred to as distribution partners, who work on the Organization's behalf to distribute these items providing relief to individuals living in poverty or affected by natural disasters. Through this extensive network, the Organization has distributed shoes, clothing, and other relief supplies to people in more than 127 countries.

The Organization operates a micro-enterprise operation in Haiti and contracts with established micro-enterprise distributors to distribute shoes in Central America, South America and Africa. This program is designed to provide impoverished people in developing nations with the resources to start and maintain their own business. In this way, the Organization focuses on long-term development by distributing shoes and clothing that are inappropriate for crisis relief or that need cleaning or conditioning in order to be useful.

Through its Travel4Souls, volunteers from across the United States join the Organization's staff on distribution trips to various countries to experience first-hand providing shoes and clothing to people in desperate situations. Teams visited Haiti, Costa Rica, Honduras, India, Jamaica and Tanzania on 18 trips in 2013 (17 trips in 2012). Shoes and clothing were distributed to children and families in orphanages, schools, villages and tent cities.

Management and General - Includes the functions necessary to ensure an adequate working environment and costs not identifiable with a single program. Applicable costs include those associated with providing coordination and articulation of the Organization's program strategy, business management, general record keeping, budgeting, and related purposes.

Fundraising - Includes costs of activities directed towards appeals for financial support, including special events. Other activities include the cost of solicitations and creation and distribution of fund raising materials.

Allocation of Functional Expenses

Expenses that can be directly attributed to a particular function are charged to that function. Certain costs have been allocated among more than one program or activity based on objectively evaluated financial and non-financial data or reasonable subjective methods determined by management.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income Taxes

Soles4Souls and CTWF qualify as not-for-profit organizations exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. Accordingly, income taxes are not provided for either organization.

Soles4Souls and CTWF each file a U.S. Federal Form 990 for organizations exempt from income tax. Soles4Souls's tax returns for years prior to fiscal year end 2010 are now closed and no longer open to further examination by the Internal Revenue Service. CTWF filed a U.S. Federal Form 990 for the year ended January 31, 2010, and a short-period tax return for the five-month period ended June 30, 2010. Subsequent CTWF tax returns are filed on a June 30 fiscal year end. All CTWF tax returns filed are still open for examination.

Management performs an evaluation of all income tax positions taken or expected to be taken in the course of preparing the Organization's income tax returns to determine whether the income tax positions meet a "more likely than not" standard of being sustained under examination by the applicable taxing authorities. Management has performed its evaluation of all income tax positions taken on all open income tax returns and has determined that there were no positions taken that do not meet the "more likely than not" standard. Accordingly, there are no provisions for income taxes, penalties or interest receivable or payable relating to uncertain income tax positions in the accompanying consolidated financial statements.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent 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.

Events Occurring After Reporting Date

The Organization has evaluated events and transactions that occurred between June 30, 2013 and March 7, 2014, the date the consolidated financial statements were available to be issued, for possible recognition or disclosure in the consolidated financial statements.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 3 - INVENTORIES

Inventories consisted of the following at June 30:

	<u>2013</u>	<u>2012</u>
Donated shoes:		
New shoes	\$ 8,025,158	\$ 4,589,386
Used shoes	1,351,978	787,367
Donated clothing items	3,249,630	2,629,615
Other donated items:		
DVDs	285,480	195,800
Other relief supplies	<u>889,251</u>	<u>1,221,568</u>
Total donated inventory	13,801,497	9,423,736
Purchased shoes	<u>240,725</u>	<u>243,865</u>
	<u>\$ 14,042,222</u>	<u>\$ 9,667,601</u>

The following is a reconciliation of the beginning and ending balances of donated inventory for the year ended June 30:

	<u>Donated Inventory</u>	
	<u>2013</u>	<u>2012</u>
Beginning of year	\$ 9,423,736	\$ 9,201,741
Contributions received	44,553,940	46,924,630
Inventory distributed that was promised	-	(1,579,200)
Donated inventory distributed in programs	<u>(40,176,179)</u>	<u>(45,123,435)</u>
End of year	<u>\$ 13,801,497</u>	<u>\$ 9,423,736</u>

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 4 - INVESTMENTS

Investments consisted of the following at June 30:

	<u>2013</u>	<u>2012</u>
Cash	\$ 2,432	\$ 70,498
Federal government tax managed fund	345,895	-
Mutual funds	8,475	141,895
Equities	158,164	2,620,272
Equity funds	115,529	1,121,400
Fixed income	<u>169,729</u>	<u>1,393,675</u>
	<u>\$ 800,224</u>	<u>\$ 5,347,740</u>

Investment income (loss) consisted of the following for the year ended June 30:

	<u>2013</u>	<u>2012</u>
Interest and dividend income	\$ 40,844	\$ 123,560
Realized gains (losses)	(163,399)	80,689
Unrealized gains (losses)	<u>369,734</u>	<u>(352,514)</u>
	247,179	(148,265)
Less: investment fees	<u>(16,975)</u>	<u>(33,053)</u>
Investment income (loss), net	<u>\$ 230,204</u>	<u>\$ (181,318)</u>

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 5 - FAIR VALUE MEASUREMENTS

Fair values of financial and nonfinancial assets measured on a recurring basis at June 30, 2013 and June 30, 2012 are as follows:

	2013			Total
	Level 1	Level 2	Level 3	
Investments				
Mutual funds	\$ 8,475	\$ -	\$ -	\$ 8,475
Federal government tax managed fund	345,895	-	-	345,895
Equities:				
Nonfinancial	1,913	-	-	1,913
Financial	31,132	-	-	31,132
Utilities	5,674	-	-	5,674
Consumer growth	31,430	-	-	31,430
Consumer staples	12,825	-	-	12,825
Consumer cyclical	19,415	-	-	19,415
Industrial commodities	5,171	-	-	5,171
Capital equipment	11,829	-	-	11,829
Technology	23,055	-	-	23,055
Services	3,063	-	-	3,063
Energy	12,657	-	-	12,657
Total equities	158,164	-	-	158,164
Equity funds:				
Emerging markets portfolio	12,126	-	-	12,126
Global real estate	47,184	-	-	47,184
International portfolio	56,219	-	-	56,219
Total equity funds	115,529	-	-	115,529
Fixed income:				
Intermediate duration portfolio	169,729	-	-	169,729
Total investments valued at fair value	\$ 797,792	\$ -	\$ -	\$ 797,792

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 5 - FAIR VALUE MEASUREMENTS (CONTINUED)

	2012			Total
	Level 1	Level 2	Level 3	
Investments				
Mutual funds	\$ 141,895	\$ -	\$ -	\$ 141,895
Equities:				
Nonfinancial	34,970	-	-	34,970
Financial	377,942	-	-	377,942
Utilities	69,456	-	-	69,456
Consumer growth	608,440	-	-	608,440
Consumer staples	278,900	-	-	278,900
Consumer cyclical	241,306	-	-	241,306
Industrial commodities	16,108	-	-	16,108
Capital equipment	188,596	-	-	188,596
Technology	469,229	-	-	469,229
Services	37,852	-	-	37,852
Energy	297,473	-	-	297,473
Total equities	2,620,272	-	-	2,620,272
Equity funds:				
Emerging markets portfolio	149,296	-	-	149,296
Global real estate	236,512	-	-	236,512
International portfolio	735,592	-	-	735,592
Total equity funds	1,121,400	-	-	1,121,400
Fixed income:				
Intermediate duration portfolio	1,393,675	-	-	1,393,675
Total investments valued at fair value	\$ 5,277,242	\$ -	\$ -	\$ 5,277,242

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 6 - PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at June 30:

	<u>2013</u>	<u>2012</u>
Land	\$ 238,800	\$ 238,800
Building and improvements	3,198,378	3,198,378
Vehicles	205,986	205,986
Equipment	181,779	132,932
Furniture and fixtures	<u>140,147</u>	<u>140,147</u>
	3,965,090	3,916,243
Less: accumulated depreciation	<u>(600,599)</u>	<u>(422,423)</u>
	<u>\$ 3,364,491</u>	<u>\$ 3,493,820</u>

NOTE 7 - INVESTMENT MARGIN LOAN

As of June 30, 2012, the Organization had an outstanding investment margin loan against its brokerage account in the amount of \$1,980,000. This loan was repaid on October 31, 2012. The interest rate on the margin loan was 2.5% per annum on the average monthly outstanding balance.

NOTE 8 - LINES OF CREDIT

In September 2011, the Organization obtained a line of credit in the amount of \$500,000 that was secured by the real estate in the headquarters and warehouse facilities. The interest rate was based on the U.S. Prime rate (3.25% at June 30, 2012). The outstanding balance on the line of credit at June 30, 2012 was \$466,011. The line of credit matured in September 2012 and was paid in full on November 28, 2012.

In October 2013, the Organization obtained a line of credit in the amount of \$300,000 that is secured by a \$300,000 certificate of deposit. The line of credit matures in October 2014 and the rate of interest is 3.4% annually.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 9 - NOTES PAYABLE

Notes payable consisted of the following at June 30:

	<u>2013</u>	<u>2012</u>
Mortgage payable on the headquarters facility located in Nashville, Tennessee and the warehouse facility located in Wadley, Alabama. Monthly payments of principal and interest in the amount of \$16,250 are scheduled through September 2021 when the unpaid principal balance matures. The rate of interest is 4.75% per annum. The loan is secured by a deed of trust on the real estate properties.	\$ 2,364,349	\$ 2,443,261
Note payable to a bank for purchase of a vehicle. Monthly principal and interest payments of \$1,602 were due through January 2014, at which time the loan was paid in full. The rate of interest was 4.88% and the note was collateralized by the vehicle.	10,985	29,140
Note payable for the purchase of a vehicle. This note was refinanced in September 2011 and requires monthly principal and interest payments of \$795 through September 2014. The rate of interest is 3.25% and is collateralized by the vehicle.	<u>11,444</u>	<u>20,446</u>
Total notes payable	<u>\$ 2,386,778</u>	<u>\$ 2,492,847</u>

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 9 - NOTES PAYABLE (CONTINUED)

The mortgage payable for the headquarters facility and the warehouse facility were refinanced and consolidated into a \$2.5 million note in September 2012. The note is collateralized by the real estate of both facilities, and requires a specified cash flow coverage ratio. The Organization was not in compliance with the cash flow coverage ratio as of June 30, 2013. The financial institution has issued a waiver on this loan covenant as of June 30, 2013.

Annual principal maturities of notes payable are as follows:

Year ending June 30,

2014	\$ 104,989
2015	90,952
2016	93,123
2017	97,644
2018	102,385
Thereafter	<u>1,897,685</u>
	<u>\$ 2,386,778</u>

Total interest expense on all indebtedness, including the investment margin loan and the line of credit, for the year ended June 30, 2013 amounted to \$140,412 (\$159,950 in 2012).

NOTE 10 - EMPLOYEE BENEFIT PLAN

The Organization has a Section 401(k) Safe Harbor plan which covers substantially all employees upon completion of three months of service. The plan allows participants to contribute up to the lesser of 84% of compensation or the amount allowable by the Internal Revenue Code. The Organization makes matching contributions based on a percentage of the participant's contributions up to 6%. Participants are immediately 100% vested in their elective contributions, the Organization's contributions and investment earnings on those balances. Total contributions by the Organization amounted to \$76,980 for the year ended June 30, 2013 (\$91,174 in 2012) and are reported in employee benefits expense in the Consolidated Statement of Functional Expenses.

The plan also provides for the Organization to make discretionary non-elective contributions. The Organization has not made any discretionary contributions to the plan as of June 30, 2013 and 2012.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 11 - CONCENTRATIONS AND CREDIT RISK

Financial instruments that potentially subject the Organization to concentrations of credit risk consist of cash and investments.

The Organization maintains cash and certificates of deposit at financial institutions whose accounts are insured by the Federal Deposit Insurance Corporation ("FDIC") up to statutory limits. As of June 30, 2013, the Organization's cash was fully insured.

Investments are subject to market risk, the risk inherent in a fluctuating market. The broker/dealer custodian of the Organization's securities is covered by the Securities Investor Protection Corporation ("SIPC"), which insures investor losses attributable to bankruptcy or fraudulent practices of brokerage firms. Coverage is limited to \$500,000, including up to \$250,000 in cash held for the purpose of securities transactions, and not for the purpose of earning interest.

Donated shoes, clothing and other relief items and micro-enterprise program fees are subject to concentration risk.

During 2013, the Organization:

- Received 38% of its shoe donations from two shoe manufacturers.
- Received 58% of its clothing donations from three manufacturers.
- Received 73% of the other relief supplies from three manufacturers.
- Utilized 3 distribution partners to distribute 99% of its shoe and clothing distributions.
- Received micro-enterprise programs fees from three companies that represent 97% of total micro-enterprise programs fees.

During 2012, the Organization:

- Received 11% of its shoe donations from one shoe manufacturer.
- Received 42% of its clothing donations from two manufacturers.
- Received 49% of the other relief supplies from one manufacturer.
- Utilized 3 distribution partners to distribute 89% of its shoe and clothing distributions.
- Received micro-enterprise programs fees from two companies that represent 79% of total micro-enterprise programs fees.

NOTE 12 - COMMITMENTS, CONTINGENCIES AND SUBSEQUENT EVENTS

The Organization is involved in various legal proceedings, claims and litigation arising in the normal course of business. In the opinion of management, after consultation with legal counsel, the ultimate resolution of such matters will not have a material adverse effect on the Organization's financial position.

SOLES4SOULS, INC. AND SUPPORTING ORGANIZATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2013 AND 2012

NOTE 13 - OTHER MATTERS

In recent years, the Organization has incurred significant cash flow losses. In addition, from March 2012 through September 2012, three members of senior management left the Organization. The Board of Directors hired an experienced not-for-profit leader as President and CEO in September of 2012, who quickly organized a management team with strong credentials in business operations, finance, philanthropy and strategic communications.

The new executive leadership has begun to re-build and re-brand the Organization by:

- Clarifying the mission statement and expanding transparency of operations.
- Evolving and expanding its focus as a social enterprise dedicated to advancing the fight against global poverty.
- Launching a major donor fundraising program under the direction of a new Chief Development Director.
- Focusing on establishing community relationships with local, national and global not-for-profits.
- Enhancing relationships with corporate donors of gifts-in-kind.
- Reducing cash overhead and operating costs by 28%, increasing available cash flow of over \$2 million dollars from fiscal year 2012 to fiscal year 2013.
- Adding additional Board members with industry and fundraising/development expertise in early 2014.

Based on the above, management believes the Organization is well-positioned to reverse the negative financial trends of the past and attain sustainable operations.