MERCY CORPS AND AFFILIATES

Consolidated Financial Statements
and Supplemental Schedules

June 30, 2012 and 2011

(With Independent Auditors' Report Thereon)

MERCY CORPS AND AFFILIATES

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KPMG LLP
Suite 3800
1300 South West Fifth Avenue
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Independent Auditors' Report

The Board of Directors
Mercy Corps and affiliates:

We have audited the accompanying consolidated statements of financial position of Mercy Corps and affiliates (the Organization) as of June 30, 2012 and 2011, and the related consolidated statements of activities, cash flows, and functional expenses for the years then ended. These consolidated financial statements are the responsibility of the Organization's management. 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mercy Corps and affiliates as of June 30, 2012 and 2011, and the changes in their net assets and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information included in Schedules I, II, and III is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audits of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

November 12, 2012

MERCY CORPS AND AFFILIATES

Consolidated Statements of Financial Position

June 30, 2012 and 2011

Assets	**2012**	**2011**
Cash	$ 58,834,662	78,631,833
Financial instruments and derivatives, net	2,892,959	481,828
Grants and accounts receivable	11,292,126	21,128,080
Microfinance loans receivable	64,795,118	55,775,320
Due from unconsolidated affiliates, net	8,113,458	2,503,615
Inventories	7,000,952	5,730,014
Prepaid expenses, deposits, and other assets	7,800,823	5,162,263
Pledges receivable, net	2,519,236	2,408,730
Notes receivable	11,067,171	11,149,243
Investments	3,587,437	1,308,359
Program-related investments	6,488,658	6,382,106
Property and equipment, net	42,879,254	40,039,091
Total assets	$ 227,271,854	230,700,482
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued liabilities	$ 25,262,280	38,273,125
Financial instruments, derivatives, net	606,398	592,964
Deferred revenue	32,910,893	27,828,986
Subsidiary and subordinated debt for microfinancing activities	60,724,121	50,842,534
Long-term debt	25,358,354	26,712,241
Total liabilities	144,862,046	144,249,850
Net assets:		
Unrestricted:		
Undesignated	57,073,689	52,933,308
Board designated	426,338	—
Total unrestricted	57,500,027	52,933,308
Temporarily restricted	24,889,781	33,497,324
Permanently restricted	20,000	20,000
Total net assets	82,409,808	86,450,632
Total liabilities and net assets	$ 227,271,854	230,700,482

See accompanying notes to consolidated financial statements.

MERCY CORPS AND AFFILIATES

Consolidated Statement of Activities

Year ended June 30, 2012

	Unrestricted	Temporarily restricted	Permanently restricted	Totals
Operating support and revenue:				
Public support and revenue:				
Government grants	$ 153,288,901	—	—	153,288,901
Material aid	7,155,726	—	—	7,155,726
Material aid – monetized	11,757,281	—	—	11,757,281
Total public support and revenue	172,201,908	—	—	172,201,908
Private support and revenue:				
Other grants	34,773,243	—	—	34,773,243
Contributions	18,788,096	8,016,270	—	26,804,366
Gifts in kind-services	1,088,682	—	—	1,088,682
Total private support and revenue	54,650,021	8,016,270	—	62,666,291
Other revenue:				
Interest income	31,350,809	—	—	31,350,809
Other revenue	2,193,574	60,218	—	2,253,792
Total other revenue	33,544,383	60,218	—	33,604,601
Net assets released from restriction	16,684,031	(16,684,031)		—
Total operating support and revenue	277,080,343	(8,607,543)	—	268,472,800
Operating expenses:				
Program services:				
Humanitarian assistance – relief	45,029,058	—	—	45,029,058
Humanitarian assistance – recovery	36,873,517	—	—	36,873,517
Livelihood/economic development	83,937,028	—	—	83,937,028
Civil society and education	44,672,365	—	—	44,672,365
Health	22,229,720	—	—	22,229,720
Total program services	232,741,688	—	—	232,741,688
Supporting services:				
General and administrative	30,357,153	—	—	30,357,153
Resource development	11,179,247	—	—	11,179,247
Total supporting services	41,536,400	—	—	41,536,400
Total operating expenses	274,278,088	—	—	274,278,088
Change in net assets from operations	2,802,255	(8,607,543)	—	(5,805,288)
Other nonoperating revenue and expenses, net:				
Foreign currency exchange loss, net	(730,626)	—	—	(730,626)
Realized and unrealized gain on investments, net	522,312	—	—	522,312
Unrealized gain on swap agreements	1,805,980	—	—	1,805,980
Other nonoperating increase in net assets	166,798	—	—	166,798
Total nonoperating revenue and expenses, net	1,764,464	—	—	1,764,464
Change in net assets	4,566,719	(8,607,543)	—	(4,040,824)
Net assets at beginning of year	52,933,308	33,497,324	20,000	86,450,632
Net assets at end of year	$ 57,500,027	24,889,781	20,000	82,409,808

See accompanying notes to consolidated financial statements.

MERCY CORPS AND AFFILIATES

Consolidated Statement of Activities

Year ended June 30, 2011

	Unrestricted	Temporarily restricted	Permanently restricted	Totals
Operating support and revenue:				
Public support and revenue:				
Government grants	$ 186,522,916	—	—	186,522,916
Material aid	12,639,812	—	—	12,639,812
Material aid – monetized	8,672,676	—	—	8,672,676
Total public support and revenue	207,835,404	—	—	207,835,404
Private support and revenue:				
Other grants	13,373,902	18,448,060	—	31,821,962
Private contributions	17,166,667	10,339,767	—	27,506,434
Gifts in kind- services	1,698,575			1,698,575
Contributions for the acquisition of property	—	829,294	—	829,294
Total private support and revenue	32,239,144	29,617,121	—	61,856,265
Other revenue:				
Interest income	25,959,973	—	—	25,959,973
Other revenue	5,791,114	5,500	—	5,796,614
Total other revenue	31,751,087	5,500	—	31,756,587
Net assets released from restriction	31,311,314	(31,311,314)	—	—
Total operating support and revenue	303,136,949	(1,688,693)	—	301,448,256
Operating expenses:				
Program services:				
Humanitarian assistance – relief	65,695,304	—	—	65,695,304
Humanitarian assistance – recovery	42,647,217	—	—	42,647,217
Livelihood/economic development	81,624,330	—	—	81,624,330
Civil society and education	47,973,805	—	—	47,973,805
Health	17,841,230	—	—	17,841,230
Total program services	255,781,886	—	—	255,781,886
Supporting services:				
General and administrative	27,664,414	—	—	27,664,414
Resource development	10,041,183	—	—	10,041,183
Total supporting services	37,705,597	—	—	37,705,597
Total operating expenses	293,487,483	—	—	293,487,483
Change in net assets from operations	9,649,466	(1,688,693)	—	7,960,773
Other nonoperating revenue and expenses, net:				
Foreign currency exchange gain	276,867	—	—	276,867
Realized and unrealized loss on investments	(2,381,680)	—	—	(2,381,680)
Unrealized loss on swap agreements	(829,048)	—	—	(829,048)
Other nonoperating expense	1,605,314	—	—	1,605,314
Total nonoperating revenue and expenses, net	(1,328,547)	—	—	(1,328,547)
Change in net assets	8,320,919	(1,688,693)	—	6,632,226
Net assets at beginning of year	44,612,389	35,186,017	20,000	79,818,406
Net assets at end of year	$ 52,933,308	33,497,324	20,000	86,450,632

See accompanying notes to consolidated financial statements.

MERCY CORPS AND AFFILIATES

Consolidated Statements of Cash Flows

Years ended June 30, 2012 and 2011

		2012	2011
Cash flows from operating activities:			
Change in net assets	$	(4,040,824)	6,632,226
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:			
Depreciation and amortization		4,055,966	3,297,457
Provision for loan losses		329,158	2,761,586
Net realized and unrealized loss on investments		208,314	2,104,813
Unrealized (gain) loss on interest rate and foreign exchange swaps		(1,805,980)	829,048
Loss on disposition of fixed assets		730,190	160,555
Contributions restricted for long-term investment		—	(829,294)
Changes in assets and liabilities:			
Grants and accounts receivable		8,963,988	6,920,801
Due from unconsolidated affiliates, net		(5,277,056)	633,715
Inventories		(1,270,938)	5,444,343
Prepaid expenses, deposits, and other assets		(3,661,622)	(948,519)
Pledges receivable		(217,414)	(352,372)
Accounts payable and accrued liabilities		(13,194,535)	6,455,669
Deferred revenue		4,710,114	3,820,270
Net cash provided by (used in) operating activities		(10,470,639)	36,930,298
Cash flows from investing activities:			
Purchase of investments		(2,523,740)	(1,796,401)
Issuances of microfinance loans, net		(7,876,211)	(17,975,849)
Acquisition of property and equipment		(7,626,319)	(3,979,633)
Disposition and addition of entities		94,361	(548,460)
Net cash used in investing activities		(17,931,909)	(24,300,343)
Cash flows from financing activities:			
Repayment of notes receivable		82,072	80,877
Proceeds from borrowings by microfinance entities		30,751,016	31,215,236
Repayments on borrowings of microfinance entities		(20,873,824)	(17,482,468)
Contributions restricted for long-term investment		—	829,294
Proceeds from the issuance of long-term debt		—	100,000
Repayments on long-term debt		(1,353,887)	(4,997,517)
Net cash provided by financing activities		8,605,377	9,745,422
Net increase (decrease) in cash and cash equivalents		(19,797,171)	22,375,377
Cash and cash equivalents at beginning of year		78,631,833	56,256,456
Cash and cash equivalents at end of year	$	58,834,662	78,631,833
Supplemental disclosures:			
Interest paid during the year	$	8,628,005	6,081,788
Noncash contributions		8,244,408	20,856,949

See accompanying notes to consolidated financial statements.

MERCY CORPS AND AFFILIATES

Consolidated Statement of Functional Expenses

Year ended June 30, 2012

	Program services						Support services		
	Humanitarian assistance – relief	Humanitarian assistance – recovery	Livelihood/ economic development	Civil society and education	Health	Total program services	General and administration	Resource development	Total expenses
Personnel	$ 10,615,573	5,808,500	17,636,494	13,357,236	5,676,297	53,094,100	19,729,578	5,330,055	78,153,733
Professional services	1,078,965	462,819	2,416,017	2,547,551	333,173	6,838,525	672,457	947,824	8,458,806
Professional services – in kind	—	—	121,115	—	—	121,115	967,567	—	1,088,682
Travel and vehicle expense	2,678,476	995,713	3,557,901	2,208,925	1,074,901	10,515,916	3,475,418	390,634	14,381,968
Office and occupancy expense	1,996,143	807,446	2,768,031	1,977,848	1,111,323	8,660,791	2,239,406	2,694,418	13,594,615
Other operating expenses	393,775	161,429	358,047	297,900	53,875	1,265,026	513,494	1,764,466	3,542,986
Material aid	—	—	—	—	6,737,761	6,737,761	417,965	—	7,155,726
Materials and supplies	9,301,610	5,158,227	4,796,738	4,373,676	1,474,744	25,104,995	1,244	28,955	25,135,194
Construction, nonowned assets	4,352,857	578,411	2,389,993	6,460,428	594,709	14,376,398	—	—	14,376,398
Training, monitoring, and evaluation	779,261	515,700	2,260,123	1,814,859	631,118	6,001,061	5,997	—	6,007,058
Subgrants	13,415,830	22,223,081	14,329,838	11,151,671	4,377,113	65,497,533	75,626	—	65,573,159
Microfinancing activity	—	—	20,910,521	—	—	20,910,521	92,336	—	21,002,857
Depreciation	416,568	162,191	1,722,573	482,271	164,706	2,948,309	1,091,981	15,676	4,055,966
Interest expense	—	—	10,669,637	—	—	10,669,637	1,074,084	7,219	11,750,940
	$ 45,029,058	36,873,517	83,937,028	44,672,365	22,229,720	232,741,688	30,357,153	11,179,247	274,278,088

See accompanying notes to consolidated financial statements.

MERCY CORPS AND AFFILIATES

Consolidated Statement of Functional Expenses

Year ended June 30, 2011

	Program services						Support services		
	Humanitarian assistance – relief	**Humanitarian assistance – recovery**	**Livelihood/ economic development**	**Civil society and education**	**Health**	**Total program services**	**General and administration**	**Resource development**	**Total expenses**
Personnel	$ 10,628,029	7,380,232	19,561,184	16,801,579	5,555,131	59,926,155	15,428,316	5,506,432	80,860,903
Professional services	3,051,405	203,580	1,060,257	1,789,964	334,390	6,439,596	820,855	704,271	7,964,722
Professional services – in kind	—	—	—	—	—	—	1,631,628	—	1,631,628
Travel and vehicle expense	2,893,252	1,490,298	3,807,347	3,013,294	1,093,627	12,297,818	2,922,589	411,658	15,632,065
Office and occupancy expense	2,143,121	1,488,913	3,292,026	2,876,530	1,192,335	10,992,925	2,311,370	2,362,910	15,667,205
Other operating expenses	338,609	279,793	1,922,939	565,681	179,483	3,286,505	2,162,967	1,029,924	6,479,396
Material aid	12,908,153	—	—	—	—	12,908,153	—	—	12,908,153
Materials and supplies	15,224,439	7,451,037	6,403,452	3,099,248	1,458,550	33,636,726	31,421	—	33,668,147
Construction, nonowned assets	2,726,893	2,663,849	3,775,944	8,239,345	2,729,139	20,135,170	6,623	—	20,141,793
Training, monitoring, and evaluation	862,915	774,430	2,903,213	2,379,026	1,115,157	8,034,741	8,354	—	8,043,095
Subgrants	14,446,152	20,737,834	14,816,677	8,765,088	4,040,491	62,806,242	128,290	—	62,934,532
Microfinancing activity	47,352	47,352	18,465,382	—	—	18,560,086	121,622	—	18,681,708
Depreciation	424,426	129,847	1,217,889	444,050	142,865	2,359,077	921,327	17,053	3,297,457
Interest expense	558	52	4,398,020	—	62	4,398,692	1,169,052	8,935	5,576,679
	$ 65,695,304	42,647,217	81,624,330	47,973,805	17,841,230	255,781,886	27,664,414	10,041,183	293,487,483

See accompanying notes to consolidated financial statements.

(1) Organization and Purpose

Mercy Corps, headquartered in Portland, Oregon, is incorporated under the laws of the State of Washington as a nonprofit corporation. Mercy Corps' mission is to alleviate suffering, poverty, and oppression by helping people build secure, productive, and just communities around the globe.

Mercy Corps' Vision for Change, based on the Universal Declaration of Human Rights, is that peaceful, secure, and just societies emerge when the private, public, and civil society sectors are able to interact with accountability, inclusive participation, and mechanisms for peaceful change.

Mercy Corps' Strategy is to work in countries in transition, where communities are suffering and recovering from disaster, conflict, or economic collapse. Mercy Corps' experience demonstrates that during these times of turmoil and tragedy, there exists the possibility for positive change. Mercy Corps adds its greatest value as an international relief and development agency by supporting those kernels of positive change with community-led and market-driven action.

Mercy Corps operates programs in more than 40 countries throughout the world. Mercy Corps classifies its program activities into five major types: Humanitarian Assistance – Relief, Humanitarian Assistance – Recovery, Livelihood and Economic Development, Civil Society and Education, and Health.

The consolidated financial statements include the accounts of Mercy Corps and its controlled affiliates, collectively, "the Organization" or "Mercy Corps." All material intercompany transactions and balances have been eliminated. Consolidated affiliates include:

Mercy Corps Foundation (MCF)

Mercy Corps Headquarters Manager, Inc.

Mercy Corps Headquarters Building, LLC

Mercy Corps Headquarters Master Tenant Manager, LLC

Mercy Corps Headquarters Master Tenant, LLC

Kompanion Financial Group Microfinance Closed Joint Stock Company

Asian Credit Public Fund

Hunchun Association for Poverty Alleviation in the Tumen River Area

Yanbian Association for Poverty Alleviation in the Tumen River Area

MICRA Philippines Foundation, Inc.

Yayasan Microfinance Innovation & Resource Center Foundation

Mercy Enterprise Corporation (MEC) d/b/a Mercy Corps Northwest

MC Singapore (formed in 2010)

Mercy Corps India (formed 2010)

Mercy Corps International, Jordan

(2) Summary of Significant Accounting Principles

(a) Basis of Accounting

The accompanying consolidated financial statements of the Organization have been prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles.

Net assets are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the Organization's net assets and changes therein are classified and reported as follows:

- Unrestricted net assets – net assets that are not subject to donor-imposed restrictions. As reflected in the accompanying financial statements, Mercy Corps Board of Directors has designated a portion of the unrestricted net assets.
- Temporarily restricted net assets – net assets that are subject to donor-imposed restrictions that permit the Organization to use or expend the assets as specified. The restrictions are satisfied either by the passage of time, or by actions of Mercy Corps.
- Permanently restricted net assets – net assets that are subject to donor-imposed restrictions that are maintained in perpetuity by the Organization.

(b) Use of Estimates

The preparation of consolidated financial statements, in conformity with accounting principles generally accepted in the United States, requires management to make estimates and assumptions that affect the reported assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates in the Organization's consolidated financial statements include loan loss reserves, fair value of investments, and net realizable value of pledges receivables. Actual results may differ from those estimates.

(c) Revenue Recognition

Contributions, including unconditional promises to give, are recognized as revenue in the period received at net realizable value. Contribution revenues are reported as increases in unrestricted net assets unless their use is limited by donor-imposed restrictions.

Funds provided under grant or contract, which are not considered contributions, are deemed to be earned and reported as revenue when Mercy Corps has incurred expenditures in compliance with the specific terms and conditions of the grant or contract. Grant or contract funds received for which no corresponding expenditure has yet been made are accounted for as deferred revenue. Expenditures made in advance of funds received are recorded as grants receivable.

Donated services that meet the criteria for recognition in accordance with generally accepted accounting principles are reported as gift in kind services and expenses in amounts equal to their estimated fair value on the date of receipt. Approximately \$1.1 million and \$1.6 million of legal services were provided pro bono to the Organization in 2012 and 2011, respectively.

Commodities are received and reported at fair value and recognized as revenue as the commodities are distributed for program purposes.

Gifts in kind and contributions of fixed assets are reported as contributions at their estimated fair values on the date of receipt and reported as expense when utilized.

(d) Functional Allocation of Expenses

The Organization allocates expenses on a functional basis among its various programs and supporting services. Expenses that can be identified with a specific program or supporting service are charged directly. Other expenses that are common to several functions are allocated by various statistical bases.

(e) Change in Net Assets from Operations

Change in net assets from operations excludes activities that Mercy Corps considers to be outside the scope of its business, as defined by their mission statement.

(f) Foreign Currency Translation

Assets and liabilities denominated in foreign currencies are translated into U.S. dollars at the exchange rate in effect on reporting dates, and revenues and expenses are translated at rates that approximate the average rate for the period in which the transactions occurred. Net transaction and translation gains and losses are included in the accompanying statements of activities in the nonoperating section as foreign currency exchange gain or loss.

(g) Income Taxes

Mercy Corps has been granted tax-exempt status under Section 501(c)(3) of the Internal Revenue Code and corresponding sections of the State of Washington provisions as a publicly supported Organization, which is not a private foundation.

Mercy Corps applies Accounting Standards Codification (ASC) Topic 740, *Accounting for Income Taxes* (ASC 740), related to uncertainties in income taxes, which prescribes a comprehensive model for recognizing, measuring, presenting, and disclosing in the consolidated financial statements tax positions taken or expected to be taken on a tax return.

The Organization believes it has not taken any significant uncertain tax positions, and accordingly, the adoption of the applicable sections of ASC 740 did not have a significant impact on the Organization's consolidated financial statements.

(h) Cash

Cash and cash equivalents consist of short-term, highly liquid investments with original maturities of three months or less at the date of acquisition. The Organization held no cash equivalents as of June 30, 2012 and 2011.

Certain cash accounts are maintained as separate accounts that represent cash held in trust or as collateralized cash. These types of accounts totaled $2,874,286 and $2,918,947 at June 30, 2012 and 2011, respectively.

(i) Investments

The Organization holds various types of investments, including money market accounts and mutual funds. Investments are recorded at fair value. Interest and dividends earned on funds are included in interest income classified as either unrestricted or temporarily restricted based on donor stipulations. There are no significant concentrations as the portfolio is diversified among issuers.

(j) Derivative Financial Instruments

Derivative financial instruments include foreign currency swaps and an interest rate swap. The Organization utilizes these strategies to minimize risk associated with fluctuations in both interest rates and foreign currency exchange rates. Derivatives are initially recognized at fair value on the date on which the derivative contract is entered into and are subsequently remeasured at fair value. All derivatives are carried as assets when their fair value is positive and as liabilities when their fair value is negative. Changes in the fair value of derivatives are recognized currently as an unrealized gain or loss on swap agreements in other non-operating revenue and expenses, net.

(k) Fair Value Measurements

The Organization applies the accounting standard, *Fair Value Measurements and Disclosures* (ASC 820), that established a framework for measuring fair value. This standard defines the fair value as the amount that would be exchanged for an asset or to transfer a liability in an orderly transaction between market participants at the measurement date.

The standard establishes a three-level fair value hierarchy that prioritizes the valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1 – Unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.

Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted market prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the whole term of the assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available.

The Organization used the following methods and significant assumptions to estimate fair value for its assets measured and carried at fair value in the consolidated financial statements:

Investments – Fair values for these investments are based on quoted market prices (Level 1).

Derivative financial instruments – The fair value of the Organization's interest rate and currency swaps are based on estimates using standard pricing models that take into account the present value of future cash flows as of the date of the statements of financial position. The fair values of the interest and currency rate swaps are based on models that rely on observable market-based data (Level 2).

(l) Fair Value of Financial Instruments

The carrying value of cash, grants and other receivables, loans receivable and payable, and variable rate long-term debt approximates their estimated fair value as of June 30, 2012 and 2011, due to the relative short maturities of these instruments. In accordance with ASC 825-10-50, *Financial Instruments – Overall – Disclosures*, management has determined that it is not practicable to estimate the fair value of notes receivable, subsidiary and subordinated debt for microfinancing activities, and long-term debt due to the unique nature of each of these transactions, including the relationship of these instruments to the various tax credit exchange programs and the international microfinance industry. Additionally, none of these transactions have available quoted market equivalents. Additional information about matters affecting the fair value, such as current interest rates and maturities, is included at note 5 for notes receivable, note 9 for long-term debt, and note 10 for subsidiary and subordinated debt for microfinancing activities.

(m) Grants and Accounts Receivable

The majority of the Organization's grants and accounts receivables are due from private foundations and federal agencies. Grants and accounts receivable are expected to be collected within one year and are recorded at net realizable value.

Pledges receivable and notes receivable that are expected to be collected in future years are recorded at fair value at the date of the contribution, as determined using the net present value of estimated future cash flows.

(n) Microfinance Loans Receivable

Financial services are an essential element of the Organization's integrated approach to helping people. In this sector, the Organization has established microfinance institutions (MFIs), structured loan guarantee programs, built capacity in existing MFIs, and created service organizations to contribute to the development of the overall microfinance industry. Activities from these services are reported as livelihood/economic development expense in the statements of activities, and it is the Organization's intent to reinvest all proceeds generated back into mission-related programs.

The following MFIs and MFI technical assistance organizations are consolidated in the accompanying consolidated financial statements.

Kompanion Financial Group Microfinance Closed Joint Stock Company (Kompanion), a for-profit entity, was formed in 2004 in the Kyrgyz Republic to engage in microfinance activities. Mercy Corps is the Founder and only shareholder of Kompanion.

Asian Credit Public Fund (ACF) was formed in 2001, and is registered in the Republic of Kazakhstan as a nonprofit nonmember organization to carry out certain types of banking operations. Mercy Corps is the Founder of ACF.

Asian Credit Fund Microcredit Organization, Limited Liability Company (ACF, MCO, LLC) was incorporated in 2007 as a for-profit commercial microcredit organization in the Republic of Kazakhstan and is wholly owned by ACF. In 2009, ACF MCO LLC was reregistered with Mercy Corps becoming a Participant, owning 60% of the capital, and ACF owning 40%. As Mercy Corps is the Founder of ACF and has a controlling interest, Mercy Corps controls ACF MCO LLC.

Ariana Financial Services JSC (AFS), a nondistributive joint stock company in Afghanistan, was formed in 2007 to engage in humanitarian purposes and social welfare activities with respect to the development of poor people in Afghanistan through the use of microfinance and microcredit. AFS ceased operations in May 2011 when it became apparent that the MFI would not become financially sustainable without a significant financial and human resource investment on the part of Mercy Corps for a minimum five-year period and/or a merger with another organization of similar size. An Assignment and Assumption Agreement was concluded on May 25, 2011 between AFS and the Microfinance Investment Support Facility for Afghanistan, LTD (MISFA), which had provided most of the lending capital and operating costs of AFS. The agreement transferred all AFS rights to outstanding loans, including interest due on loans, and other assets to MISFA.

Hunchun Association for Poverty Alleviation in the Tumen River Area and the Yanbian Association for Poverty Alleviation in the Tumen River Area (collectively, the PATRAs) were formed in 2002 and 2003, respectively, as a means toward the alleviation of poverty and suffering in certain areas in China. These organizations are registered under Chinese law and are considered local projects of Mercy Corps. Under a Memorandum of Understanding, Mercy Corps controls the PATRA entities.

In 2001, Mercy Corps established Mercy Enterprise Corporation (MEC), dba Mercy Corps Northwest, as a nonprofit corporation under the laws of the State of Oregon in order to provide economic development services to low-income populations in the states of Oregon and Washington. Mercy Corps maintains control of the board of directors along with control and management of MEC's programs.

MICRA Philippines Foundation, Inc. was formed in 2008 as a non-stock, nonprofit corporation under the laws of the Republic of the Philippines. The purpose of the foundation is to support the Philippine microfinance sector by providing technical inputs, training, education and research. The Foundation is controlled by a Board of Trustees, composed primarily of Mercy Corps employees.

Yayasan Microfinance Innovation & Resource Center Foundation was formed in 2006 in Indonesia to provide technical assistance to the development, improvement and progress of the microfinance industry sector. The Foundation is controlled by an Advisor Board, composed of Mercy Corps employees.

Microfinance loans receivable are recorded in the consolidated statements of financial position at their unpaid principal balances net of allowance for loan losses. Interest income is accrued based on the outstanding principal amount and contractual terms of each individual loan. The Organization reviews its loans to assess impairment on a regular basis. A loan is considered impaired when, based on current information, it is probable that the Organization will not receive all amounts due in accordance with the contractual terms of the underlying loan agreement. When an impairment loss has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan receivable and the present value of the estimated future cash flows including amounts recoverable from guarantees and collateral discounted at the loan receivable's original effective interest rate. All loan receivable losses are recognized in the consolidated statements of activities. When a loan is uncollectible, it is written off against the related reserve for loan impairment. Loan balances are written off when management determines that the loans are uncollectible and when all necessary steps to collect the loan are exhausted.

(o) Inventories and Material Aid

The Organization receives agricultural commodities from governments for distribution via Organization programs and for monetization in which proceeds are to be used to fund Organization programs. Commodities received for distribution are recorded at estimated fair value as inventory and refundable advances. Revenue is recognized as inventory is distributed, and is recorded in the consolidated statements of activities as "Material Aid." Funds received from monetization of commodities are deferred until utilized in program activities. Revenue earned from monetization proceeds is recognized in the consolidated statements of activities as "Material aid – monetized."

Material aid commodities received from the U.S. government that are held for sale are valued at the lesser of the fair value on the contribution date or the expected sales price in the foreign location, if impaired. Material aid commodities held for distribution and not for sale are valued at estimated fair value.

(p) Program-Related Investments

Program-related investments represent the Organization's investments in domestic and overseas organizations that do not meet the standard of control for consolidation under U.S. generally accepted accounting principles. The investments are typically in the form of equity investments funded with grants or the Organization's unrestricted funds. The purpose of these investments is the furtherance of the Organization's mission rather than the generation of income. Investments are recorded on either the cost or equity method, depending on the Organization's level of ownership and influence over the entities.

(q) Property and Equipment, Net

Land, buildings, and equipment are stated at acquisition cost or fair value on date of contribution. Depreciation is computed on a straight-line basis over the shorter of the estimated useful lives of the respective assets or the related lease term. The estimated useful lives by asset class are as follows:

	Years
Buildings	30 – 39
Leasehold improvements	3 – 30
Furniture, fixtures and equipment	3 – 10
Vehicles	3 – 5

The Organization has adopted a policy of applying a time restriction that expires over the useful life of the long-lived assets acquired, or constructed with contributions restricted for that purpose, and therefore, releases amounts from temporarily restricted net assets ratably over the same useful life.

(r) Reclassifications

Certain reclassifications have been made to prior year amounts to conform to the current year presentation.

(3) Fair Value of Financial Instruments and Investments

Fair value measurements at June 30, 2012 consisted of the following:

	Level 1	Level 2	Total
Assets:			
Investments:			
Mutual funds – equity	$ 1,328,077	—	1,328,077
Mutual funds – fixed income	1,956,234	—	1,956,234
Common Stocks	303,126	—	303,126
Total investments	3,587,437	—	3,587,437
Derivative financial instruments:			
Foreign currency swap arrangements	—	2,892,959	2,892,959
Total	$ 3,587,437	2,892,959	6,480,396
Liabilities:			
Derivative financial instruments:			
Interest rate swaps	$ —	606,398	606,398
Total	$ —	606,398	606,398

Fair value measurements at June 30, 2011 consisted of the following:

		Level 1	Level 2	Total
Assets:				
Investments:				
Mutual funds – equity	$	781,142	—	781,142
Mutual funds – fixed income		486,420	—	486,420
Equity investment		40,797	—	40,797
Total investments		1,308,359	—	1,308,359
Derivative financial instruments:				
Foreign currency swap arrangements		—	481,828	481,828
Total	$	1,308,359	481,828	1,790,187
Liabilities:				
Derivative financial instruments:				
Interest rate swaps	$	—	592,964	592,964

Mercy Corps had no Level 3 assets or liabilities measured at fair value at June 30, 2012 and 2011.

(4) Pledges Receivable

Unconditional promises to give are included in the consolidated financial statements as pledges receivable and revenue of the appropriate net asset category. Pledges receivable are expected to be collected in future years and are recorded after discounting at 0.21% to 0.41% to the present value of expected future cash flows.

Unconditional promises are expected to be collected in the following periods:

		2012	2011
One year or less	$	1,805,396	2,026,967
Between one year and five years		726,343	992,500
		2,531,739	3,019,467
Less allowance		—	(600,000)
Less discount		(12,503)	(10,737)
Pledges receivable, net	$	2,519,236	2,408,730

(5) Notes Receivable

At June 30, 2012 and 2011, notes receivable comprises the following:

		2012	2011
A note receivable from a U.S. corporation, interest at prime less 2.00% and at a guaranteed minimum 3.00% and maximum 6.00%, matures January 17, 2013, rate of 3% at June 30, 2012 and 2011	$	79,682	161,754
A note receivable from Mercy Corps Investment Fund, LLC, interest at 4.75%, matures April 1, 2015		10,987,489	10,987,489
Total notes receivable	$	11,067,171	11,149,243

As discussed further at note 9, Mercy Corps Investment Fund, LLC, is a third-party entity controlled by U.S. Bank, and therefore, it is not consolidated into the Organization's financials.

(6) Microfinance Loans Receivable

Microcredit loans comprise variable and fixed-rate loans with individuals and groups. Group loans are unsecured loans granted to a group of borrowers who sign a loan agreement with joint and several liability to repay a loan. The loans bear interest at rates generally at or below the local market industry average available. Microcredit loans are issued with original maturities ranging from 3 to 36 months. Individual microcredit loans are generally secured by real estate or business assets and have fixed payments.

Microfinance loans receivable were concentrated in the following countries as of June 30, 2012 and 2011:

		2012	2011
China	$	1,151,571	1,144,437
Kazakhstan		4,125,498	3,354,437
Kyrgyzstan		62,186,012	53,967,017
Other		601,933	612,834
		68,065,014	59,078,725
Less loan loss reserves		(3,269,896)	(3,303,405)
Microfinance loans receivable, net	$	64,795,118	55,775,320

The Organization adopted ASU No. 2010 20, Disclosure about the Credit Quality of Financing Receivables and the Allowance for Credit Losses (Topic 310), effective June 30, 2012. This ASU is intended to provide financial statement users with greater transparency about an entity's allowance for credit losses and the credit quality of its financial receivables. This ASU amends existing disclosures and provides additional disclosures about its financing receivables on a disaggregated basis.

Activity in the provision for loan loss reserve on microcredit loans is as follows for the years ended June 30, 2012 and 2011:

		2012	2011
Loan loss reserve, June 30, 2011	$	(3,303,405)	(1,703,749)
Additional reserve, or reversal – current year, net		33,509	(1,599,656)
Loan loss reserve, June 30, 2012	$	(3,269,896)	(3,303,405)

The aging of financing receivables as of June 30, 2012 is presented as follows:

Allowances for estimated losses are established based on prior collection experience and observed trends in the rate of default, as well as a consideration of current economic trends and indicators. Loan balances are written off when they are deemed to be ultimately uncollectible.

Changes in allowance for estimated losses on financing receivables as of June 30, 2012 are presented as follows:

Beginning balance	$	(3,303,405)
Adjustments to reserve		(255,573)
Writeoff		350,926
Recovery		(61,845)
Ending balance	$	(3,269,897)

The reserves noted above can be attributed to loans that are past due or current as follows at June 30, 2012:

		Current	Past due	Total
Microfinance loans receivable	$	67,185,455	879,559	68,065,014
Less: loan loss reserves		(2,754,188)	(515,708)	(3,269,896)
Microfinance loans receivable, net	$	64,431,267	363,851	64,795,118

(7) Property and Equipment

		2012	2011
Land	$	3,816,024	3,787,172
Building and leasehold improvements		36,943,082	33,695,716
Vehicles		8,858,556	6,875,014
Furniture, fixtures, and equipment		6,432,070	5,013,024
Property and equipment		56,049,732	49,370,926
Less accumulated depreciation and amortization		(13,170,478)	(9,331,835)
Property and equipment, net	$	42,879,254	40,039,091

(8) Program-Related Investments

The Organization’s program-related investments at June 30, 2012 and 2011 are as follows:

		2012	2011
PT Bank Andara, Indonesia	$	4,700,372	5,008,428
TenGer Financial Group LLC (previously, XAC–GE LLC), Mongolia		623,543	623,543
Kompanion Invest		478,168	—
MicroVest I, LLP		32,600	200,000
MICRO		616,267	486,024
MC India			45,903
MEVCF		32,500	13,000
MLO IMON International LLC, Tajikistan		5,208	5,208
	$	6,488,658	6,382,106

PT Bank Andara (Andara), a limited liability company, was organized under the laws of the Republic of Indonesia in 2009 by an investor consortium, led by Mercy Corps. Mercy Corps founded Bank Andara to deliver innovative financial services to millions of low-income Indonesian families. Andara serves as the strategic banking partner to the Indonesian microfinance sector, which encompasses over 50,000 institutions. At June 30, 2012 and 2011, the Organization owned 26.15% and 33.65%, respectively, of the outstanding shares of Andara. In July 2012, Mercy Corps purchased an additional 2,136 shares of Andara for $250,000. This is not reflected in the financial statements for the year ended June 30, 2012. In July 2012, Mercy Corps ownership dropped to 22% due to additional investments from other equity investors. This investment is reported on the equity method of accounting. The summarized financial data for Andara is as follows:

		2012	**2011**
Total assets	$	95,741,787	48,413,805
Total liabilities		(77,765,822)	(33,527,610)
Total equity	$	17,975,965	14,886,195
Total operating revenue	$	8,490,008	3,771,342
Total operating expense		(11,200,848)	(6,370,853)
Nonoperating gain (loss)		37,713	(200,911)
Net loss	$	(2,673,127)	(2,800,422)

TenGer Financial Group, LLC (TenGer), formerly, XAC-GE LLC, is a Mongolian company, whose largest holding is XacBank. XacBank was formed in 2001 through a combination of microfinance activities from local nonbank financial institutions. Mercy Corps was one of the initial funders of this entity through a variety of investments that started in December 1999, when Mercy Corps formed a for-profit, nonbanking institution whose mission was to serve the credit needs of small and medium enterprises (SMEs) in the Mongolian Gobi region. At June 30, 2012 and 2011, the Organization owned 8.4% and 11.42% of the outstanding shares of TenGer. This investment is recorded on a cost basis.

Kompanion Invest was formed in Kyrgyzstan in October 2011 to provide a bank based on the Shariah principles. The organization is owned 99.9% by Kompanion Financial Group Microfinance CJSC (Kompanion), a wholly owned subsidiary of Mercy Corps. Kompanion does not consolidate Kompanion Invest, but does report the investment on an equity basis.

MicroVest I, LLP (the Fund) is a Delaware limited partnership. The investment objective of the Fund is to provide social impact and capital appreciation by lending to and making equity investments in MFI's located throughout the developing world. In 2011, Mercy Corp divested its interest in Microvest. The remaining investment balance represents amount not yet distributed at June 30, 2012. At June 30, 2011, the Organization owned less than 2% of the Fund and, accordingly, reported this investment on a cost basis.

MICRO Insurance Catastrophe Risk Organization SCC and MiCRO Insurance Catastrophe Risk Organization Cell A (MICRO) were formed in March 2011 to engage in the insurance business to achieve alleviation of poverty in Haiti and elsewhere in the Caribbean region by providing immediate relief to the economically disadvantaged in the event of future natural disasters. The entity is organized to allow ownership of the various legal components at different levels. At June 30, 2012, Mercy Corps owned 50%

of MiCRO – SCC and 23.3% of MiCRO – Cell A. At June 30, 2011 Mercy Corps owned 50.0% of both. Mercy Corps reports the investment in MICRO's on an equity basis.

Mercy Corps India (MC India) was formed in August 2010 as joint-stock company. As of June 30, 2012, the accounts of MC India are consolidated with Mercy Corps. There has yet to be any significant activity in Mercy Corps India.

In fiscal 2011, Mercy Corps invested in the Middle East Venture Capital Fund, L.P. (MEVCF). The purpose of MEVCF is a venture capital fund focusing primarily on stimulating economic development by making investments in companies in the West Bank and Gaza by providing seed and early stage financing to small and medium sized businesses in the information and communications technology sectors. At June 30, 2012 and 2011, Mercy Corps owned less than 2% of this fund. The investment is recorded on a cost basis.

MLO IMON International LLC (IMON) is a microfinance institution established in 2008 in the Republic of Tajikistan. At June 30, 2012 and 2011, the Organization owned less than 1% of IMON. This investment is recorded on a cost basis. Mercy Corps is also one of two Founders of International Micro lending Fund IMON, a noncommercial not-for-profit microfinance fund that owns 90.8% of IMON. As Mercy Corps does not control International Micro Lending Fund IMON, their results are not included in Mercy Corps' consolidated financial statements.

(9) Debt

On September 14, 2009, Mercy Corps occupied a new headquarter building in Portland, Oregon. Financing for the $38 million project was provided by a Mercy Corps capital campaign, commercial loans, sale of a condominiumized unit, and both New Market Tax Credit (NMTC) and Federal Historic Tax Credit (FHTC) funding.

Mercy Corps Investment Fund, LLC (MCIF) is the investor for the NMTC program. MCIF is funded by a commercial loan, a loan from Mercy Corps Foundation and equity investment from a private investor. As the NMTC program investor, MCIF is required to make Qualified Equity Investments (QEIs) in eligible Community Development Entities (CDEs) with available tax credit allocations. MCIF contributed QEI funds to three separate CDEs. Each of the three CDEs used the QEI funds, through designated sub-CDEs, to make Qualified Low-Income Community Investments (QLICIs) in the form of loans to Mercy Corps Headquarters Building, LLC, as a Qualified Active Low-Income Community Investment Business (QALICB). Mercy Corps does not control or have an interest in MCIF or in the sub-CDEs, and accordingly, MCIF and the sub-CDEs are not consolidated in Mercy Corps' consolidated financial statements. Mercy Corps guarantees MCIF's commercial loan. The guaranty requires that Mercy Corps set aside funds monthly into a bank-controlled account, the balance of which is reported as a deposit on Mercy Corps' consolidated statement of financial position.

Mercy Corps Headquarters Building, LLC's (Building) sole purpose is to function as a QALICB. Building is funded by QLICI loans from sub-CDEs, FHTC equity investment from Mercy Corps Headquarters Master Tenant, LLC (Tenant), and other equity investment from Mercy Corps Headquarters Manager, Inc. (Manager).

At June 30, long-term debt consisted of the following:

	2012	2011
NCF Sub-CDE, LLC:		
Interest rate of LIBOR+1.9% (2.15% at June 30, 2012 and 2.09% at 2011) for 28.12% of the outstanding principal balance and a fixed rate of 4.11% for 71.88% of the outstanding principal balance. Interest-only payments are due monthly, until the loan matures on March 3, 2038, secured by real property	$ 9,801,000	9,801,000
NNMF Sub-CDE III, LLC:		
Interest rate of LIBOR+1.9% (2.15% at June 30, 2012 and 2.09% at 2011) for 28.12% of the outstanding principal balance and a fixed rate of 3.67% for 71.88% of the outstanding principal balance. Interest-only payments are due monthly, until the loan matures on March 19, 2038, secured by real property	7,275,000	7,275,000
U.S. Bank Sub-CDE XX, LLC:		
Interest rate of LIBOR+1.9% (2.15% at June 30, 2012 and 2.09% at 2011) for 28.12% of the outstanding principal balance and a fixed rate of 3.67% for 71.88% of the outstanding principal balance. Interest-only payments are due monthly, until the loan matures on March 19, 2038, secured by real property	6,930,000	6,930,000
Meyer Memorial Trust:		
Interest rate is fixed at 2.00%. The unsecured loan is payable in three installments from June 2011 through June 2013.	500,000	750,000
U.S. Bank:		
Interest rate of LIBOR+1.90% (2.09% at 2011) Balance was paid in June 2012	—	1,072,686
Eastern Bank:		
Interest rate of Prime+1.00% (4.25% at June 30, 2012 and 2011, and payable in monthly principal and interest installments, with a balloon payment due in November 2018), secured by real property.	509,652	523,706
Portland Development Commission:		
Interest is variable (1% at June 30, 2012 and 2011), payable in monthly principal and interest installments, with a balloon payment due in March 2018, secured by real property	342,702	359,849
	$ 25,358,354	26,712,241

(Continued)

Future maturities of long-term debt outstanding at June 30, 2012 are as follows:

Year ended:		
2013	$	528,374
2014		29,604
2015		30,887
2016		32,225
2017		33,622
Thereafter		24,703,642
	$	25,358,354

(a) Line of Credit

The Organization has a $3,500,000 line of credit commitment with a bank for working capital purposes, which bears interest at a Base Rate (higher of Prime, LIBOR plus 1.50%, or Fed Funds Rate plus 1.50%) or LIBOR plus 2.15%, depending on the term selected by the Organization and a fee of 0.50% on the unused portion of the line of credit. The line is collateralized by a security interest in the Organization's non-building assets, was renewed on July 1, 2012 and expires on July 1, 2013. As of June 30, 2012 and 2011, the Organization has no outstanding borrowings under the line of credit.

(b) Covenants

The credit agreements with U.S. Bank, Eastern Bank and the line of credit bank contain certain restrictive covenants that require, among other things, that the Organization maintain certain fixed charge coverage ratios and minimum levels of unrestricted cash and cash equivalents.

(10) Subsidiary and Subordinated Debt for Microfinancing Activities

Microfinancing debt proceeds are primarily used to finance the Organization's microfinance lending activities. Typically, this debt is not collateralized and principal payments are expected to be made from the flow of cash from collection of the MFI loan receivables. Mercy Corps does not guarantee the repayment on this debt. Payment terms on these loans vary.

Debt maturities as of June 30, 2012 were as follows:

Year ended:		
2013	$	11,749,679
2014		21,461,500
2015		17,701,101
2016		9,133,419
2017		—
Thereafter		678,422
	$	60,724,121

The above debt is held by the following subsidiaries of Mercy Corps:

	2012	2011
Mercy Enterprise Corporation	$ 781,125	700,000
Kompanion	53,758,666	44,912,015
ACF, MCO, LLC	6,181,449	5,230,519
MICRA Philippines	2,881	—
	$ 60,724,121	50,842,534

Interest rates at June 30, 2012 are as follows:

Subsidiary	Lender	Interest rates	Balance
Mercy Enterprise Corporation	Various	2.00% - 4.00%	$ 781,125
Kompanion	BlueOrchard	6.80% - 9.00%	4,025,441
Kompanion	Deutsche Bank	7.00% - 10.50%	7,025,049
Kompanion	Developing Word Markets	6.50%	6,038,162
Kompanion	Eurasian Bank	6.01% - 13.00%	6,497,535
Kompanion	Frontiers	19.00%	213,362
Kompanion	Incofin	7.00% - 8.00%	7,447,066
Kompanion	Oikocredit	15.00%	3,907,105
Kompanion	responsAbility	7.00% - 18.00%	7,534,982
Kompanion	Symbiotics	6.75% - 8.00%	5,031,802
Kompanion	Triodos	7.25%	6,038,162
ACF, MCO, LLC	Various	5.00% - 17.25%	6,181,449
MICRA Philippines	Various	Various	2,881
			$ 60,724,121

The above debt also includes subordinated debts of $7,878,800 and $7,703,369 at June 30, 2012 and 2011, respectively. This subordinated debt is subordinate to all other debt of the individual subsidiary. Payment terms can be accelerated only if the respective subsidiary fails to make interest payments, uses proceeds for a purpose other than that stated in the debt agreements, or ceases its normal operations. The subordinated debt maturity dates range from 2013 to 2018; however, the actual maturity dates are automatically extended each year unless the lender exercises its rights to set the final maturity date.

(11) Temporarily Restricted Net Assets

Temporarily restricted net assets are available for the following purposes as of June 30, 2012 and 2011:

	2012	2011
Organization programs	$ 17,507,683	26,259,692
Headquarters building	7,382,098	7,237,632
	$ 24,889,781	33,497,324

(12) Permanently Restricted Net Assets

The Organization applies ASC 958-205, *Presentation of Financial Statements* in accounting for their permanently restricted net assets. The Organization has interpreted UPMIFA as requiring the preservation of the original gift as of the gift date of donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Organization classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The earnings on the donor-restricted endowment fund that are classified as temporarily restricted net assets until those amounts are appropriated for expenditure in a manner consistent with standard of prudence prescribed by UPMIFA. As of June 30, 2012 and 2011, the Organization had one donor-restricted endowment of $20,000.

(13) Obligations under Operating Leases

The Organization leases office space under operating leases that require payments through 2015. The leases contain annual escalation clauses at fixed percentages or based on the consumer price index. At June 30, 2012 the Organization's aggregate minimum annual operating lease commitments are as follows:

2013	$ 798,707
2014	446,059
2015	176,956
2016	66,540
2017	75,234
Thereafter	54,323
	$ 1,617,819

Total rent expense was $4,586,550 and $3,841,145 for the fiscal years ended June 30, 2012 and 2011. A portion of this rent expense relates to facilities that are not under a formal lease agreement.

(14) Commitments and Contingencies

The Organization receives a substantial portion of its funding in the form of grants from the U.S. government. These grants contain certain compliance and internal control requirements that, if violated, may result in the disallowance of certain costs incurred under the grant programs. As of June 30, 2012 and 2011, the Organization recorded a contingent liability of $936,300 and $691,500, respectively for estimated disallowances based on management's review of prior history and assessment of the current status of grant programs.

The Organization is involved in various other legal matters and claims in the ordinary course of its operations. While it is not possible to determine the ultimate liability, if any, in these matters at this time, in the opinion of management, such matters will not have a material adverse effect on the financial condition of the Organization.

(15) Employee Benefit Plan

The Organization has a defined contribution plan under Internal Revenue Code Section 403(b) for employees who meet the eligibility conditions. Employees are eligible to make voluntary pretax contributions beginning the first day of the month following their employment date. Employees are eligible to receive employer contributions equal to 6% of gross salary after one year of service. The Organization's contributions to the plan for the years ended June 30, 2012 and 2011 amounted to $1,095,493 and $991,335, respectively.

The Organization also has an employee benefit plan for certain third-country nationals who are otherwise ineligible for the defined-contribution plan under Internal Revenue Code Section 403(b). These employees are eligible to receive employer contributions equal to 6% of gross salary after one year of service. The Organization's contributions to the program for the years ended June 30, 2012 and 2011 amounted to $280,193 and $339,210, respectively.

Within the various countries in which the Organization operates outside the U.S., most employees are citizens of the host country. These employees are generally not eligible for the Organization's defined contribution plan or for the employee benefit plan for third-country nationals; however, they are eligible for certain local government sponsored plans appropriate for that country.

(16) Related Parties

Mercy Corps Scotland (MCS) is a nonprofit corporation registered in the United Kingdom. MCS has a separate board of directors and controls and manages its own programs. MCS possesses legal and fiscal responsibility and final oversight for projects implemented with grants and contributions that it receives from donors and government agencies. MCS has a clear and unequivocal responsibility to ensure that any program it supports or undertakes falls within the scope of its activities as set forth under Scottish charity legislation and that all funds are used appropriately. The Organization does not and cannot exert direct financial or operational control over MCS, and as such, MCS is not included in the Organization's consolidated financial statements.

MCS and the Organization share the same mission, purpose, and values as partners in an international network of colleagues working together to fulfill the basic purpose of the Organization's programs worldwide. MCS and the Organization work closely together as affiliates and, in some instances, both organizations will pool administrative and technical resources for the benefit of their respective projects. In such cases, an invoice for the actual costs incurred will be sent between MCS and the Organization.

The Organization entered into a Memorandum of Understanding (MOU) with MCS on April 14, 2005. This MOU states that the Organization will assume any of MCS' financial liabilities that might arise from donor disallowances. Additionally, the Organization has agreed to indemnify MCS for all expenses related to material aid transactions in Europe. As of June 30, 2012 and 2011, the Organization is not aware of any material known or contingent donor disallowances arising from program activities carried out by MCS.

As of June 30, 2012 and 2011 the net amount due from MCS and other affiliates was $8,113,458 and $2,503,615, respectively.

(17) Significant Sources of Revenue and Concentration of Risk

(a) Significant Sources of Revenue

The Organization receives a majority of its funding through grants from the U.S. government. A reduction in the amount of grants available or in the Organization's ability to receive government grants would have a material impact on its programs and operations.

(b) Concentration of Risk

For cash held in the United States of America, the Organization places its cash in high credit quality institutions. At times, such amounts may be in excess of the Federal Deposit Insurance Company (FDIC) limits. Management believes that the risk with respect to the balances in excess of FDIC limits is minimal. At June 30, 2012 and 2011, the Organization held $36,829,979 and $50,765,941, respectively, of cash and cash equivalents in U.S. financial institutions, of which $35,647,451 and $48,727,268 was uninsured.

In order to fulfill grant agreements, the Organization maintains cash balances inside foreign countries and in the local currencies. The Organization's MFI's also hold cash overseas for purposes of ongoing operations. Uninsured cash held overseas, in approximately 38 countries, was $22,004,683 and $29,066,313, at June 30, 2012 and 2011, respectively.

(18) Subsequent Events

The Organization has performed an evaluation of subsequent events through November 12, 2012, which is the date the consolidated financial statements were available to be issued.

MERCY CORPS AND AFFILIATES

Supplemental Schedules – Mercy Corps

Mercy Corps

June 30, 2012 and 2011

The following Schedules I, II, and III are a presentation of the financial position and financial activities and changes in net assets for Mercy Corps on an unconsolidated basis. These amounts are included as part of the consolidated financial statements of Mercy Corps and affiliates for the fiscal years ended June 30, 2012 and 2011.

Schedule I

MERCY CORPS AND AFFILIATES

Supplemental Schedule – Mercy Corps Statements of Financial Position

June 30, 2012 and 2011

Assets		**2012**	**2011**
Cash	$	48,738,006	68,824,836
Grants and accounts receivable		12,858,318	22,139,948
Microfinance loans receivable		41,426	29,376
Due from unconsolidated affiliates, net		15,437,745	9,310,165
Inventories		7,000,952	5,730,014
Prepaid expenses, deposits, and other assets		5,049,761	4,185,565
Pledges receivable, net		2,519,236	2,408,730
Notes receivable		79,682	161,754
Investments		7,799,403	5,522,091
Program-related investments		19,119,794	13,472,756
Property and equipment, net		7,992,043	6,855,904
Total assets	$	126,636,366	138,641,139
Liabilities and Net Assets			
Liabilities:			
Accounts payable and accrued liabilities	$	21,393,856	36,180,866
Deferred revenue		31,445,372	26,886,335
Long-term debt		1,352,354	1,633,555
Total liabilities		54,191,582	64,700,756
Net assets:			
Unrestricted:			
Undesignated		47,128,665	40,443,059
Designated		426,338	—
		47,555,003	40,443,059
Temporarily restricted		24,889,781	33,497,324
Permanently restricted		—	—
Total net assets		72,444,784	73,940,383
Total liabilities and net assets	$	126,636,366	138,641,139

See accompanying independent auditors' report.

Schedule II

MERCY CORPS AND AFFILIATES

Supplemental Schedule – Mercy Corps Statement of Activities

Mercy Corps

Year ended June 30, 2012

	Unrestricted	Temporarily restricted	Totals
Operating support and revenue:			
Public support and revenue:			
Government grants	$ 151,448,528	—	151,448,528
Material aid	7,155,726	—	7,155,726
Material aid – monetized	11,757,281	—	11,757,281
Total public support and revenue	170,361,535	—	170,361,535
Private support and revenue:			
Other grants	34,511,360	—	34,511,360
Contributions	18,683,017	8,016,270	26,699,287
Gift in kind services	967,567	—	967,567
Total private support and revenue	54,161,944	8,016,270	62,178,214
Other revenue:			
Interest income	397,006	—	397,006
Other revenue	1,330,089	60,218	1,390,307
Total other revenue	1,727,095	60,218	1,787,313
Net assets released from restriction	16,684,031	(16,684,031)	—
Total operating support and revenue	242,934,605	(8,607,543)	234,327,062
Operating expenses:			
Program services:			
Humanitarian assistance – relief	45,029,058	—	45,029,058
Humanitarian assistance – recovery	36,873,516	—	36,873,516
Livelihood/economic development	51,745,449	—	51,745,449
Civil society and education	44,819,516	—	44,819,516
Health	22,229,721	—	22,229,721
Total program services	200,697,260	—	200,697,260
Supporting services:			
General and administrative	29,477,360	—	29,477,360
Resource development	11,385,258	—	11,385,258
Total supporting services	40,862,618	—	40,862,618
Total operating expenses	241,559,878	—	241,559,878
Change in net assets from operations	1,374,727	(8,607,543)	(7,232,816)
Other nonoperating revenue and expenses, net:			
Foreign currency exchange loss, net	(542,589)	—	(542,589)
Realized and unrealized gain on investments, net (1)	6,279,806	—	6,279,806
Total nonoperating revenue and expenses, net	5,737,217	—	5,737,217
Change in net assets	7,111,944	(8,607,543)	(1,495,599)
Net assets at beginning of year	40,443,059	33,497,324	73,940,383
Net assets at end of year	$ 47,555,003	24,889,781	72,444,784

(1) $5,757,494 of this balance represents the recapitalization of Kompanion and Asian Credit Fund. These entities are recorded on a cost basis by Mercy Corps. The cost basis investment is eliminated in consolidation, but results in this signficant increase in the current year unconsolidated statements of Mercy Corps.

See accompanying independent auditors' report.

Schedule III

MERCY CORPS AND AFFILIATES

Supplemental Schedule – Mercy Corps Statement of Activities

Mercy Corps

Year ended June 30, 2011

	Unrestricted	Temporarily restricted	Totals
Operating support and revenue:			
Public support and revenue:			
Government grants	$ 185,277,544	—	185,277,544
Material aid	12,639,812	—	12,639,812
Material aid – monetized	8,672,676	—	8,672,676
Total public support and revenue	206,590,032	—	206,590,032
Private support and revenue:			
Other grants	13,073,777	18,448,060	31,521,837
Private contributions	16,961,758	10,339,767	27,301,525
Gift in kind -services	1,631,628	—	1,631,628
Contributions for the acquisition of property	—	829,294	829,294
Total private support and revenue	31,667,163	29,617,121	61,284,284
Other revenue:			
Interest income	665,742	—	665,742
Other revenue	2,045,837	5,500	2,051,337
Total other revenue	2,711,579	5,500	2,717,079
Net assets released from restriction	31,311,314	(31,311,314)	—
Total operating support and revenue	272,280,088	(1,688,693)	270,591,395
Operating expenses:			
Program services:			
Humanitarian assistance – relief	65,695,304	—	65,695,304
Humanitarian assistance – recovery	42,647,217	—	42,647,217
Livelihood/economic development	57,378,914	—	57,378,914
Civil society and education	48,078,250	—	48,078,250
Health	17,841,230	—	17,841,230
Total program services	231,640,915	—	231,640,915
Supporting services:			
General and administrative	26,744,101	—	26,744,101
Resource development	10,340,015	—	10,340,015
Total supporting services	37,084,116	—	37,084,116
Total operating expenses	268,725,031	—	268,725,031
Change in net assets from operations	3,555,057	(1,688,693)	1,866,364
Other nonoperating revenue and expenses, net:			
Foreign currency exchange gain	277,159	—	277,159
Realized and unrealized gain on investments	(2,569,320)	—	(2,569,320)
Total nonoperating revenue and expenses, net	(2,292,161)	—	(2,292,161)
Change in net assets	1,262,896	(1,688,693)	(425,797)
Net assets at beginning of year	39,180,163	35,186,017	74,366,180
Net assets at end of year	$ 40,443,059	33,497,324	73,940,383

See accompanying independent auditors' report.