



OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(With Independent Auditors' Report Thereon)

OPERATION SMILE, INC. AND AFFILIATE

Table of Contents

	Page(s)
Independent Auditors' Report	1 – 2
Combined Financial Statements:	
Combined Statements of Financial Position	3
Combined Statements of Activities	4
Combined Statements of Cash Flows	5
Combined Statements of Functional Expenses	6
Notes to Combined Financial Statements	7 – 15



KPMG LLP
Suite 1900
440 Monticello Avenue
Norfolk, VA 23510

Independent Auditors' Report

The Board of Directors
Operation Smile, Inc.:

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

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these combined financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of combined financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these combined 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 combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the combined financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the combined 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 combined 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 combined financial statements referred to above present fairly, in all material respects, the financial position of Operation Smile, Inc. and affiliate as of June 30, 2013 and 2012, and the results of their operations and their cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

KPMG LLP

Norfolk, Virginia
November 27, 2013

OPERATION SMILE, INC. AND AFFILIATE

Combined Statements of Financial Position

June 30, 2013 and 2012

Assets	2013	2012
Cash (notes 11 and 12)	\$ 5,439,932	6,827,162
Investments (note 3)	1,689,482	3,043,591
Prepaid expenses	181,026	359,261
Mission advances and other receivables	255,297	76,919
Contributions receivable, net (note 2)	15,828,884	14,145,340
Inventories	5,419,218	7,015,320
Property and equipment, net (notes 4, 6, and 11)	18,815,081	16,345,662
Total assets	\$ 47,628,920	47,813,255
Liabilities and Net Assets		
Accounts payable and accrued expenses	\$ 4,120,197	7,013,698
Deferred revenue	194,125	317,687
Capital lease payable (notes 4 and 6)	67,669	33,276
Long-term debt (note 11)	9,467,575	8,130,152
Total liabilities	13,849,566	15,494,813
Net assets:		
Unrestricted	19,206,835	14,573,810
Temporarily restricted (note 7)	14,572,519	17,744,632
Total net assets	33,779,354	32,318,442
Commitments, contingencies, and subsequent events (notes 6, 11, and 12)		
Total liabilities and net assets	\$ 47,628,920	47,813,255

See accompanying notes to combined financial statements.

OPERATION SMILE, INC. AND AFFILIATE

Combined Statements of Activities

Years ended June 30, 2013 and 2012

	2013			2012		
	Unrestricted net assets	Temporarily restricted net assets	Total	Unrestricted net assets	Temporarily restricted net assets	Total
Revenues:						
Contributions (note 10)	\$ 36,019,018	13,497,803	49,516,821	37,298,170	17,367,970	54,666,140
Gifts-in-kind (note 5)	2,228,823	—	2,228,823	3,356,591	—	3,356,591
Contributed services (note 5)	26,424,721	—	26,424,721	26,253,585	—	26,253,585
Program service revenue	687,755	—	687,755	1,277,336	—	1,277,336
Foreign currency transaction gains (losses), net	4,017	—	4,017	(83,689)	—	(83,689)
Other income (expense), net	40,831	—	40,831	12,650	—	12,650
Net assets released from restrictions (note 8)	16,669,916	(16,669,916)	—	8,051,212	(8,051,212)	—
Total revenues	<u>82,075,081</u>	<u>(3,172,113)</u>	<u>78,902,968</u>	<u>76,165,855</u>	<u>9,316,758</u>	<u>85,482,613</u>
Expenses:						
Program services :						
Medical missions (note 5)	39,057,337	—	39,057,337	38,963,786	—	38,963,786
Education and sustainability	15,195,423	—	15,195,423	18,174,955	—	18,174,955
Total program services	<u>54,252,760</u>	<u>—</u>	<u>54,252,760</u>	<u>57,138,741</u>	<u>—</u>	<u>57,138,741</u>
Supporting services:						
Fund-raising	16,248,847	—	16,248,847	16,121,782	—	16,121,782
Administration	6,940,449	—	6,940,449	4,807,349	—	4,807,349
Total supporting services	<u>23,189,296</u>	<u>—</u>	<u>23,189,296</u>	<u>20,929,131</u>	<u>—</u>	<u>20,929,131</u>
Total expenses	<u>77,442,056</u>	<u>—</u>	<u>77,442,056</u>	<u>78,067,872</u>	<u>—</u>	<u>78,067,872</u>
Change in net assets	4,633,025	(3,172,113)	1,460,912	(1,902,017)	9,316,758	7,414,741
Net assets at beginning of year	14,573,810	17,744,632	32,318,442	16,475,827	8,427,874	24,903,701
Net assets at end of year	<u>\$ 19,206,835</u>	<u>14,572,519</u>	<u>33,779,354</u>	<u>14,573,810</u>	<u>17,744,632</u>	<u>32,318,442</u>

See accompanying notes to combined financial statements.

OPERATION SMILE, INC. AND AFFILIATE

Combined Statements of Cash Flows

Years ended June 30, 2013 and 2012

	2013	2012
Cash flows from operating activities:		
Change in net assets	\$ 1,460,912	7,414,741
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Depreciation expense	599,847	331,397
Loss on disposal of equipment	48,076	45,093
Equipment donation to program countries	15,502	31,004
Net realized and unrealized (gains) losses on investments	(637)	6,025
Net use (receipt) of in-kind donations of supplies and inventory	1,452,132	(126,773)
In-kind donation of artwork	—	(210,347)
Investment contributions received	(160,846)	(268,874)
Changes in operating assets and liabilities:		
Prepaid expenses	178,235	812,268
Mission advances and other receivables	(178,378)	495,010
Contributions receivable	(1,683,544)	(8,604,955)
Inventories	143,970	(157,029)
Accounts payable and accrued expenses	(2,893,501)	2,122,488
Deferred revenue	(123,562)	(519,988)
Net cash (used in) provided by operating activities	(1,141,794)	1,370,060
Cash flows from investing activities:		
Purchases of property and equipment	(3,132,844)	(10,470,585)
Purchases of investments	(198)	(2,720)
Proceeds from sales and maturities of investments	1,515,790	2,728,195
Net cash used in investing activities	(1,617,252)	(7,745,110)
Cash flows used in financing activities:		
Borrowings on long-term debt	1,337,423	8,130,152
Net borrowings (repayments) on capital leases	34,393	(12,671)
Net cash provided by financing activities	1,371,816	8,117,481
Net increase (decrease) in cash	(1,387,230)	1,742,431
Cash at beginning of year	6,827,162	5,084,731
Cash at end of year	\$ 5,439,932	6,827,162
Supplemental cash flow information:		
Cash paid for interest, net of capitalized interest	\$ 312,148	8,696

See disclosure of noncash items in note 5.

See accompanying notes to combined financial statements.

OPERATION SMILE, INC. AND AFFILIATE

Combined Statements of Functional Expenses

Years ended June 30, 2013 and 2012

	2013						
	Program services			Supporting services			Total expenses
	Medical missions	Education and sustainability	Total	Fund-raising	Administration	Total	
Grants	\$ 1,349,430	5,012,901	6,362,331	—	—	—	6,362,331
Salaries and benefits	2,079,824	1,714,772	3,794,596	2,438,740	2,477,281	4,916,021	8,710,617
Professional services	542,463	1,233,577	1,776,040	1,078,810	1,406,881	2,485,691	4,261,731
Advertising and promotion	63,359	132,531	195,890	1,061,974	97,297	1,159,271	1,355,161
Supplies and equipment	5,700,944	316,139	6,017,083	433,137	1,114,083	1,547,220	7,564,303
Occupancy	289,192	39,690	328,882	100,093	224,652	324,745	653,627
Travel and conferences	2,488,391	994,023	3,482,414	326,636	267,539	594,175	4,076,589
Interest	3,852	1,561	5,413	1,015	305,720	306,735	312,148
Depreciation	112,961	18,758	131,719	—	468,128	468,128	599,847
Insurance	36,459	1,613	38,072	861	52,654	53,515	91,587
Other mission expense	323,841	—	323,841	—	—	—	323,841
Fundraising	—	—	—	10,776,024	—	10,776,024	10,776,024
Public education and awareness	—	5,301,206	5,301,206	—	455,891	455,891	5,757,097
Contributed services	26,022,319	402,402	26,424,721	—	—	—	26,424,721
Other	44,302	26,250	70,552	31,557	70,323	101,880	172,432
Total expenses	\$ 39,057,337	15,195,423	54,252,760	16,248,847	6,940,449	23,189,296	77,442,056

	2012						
	Program services			Supporting services			Total expenses
	Medical missions	Education and sustainability	Total	Fund-raising	Administration	Total	
Grants	\$ 1,453,855	5,996,659	7,450,514	—	—	—	7,450,514
Salaries and benefits	2,107,670	2,001,486	4,109,156	2,245,308	1,985,873	4,231,181	8,340,337
Professional services	567,052	1,226,835	1,793,887	931,484	750,790	1,682,274	3,476,161
Advertising and promotion	57,986	344,624	402,610	932,337	161,743	1,094,080	1,496,690
Supplies and equipment	4,905,093	301,952	5,207,045	679,138	890,028	1,569,166	6,776,211
Occupancy	285,009	41,977	326,986	74,617	63,225	137,842	464,828
Travel and conferences	2,817,777	2,213,552	5,031,329	308,483	243,799	552,282	5,583,611
Interest	3,277	1,622	4,899	949	2,848	3,797	8,696
Depreciation	172,984	—	172,984	—	158,413	158,413	331,397
Insurance	48,243	4,722	52,965	1,909	29,784	31,693	84,658
Other mission expense	272,500	313	272,813	—	17	17	272,830
Fundraising	—	—	—	10,923,129	—	10,923,129	10,923,129
Public education and awareness	—	6,023,824	6,023,824	—	478,315	478,315	6,502,139
Contributed services	26,253,585	—	26,253,585	—	—	—	26,253,585
Other	18,755	17,389	36,144	24,428	42,514	66,942	103,086
Total expenses	\$ 38,963,786	18,174,955	57,138,741	16,121,782	4,807,349	20,929,131	78,067,872

See accompanying notes to combined financial statements.

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(1) Nature of Organization and Summary of Significant Accounting Policies

(a) *Nature of Organization*

Operation Smile, Inc. (Operation Smile) is a 501c(3) not-for-profit voluntary health and welfare organization whose principal purpose is to perform life-changing reconstructive surgery on children with facial deformities such as cleft lips and cleft palates in developing countries and the United States. Operation Smile is the largest volunteer-based charity providing free cleft surgeries for children around the world, and is a leading advocate for medical education and training to impact universal surgery practices and related public health initiatives to build long-term self-sufficiency in developing countries. The organization's activities also focus on community-based education and training, nutrition, research, as well as post-operative and comprehensive care.

In May 2010, OS HQ, LLC, a wholly owned subsidiary of Operation Smile, was formed to hold the assets and liabilities for a new global center located in Virginia Beach, Virginia. A groundbreaking was held in September 2010 with construction completed in the Fall 2012.

In July 2003, Operation Smile Foundation, Inc. (the Foundation), also a 501c(3) organization, became active. The purpose of the Foundation is to provide long-term financial support and fundraising capabilities to Operation Smile. The bylaws of the Foundation require that 85% of the earnings and other income, as defined, be disbursed to Operation Smile on a quarterly basis. The remaining 15% is to remain in the Foundation for the purpose of expanding and preserving the Foundation's asset base. As discussed in note 12, in July 2013, Operation Smile and the Foundation ceased to be affiliated entities.

Operation Smile and the Foundation comprise the combined group collectively referred to as OSI. OSI currently has nine active chapter organizations throughout the United States and four representative offices in international countries, and their activities have been included in the accompanying financial statements. The accompanying combined financial statements do not include the accounts of OSI affiliates in international countries. OSI has international foundations that host mission teams, which are responsible for all in-country mission logistics. International foundations may also raise funds and awareness to support programs in international countries.

(b) *Principles of Combination*

The accompanying combined financial statements include the accounts of Operation Smile (including its wholly owned subsidiary, OS HQ, LLC) and the Foundation. All significant intercompany balances and transactions have been eliminated in combination.

(c) *Classification of Gifts*

OSI reports gifts of cash and other assets, including unconditional promises to give, as increases to unrestricted net assets, unless use of the related assets is limited by donor-imposed restrictions. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the accompanying combined statements of activities as net assets released from restrictions.

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(d) Unconditional Promises to Give

Contributions are recognized as revenue when an unconditional promise to give has been made. Unconditional promises to give that are expected to be collected within one year are recorded at net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using risk-free interest rates applicable to the years in which the promises were received. Amortization of the discounts is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. Conditional promises to give are not included as revenue until the conditions are substantially met.

(e) Cash

Cash consists primarily of cash in banks. Cash in banks exceeded federally insured limits at both June 30, 2013 and 2012. Total cash for the year ended June 30, 2013 and 2012 was \$5,439,932 and \$6,827,162, respectively.

(f) Investments

Investment securities consist primarily of money market funds held in investment broker accounts, U.S. Treasury bills, and mutual funds. The net realized and unrealized gains and losses on investments are reflected in other income (expense), net, in the accompanying combined statements of activities.

(g) Prepaid Expenses

Prepaid expenses are stated at cost less applicable amortization and include expenses prepaid for events that will occur in the next fiscal year and for insurance premiums, which are expensed over their estimated useful lives using the straight-line method.

(h) Inventories

Inventories consist primarily of supplies to be used for medical missions. Purchased inventory is valued at the lower of cost or fair value and donated inventory is valued at fair value, both on the first-in, first-out basis.

(i) Property and Equipment

Property and equipment are stated at cost except for donated equipment, artwork, and land, which are stated at fair value at the date of receipt. Medical equipment and furniture, fixtures, and office equipment are depreciated using the straight-line method over estimated useful lives ranging from 3 to 10 years. No provision for depreciation is made on land or artwork. No provision for depreciation is made on construction in process or work in process until such time as the relevant assets are completed and placed in service. Buildings and building improvements are depreciated using the straight-line method over their estimated useful lives of 40 years. Total depreciation expense for the years ended June 30, 2013 and 2012 was \$599,847 and \$331,397, respectively.

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(j) **Deferred Revenue**

Deferred revenue consists of cash collected for events that will occur in future periods.

(k) **Classification of Net Assets**

OSI's net assets are grouped into the following three classes:

Unrestricted Net Assets – Unrestricted net assets generally result from contributions and other revenues not subject to donor-imposed restrictions.

Temporarily Restricted Net Assets – Temporarily restricted net assets generally result from contributions and other revenues whose use by the organization is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of OSI pursuant to those stipulations.

Permanently Restricted Net Assets – Permanently restricted net assets result from contributions whose use by the organization is limited by donor stipulation that neither expire by passage of time nor can be fulfilled or otherwise removed by OSI. There were no permanently restricted net assets at June 30, 2013 or 2012.

(l) **Functional Expenses**

OSI allocates its 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 allocated directly. Other expenses that are common to several functions are allocated based on various statistical bases, such as content, time, and purpose.

(m) **Joint Cost Allocation**

OSI incurred expenses that were identifiable with a particular function but served joint purposes. Expenses related to certain events, donor communication, and program materials jointly support medical missions, education and sustainability, fundraising, and administration and were allocated by their function classification as follows for the years ended June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Medical missions	\$ 70,230	33,177
Education and sustainability	5,885,166	6,470,618
Fund-raising	9,827,863	9,148,512
Administration	1,076,129	867,295
Total joint costs	<u>\$ 16,859,388</u>	<u>16,519,602</u>

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(n) **Capitalized Interest**

OSI's policy is to capitalize interest cost incurred on debt during the construction of major projects exceeding one year. A reconciliation of total interest cost to "Interest" as reported in the combined statements of functional expenses for 2013 and 2012 is as follows:

	<u>2013</u>	<u>2012</u>
Interest cost capitalized	\$ 132,898	116,311
Interest cost charged to income	312,148	8,696
Total interest cost	<u>\$ 445,046</u>	<u>125,007</u>

(o) **Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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 these estimates.

(p) **Fair Value Measurements**

OSI utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and determines fair value based on assumptions that market participants would use in pricing an asset or liability in the principal or most advantageous market. When considering market participant assumptions in fair value measurements, the following fair value hierarchy distinguishes between observable and unobservable inputs, which are categorized in one of the following levels:

- Level 1 Inputs: Unadjusted quoted prices in active markets for identical assets or liabilities accessible to OSI at the measurement date.
- Level 2 Inputs: Other than quoted prices included in Level 1 inputs that are observable for the asset or liability, either directly or indirectly.
- Level 3 Inputs: Unobservable inputs for the asset or liability used to measure fair value to the extent that observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at measurement date.

OSI's investments represent the financial assets that are accounted for at fair value on a recurring basis. At June 30, 2013 and 2012, the carrying value of all the investments was considered to be the fair value determined using Level 1 inputs in the fair value hierarchy. There were no transfers in and out of Levels 1 and 2 for the years ended June 30, 2013 and 2012.

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(q) **Impairment of Long-Lived Assets**

Long-lived assets, such as property and equipment, and purchased intangible assets subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. As of June 30, 2013 and 2012, there was no indication of impairment. Any assets to be disposed of within the next fiscal year would be separately presented in the statements of financial position and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposal group classified as held-for-sale would be presented separately in the appropriate asset and liability sections of the statements of financial position.

(2) **Contributions Receivable**

Contributions receivable at June 30, 2013 and 2012 are expected to be received as follows:

	<u>2013</u>	<u>2012</u>
Within one year	\$ 4,127,017	2,391,262
From one to five years	11,892,210	12,017,345
	<u>16,019,227</u>	<u>14,408,607</u>
Less discount to present value at rates, which range from 0.13% to 3.29%	<u>190,343</u>	<u>263,267</u>
	<u>\$ 15,828,884</u>	<u>14,145,340</u>

(3) **Investments**

Investments consist of the following at June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Money market funds	\$ 1,689,482	2,928,304
Mutual funds	<u>—</u>	<u>115,287</u>
Total investments	<u>\$ 1,689,482</u>	<u>3,043,591</u>

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(4) Property and Equipment

Property and equipment consist of the following at June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Construction in process (new global center)	\$ —	12,215,385
Work in process	7,751	76,316
Medical equipment	2,689,312	2,548,890
Furniture, fixtures, and office equipment	1,528,482	1,310,026
Buildings	14,932,143	240,555
Building improvements	634,681	362,448
Land	3,094,293	3,094,293
Artwork	210,347	210,347
	<u>23,097,009</u>	<u>20,058,260</u>
Less accumulated depreciation	<u>4,281,928</u>	<u>3,712,598</u>
Property and equipment, net	<u>\$ 18,815,081</u>	<u>16,345,662</u>

As of June 30, 2013 and 2012, furniture, fixtures, and office equipment recorded under capital leases have a cost basis of \$91,436 and \$88,909 and related accumulated amortization of \$23,767 and \$55,633 for a net book value of \$67,669 and \$33,276, respectively.

(5) Contributed Services and Gifts-in-Kind

OSI's medical missions are staffed by volunteer surgical teams. In addition, when patients require treatment in the United States under the World Care Program, the hospital stay and related services are fully or partially donated by the hospitals and physicians. Services are also contributed within the United States for medical and dental care. These donated medical services are recorded at their estimated fair values and are classified as contributed services revenues and medical missions expenses in the accompanying combined statements of activities. Such services amounted to \$26,424,721 and \$26,253,585 in 2013 and 2012, respectively. OSI's medical missions are staffed by volunteer administrative support staff. These administrative personnel services are not recorded in the accompanying combined financial statements.

Donated mission supplies are received throughout the year for use in the overall Operation Smile mission, are recorded at their estimated fair values, and are classified as gifts-in-kind revenues in the accompanying statements of activities. Such donations amounted to \$2,203,196 and \$3,146,244 in 2013 and 2012, respectively. These supplies are expensed as they are used on missions and are classified as medical missions expenses in the accompanying statements of activities. Use of donated mission supplies amounted to \$3,655,328 and \$3,019,471 in 2013 and 2012, respectively.

The organization received a sculpture to be placed at the new global center. The estimated fair market value of the sculpture, \$210,347, is included in gifts-in-kind revenues in the accompanying statements of activities for 2012. Other donated non-mission supplies amounted to \$25,627 and \$0 in 2013 and 2012, respectively.

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(6) Leases

OSI is obligated under capital and operating leases for its facility and certain equipment. The facility lease is an operating lease expiring in November 2013.

Future minimum lease payments under the operating lease and the present value of future minimum capital lease payments as of June 30, 2013 are as follows:

	<u>Capital lease</u>	<u>Operating lease</u>
Year ending June 30:		
2014	\$ 24,634	163,171
2015	24,361	69,756
2016	18,253	45,733
2017	11,762	—
2018	5,881	—
	<u>84,891</u>	<u>\$ 278,660</u>
Total minimum lease payments		
Less amount representing interest	<u>17,222</u>	
Present value of net minimum lease payments	67,669	
Less current maturities of capital lease obligations	<u>18,682</u>	
Capital lease obligations, excluding current maturities	<u>\$ 48,987</u>	

Total rent expense was \$316,287 and \$327,349 in 2013 and 2012, respectively.

(7) Temporarily Restricted Net Assets

Temporarily restricted net assets consist of the following at June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Care centers	\$ 314,109	448,255
Domestic programs	43,505	54,828
Fellowships	271,412	90,200
Global education and sustainability	15,187	67,097
International programs	886,583	1,124,931
Land	—	3,050,000
Research	38,383	141,414
Other programs	<u>109,309</u>	<u>57,165</u>
Total purpose restricted	1,678,488	5,033,890
Total time restricted	<u>12,894,031</u>	<u>12,710,742</u>
Total temporarily restricted net assets	<u>\$ 14,572,519</u>	<u>17,744,632</u>

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

(8) Net Assets Released from Restrictions

Net assets were released from donor restrictions by incurring expenses to satisfy the restricted purpose or by occurrence of other events specified by the donors. Total net assets released were \$16,669,916 and \$8,051,212 for the years ended June 30, 2013 and 2012, respectively.

(9) Retirement Savings Plan

OSI has a 401(k) retirement savings plan. Employees are eligible the first of the quarter following four months of employment. OSI matches a portion of the employee contributions and makes a safe harbor contribution on behalf of each employee. OSI's contributions to the retirement savings plans for the years ended June 30, 2013 and 2012 were \$493,372 and \$488,521, respectively.

(10) Related-Party Transactions

OSI received contributions from its Board of Directors and respective committee members of \$116,894 and \$216,894 for the years ended June 30, 2013 and 2012, respectively. Some board members may contribute directly to independent, affiliated Operation Smile international foundations.

(11) Long-Term Debt

Long-term debt at June 30, 2013 and 2012 consists of the following:

	<u>2013</u>	<u>2012</u>
Nonrevolving construction loan up to \$8,500,000, 5.5% interest payable monthly for the first 36 months, followed by monthly installments of principal and interest through July 22, 2018	\$ 8,467,575	7,130,152
Noninterest bearing promissory note (\$1,000,000 principal)	<u>1,000,000</u>	<u>1,000,000</u>
Total long-term debt	9,467,575	8,130,152
Less current installments	<u>—</u>	<u>—</u>
Long-term debt, excluding current installments	<u>\$ 9,467,575</u>	<u>8,130,152</u>

In July 2011, a donor pledged \$10,000,000 and OSI entered into a construction loan agreement with a financial institution to complete construction of its new global center. The loan is guaranteed by the donor and is secured by a first priority lien on the property. The loan agreement requires OSI to maintain a minimum aggregate liquidity of \$5,000,000, as defined, as well as a \$1,000,000 compensating balance to be held by the financial institution until the loan is paid in full. Repayment terms are interest only due monthly for 36 months, followed by 47 consecutive, equal monthly installments of principal and interest based on a 20-year amortization, and the then-current interest rate, as determined by the financial institution.

OPERATION SMILE, INC. AND AFFILIATE

Combined Financial Statements

June 30, 2013 and 2012

In September 2011, OSI obtained \$1,000,000 cash and entered into an interest-free promissory note for the same amount for expansion of its global direct response program. Repayment of the note began in November 2013.

(12) Subsequent Events

On July 11, 2013, OSI effectuated a spin-off of the Foundation as a nonaffiliated organization. As part of the agreement to spin-off the Foundation, OSI agreed to pay the Foundation \$3,500,000 million in cash plus another \$500,000 in inventory and supplies. The majority of the required payment is to fulfill OSI's repayment obligation of debt owed to the Foundation. Per the agreement, on July 11, 2013, OSI paid \$2,000,000 from unrestricted cash to the Foundation. Of the remaining \$1,500,000 of cash owed to the Foundation, \$500,000 will be paid annually beginning on December 31, 2013.

OSI has evaluated subsequent events from the statement of financial position date through November 27, 2013, the date these combined financial statements were available to be issued, and determined there are no other items to disclose.