

FINANCIAL STATEMENTS

Family Health International
Years Ended September 30, 2014 and 2013
With Report of Independent Auditors

Ernst & Young LLP



Building a better
working world

Family Health International

Financial Statements

Years Ended September 30, 2014 and 2013

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Report of Independent Auditors

The Audit Committee
Family Health International

Report on the Financial Statements

We have audited the accompanying financial statements of Family Health International (FHI 360), which comprise the statements of financial position as of September 30, 2014 and 2013, and the related statements of activities and changes in net assets, cash flows and functional expenses for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity 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 financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.



We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of FHI 360 as of September 30, 2014 and 2013, and the changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

June 30, 2015

Family Health International
Statements of Financial Position

	September 30	
	2014	2013
Assets		
Current assets:		
Cash and cash equivalents	\$ 73,953,244	\$ 75,030,882
Restricted cash	11,523,087	12,639,663
Accounts receivable related-party	877,152	–
Accounts receivable	52,360,156	57,209,966
Short-term investments at fair value	12,232,250	17,979,442
Receivable under federal letter of credit	34,313,781	10,294,680
Prepaid expenses	9,058,866	12,163,466
Advances to field offices	1,139,926	3,813,370
Total current assets	<u>195,458,462</u>	189,131,469
Other assets	1,873,289	1,722,316
Property and equipment:		
Property and equipment, net	14,977,711	15,444,149
Total assets	<u>\$ 212,309,462</u>	<u>\$ 206,297,934</u>
Liabilities and net assets		
Current liabilities:		
Accounts payable	\$ 1,101,298	\$ 14,943,528
Accrued expenses	45,774,817	24,878,041
Accrued salaries, payroll taxes, and fringe benefits	11,383,342	7,876,972
Accrued field office severance, leave, and retirement	15,505,768	18,418,726
Deferred revenue	46,641,109	47,194,810
Current portion of deferred rent	850,477	240,165
Note payable related-party	–	2,500,000
Current portion of note payable	610,916	5,346,984
Total current liabilities	<u>121,867,727</u>	121,399,226
Other liabilities	58,172	70,366
Deferred rent, less current portion	646,541	182,575
Note payable, less current portion	10,165,944	1,656,686
Total liabilities	<u>132,738,384</u>	123,308,853
Net assets:		
Unrestricted net assets	78,846,143	82,264,146
Temporarily restricted net assets	724,935	724,935
Total net assets	<u>79,571,078</u>	<u>82,989,081</u>
Total liabilities and net assets	<u>\$ 212,309,462</u>	<u>\$ 206,297,934</u>

See accompanying notes.

Family Health International
Statement of Activities and Changes in Net Assets

Year Ended September 30, 2014

	Unrestricted				Temporarily Restricted	Total
	Contracts and Grants		Other			
	Government	Non- Government	Supported Activities			
Revenues, gains, and other support:						
Contract and grant income:						
Agency for International Development	\$ 457,461,515	\$ -	\$ -	\$ -		\$ 457,461,515
National Institutes of Health	23,685,964	-	-	-		23,685,964
Centers for Disease Control	14,350,076	-	-	-		14,350,076
Department of Health and Human Services	10,486,922	-	-	-		10,486,922
Department of State	20,910,113	-	-	-		20,910,113
Department of Education	2,940,023	-	-	-		2,940,023
Other U.S. Government	2,800,934	-	-	-		2,800,934
Subcontracts from other organizations	-	56,313,325	-	-		56,313,325
	<u>532,635,547</u>	<u>56,313,325</u>	<u>-</u>	<u>-</u>		<u>588,948,872</u>
Sublease income	-	-	4,534,349	-		4,534,349
Income from services	-	45,663,437	-	-		45,663,437
Contributions	-	2,341,401	1,043,816	-		3,385,217
Investment income	-	8,677	78,039	-		86,716
Other income (loss)	-	6,500	(51,637)	-		(45,137)
Total revenues, gains, and other support	<u>532,635,547</u>	<u>104,333,340</u>	<u>5,604,567</u>	<u>-</u>		<u>642,573,454</u>
Expenses:						
Program services:						
Direct project costs	437,048,335	85,086,086	7,299,679	-		529,434,100
Supporting services:						
General and administrative	87,819,088	22,778,745	471,056	-		111,068,889
Subrecipient and subcontractor management	4,861,927	626,541	-	-		5,488,468
Total expenses	<u>529,729,350</u>	<u>108,491,372</u>	<u>7,770,735</u>	<u>-</u>		<u>645,991,457</u>
Change in net assets	<u>\$ 2,906,197</u>	<u>\$ (4,158,032)</u>	<u>(2,166,168)</u>	<u>-</u>		<u>(3,418,003)</u>
Net assets at beginning of year			82,264,146	724,935		82,989,081
Net assets at end of year			<u>\$ 78,846,143</u>	<u>\$ 724,935</u>		<u>\$ 79,571,078</u>

See accompanying notes.

Family Health International
Statement of Activities and Changes in Net Assets

Year Ended September 30, 2013

	Unrestricted				Total
	Contracts and Grants		Other Supported Activities	Temporarily Restricted	
	Government	Non- Government			
Revenues, gains, and other support:					
Contract and grant income:					
Agency for International Development	\$ 476,823,447	\$ -	\$ -	\$ -	\$ 476,823,447
National Institutes of Health	45,218,456	-	-	-	45,218,456
Centers for Disease Control	19,546,771	-	-	-	19,546,771
Department of Health and Human Services	10,401,314	-	-	-	10,401,314
Department of State	11,825,633	-	-	-	11,825,633
Department of Education	3,431,197	-	-	-	3,431,197
Other U.S. Government	3,593,795	-	-	-	3,593,795
Subcontracts from other organizations	-	25,055,896	-	-	25,055,896
	<u>570,840,613</u>	<u>25,055,896</u>	<u>-</u>	<u>-</u>	<u>595,896,509</u>
Sublease income	-	-	4,063,896	-	4,063,896
Income from services	1,453,013	33,717,133	-	-	35,170,146
Contributions	-	-	10,872,233	11,238	10,883,471
Investment income	1,400	-	55,461	-	56,861
Other income (loss)	(11,724)	-	40,081	-	28,357
Total revenues, gains, and other support	<u>572,283,302</u>	<u>58,773,029</u>	<u>15,031,671</u>	<u>11,238</u>	<u>646,099,240</u>
Expenses:					
Program services:					
Direct project costs	471,480,637	48,243,082	4,430,039	-	524,153,758
Supporting services:					
General and administrative	94,929,279	12,996,541	638,018	-	108,563,838
Subrecipient and subcontractor management	2,879,782	263,248	296	-	3,143,326
Total expenses	<u>569,289,698</u>	<u>61,502,871</u>	<u>5,068,353</u>	<u>-</u>	<u>635,860,922</u>
Change in net assets	<u>\$ 2,993,604</u>	<u>\$ (2,729,842)</u>	<u>9,963,318</u>	<u>11,238</u>	<u>10,238,318</u>
Net assets at beginning of year			72,037,066	713,697	72,750,763
Net assets at end of year			<u>\$ 82,264,146</u>	<u>\$ 724,935</u>	<u>\$ 82,989,081</u>

See accompanying notes.

Family Health International

Statements of Cash Flows

	September 30	
	2014	2013
Operating activities		
Change in net assets	\$ (3,418,003)	\$ 10,238,318
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Net realized and unrealized (gain) loss on investments	(33,185)	23,084
Depreciation	4,208,104	4,986,110
Provision for uncollectible accounts	–	116,586
Changes in operating assets and liabilities:		
Accounts receivable	3,972,658	16,679,626
Receivable under Federal letter of credit	(24,019,101)	17,517,847
Prepaid expenses	3,104,600	(6,277,138)
Advances to field offices	2,673,444	2,769,530
Other assets	(150,973)	–
Accounts payable	(13,842,230)	(4,759,725)
Accrued expenses and other liabilities	21,477,994	4,296,947
Deferred revenue	(553,701)	7,041,036
Deferred rent	1,074,278	(92,188)
Net cash (used in) provided by operating activities	(5,506,115)	52,540,033
Investing activities		
Purchase of investments	(60,433)	(11,748,433)
Proceeds from sale of investments	6,957,386	2,186,434
Purchase of equipment	(3,741,666)	(3,769,600)
Net cash provided by (used in) investing activities	3,155,287	(13,331,599)
Financing activities		
Proceeds from note payable	1,273,190	–
Payments on note payable	–	(6,537)
Net cash provided by (used in) financing activities	1,273,190	(6,537)
Net (decrease) increase in cash and cash equivalents	(1,077,638)	39,201,897
Cash and cash equivalents, beginning of year	75,030,882	35,828,985
Cash and cash equivalents, end of year	\$ 73,953,244	\$ 75,030,882

See accompanying notes.

Family Health International
Statement of Functional Expenses

Year Ended September 30, 2014

	Direct Project Costs	General and Administrative	Subrecipient and Subcontractor Management	Total
Salaries	\$ 67,643,812	\$ 48,416,009	\$ 2,945,798	\$ 119,005,619
Allowances	7,641,333	530,255	5,545	\$ 8,177,133
Fringe benefits	20,563,833	14,134,544	852,914	35,551,291
Total personnel	95,848,978	63,080,808	3,804,257	162,734,043
Subawards and grants	196,789,233	-	-	196,789,233
Field office disbursements	91,696,215	2,875,140	37,357	94,608,711
Participant and escort expenses	19,528,085	-	-	19,528,085
Occupancy	3,049,089	19,703,063	1,225,234	23,977,386
Consultants and professional fees	21,578,583	7,026,849	202,432	28,807,864
Travel	32,776,641	5,033,173	37,242	37,847,056
Supplies	9,595,511	406,460	3	10,001,974
Equipment	9,970,669	841,002	-	10,811,671
Equipment rental	670,960	405,613	65	1,076,638
Equipment maintenance and repairs	3,507,073	144,262	54	3,651,389
Freight and postage	1,475,445	133,223	92	1,608,760
Subscriptions and publications	629,018	251,191	9,224	889,433
Printing	4,516,994	248,319	-	4,765,313
Meetings	17,497,727	1,078,470	-	18,576,197
Membership dues	19,118	293,072	2	312,192
Insurance	582,314	750,293	-	1,332,607
Employee relocation and training	1,424,119	386,742	8,926	1,819,787
Depreciation	52,231	4,155,874	-	4,208,105
Employment advertising	351,830	136,515	27	488,372
Office expense	5,187,081	1,388,715	2,460	6,578,256
Other expenses	5,839,542	2,730,105	161,093	8,730,740
Total functional expenses	522,586,456	111,068,889	5,488,468	639,143,813
Nonallocable charges	6,847,644	-	-	6,847,644
Total expenses	<u>\$ 529,434,100</u>	<u>\$ 111,068,889</u>	<u>\$ 5,488,468</u>	<u>\$ 645,991,457</u>

See accompanying notes.

Family Health International
Statement of Functional Expenses

Year Ended September 30, 2013

	Direct Project Costs	General and Administrative	Subrecipient and Subcontractor Management	Total
Salaries	\$ 67,686,435	\$ 46,429,048	\$ 2,208,434	\$ 116,323,917
Allowances	6,887,378	543,674	-	7,431,052
Fringe benefits	20,365,549	13,708,573	635,021	34,709,143
Total personnel	94,939,362	60,681,295	2,843,455	158,464,112
Subawards and grants	206,197,648	-	-	206,197,648
Field office disbursements	76,750,182	3,217,005	40,588	80,007,775
Participant and escort expenses	16,256,950	72,897	-	16,329,847
Occupancy	8,479,726	19,601,025	35	28,080,786
Consultants and professional fees	24,244,117	7,114,908	186,866	31,545,891
Travel	34,076,921	3,820,388	37,177	37,934,486
Supplies	8,526,375	2,644,774	1,081	11,172,230
Equipment	13,649,357	699,556	-	14,348,913
Equipment rental	583,694	314,338	-	898,032
Equipment maintenance and repairs	3,706,098	805,481	31,562	4,543,141
Freight and postage	1,566,772	135,143	117	1,702,032
Subscriptions and publications	917,728	170,238	-	1,087,966
Printing	4,434,053	555,665	1,719	4,991,437
Meetings	18,710,730	896,271	-	19,607,001
Membership dues	246,112	162,155	-	408,267
Insurance	1,411,395	242,625	-	1,654,020
Employee relocation and training	1,300,314	504,631	-	1,804,945
Depreciation	52,335	4,933,775	-	4,986,110
Employment advertising	485,555	48,249	-	533,804
Office expense	4,962,955	827,229	218	5,790,402
Other expenses	(68,845)	1,111,542	508	1,043,205
Total functional expenses	521,429,534	108,559,190	3,143,326	633,132,050
Nonallocable charges	2,724,224	4,648	-	2,728,872
Total expenses	<u>\$ 524,153,758</u>	<u>\$ 108,563,838</u>	<u>\$ 3,143,326</u>	<u>\$ 635,860,922</u>

See accompanying notes.

Family Health International

Notes to Financial Statements

September 30, 2014 and 2013

1. Significant Accounting Policies

Description of the Organization

Family Health International (FHI 360) is a nonprofit global health and development organization that conducts a worldwide diversified program of research, education, and services.

Basis of Accounting

FHI 360 follows the accrual basis of accounting.

Use of Estimates

The preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Program Clusters

OMB Circular A-133 defines a cluster of programs as a grouping of closely related programs that share common compliance requirements. According to this definition, similar programs were deemed to be a cluster of programs and are grouped as such on the Schedule of Expenditures of Federal Awards.

Cash and Cash Equivalents

FHI 360 considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. The total value of cash and cash equivalents at September 30, 2014 and 2013 was \$73,953,244 and \$75,030,882, respectively, which includes cash of \$325,000 and \$325,000, respectively, that is held in a certificate of deposit and is used as collateral for corporate purchases.

Cash and cash equivalents held in the United States are insured according to FDIC regulations. The majority of cash and cash equivalents are held in accounts with balances exceeding the insured limit. Cash amounts maintained overseas are largely uninsured. Cash and cash equivalents as of September 30, 2014 and 2013, held outside of the United States were approximately \$8.8 million and \$11.9 million, respectively.

Family Health International

Notes to Financial Statements (continued)

1. Significant Accounting Policies (continued)

Restricted Cash

FHI 360 received funds under a grant agreement that stipulated the cash is to be placed in a separate account until such time the funds are expended to meet the purpose of the grant. The total amount in the account as of September 30, 2014 and 2013 was \$11,523,087 and \$12,639,663, respectively.

Short-Term Investments

Short-term investments are stated at fair value. The short-term investments consist of government agency obligations and certificates of deposit as of September 30, 2014 and 2013.

Advances to Field Offices

FHI 360 records and tracks funds given to field offices that are remaining at year-end as advances to field offices. When the field office expends the funds for an allowable project, the advance is removed and the appropriate expenditure and revenue amounts are recognized in accordance with the respective agreement. Advances to field offices consist primarily of cash, advances for travel, and other advances. Advances to field offices were \$1,139,926 and \$3,813,370 at September 30, 2014 and 2013, respectively.

Revenue Recognition

Revenue from Federal contracts and grants is recorded to the extent reimbursable costs are incurred. Revenue from contracts with private organizations to conduct research on a fee basis (income from services) is recognized to the extent of expenditures incurred during the contract period.

Unconditional contributions are recognized as revenue when received and are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the nature of any donor restrictions. When a 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 statement of activities as net assets released from restrictions. For 2014 and 2013, there were donor-restricted contributions of zero and \$11,238, respectively.

Family Health International

Notes to Financial Statements (continued)

1. Significant Accounting Policies (continued)

FHI 360 has ongoing multi-year contracts to provide clinical trials services primarily in Asia and Africa. Payments to FHI 360 are made under fixed rate schedules. Revenue is recognized using a proportional performance methodology which factors in the percent of completion of tasks identified in the final statements of work. Total revenues recognized under such contracts were \$47,382 and \$842,527 for the years ended September 30, 2014 and 2013, respectively.

Accounts Receivable

The allowance for doubtful accounts is based on FHI 360's best estimate of the amount of probable credit losses existing in its accounts receivable. FHI 360's allowance for doubtful accounts was \$127,924 and \$318,714 as of September 30, 2014 and 2013, respectively.

Federal Letters of Credit

All U.S. Agency for International Development (USAID) funded agreements and several National Institutes of Health (NIH), Centers for Disease Control (CDC), and Department of Health and Human Services (DHHS) agreements are funded by Federal letters of credit. Drawdowns are paid through the Department of Payment Management. The difference in the estimation of expenditures for requesting funds and the actual expenditures for reporting purposes results in a receivable balance or an unearned income balance at the end of each accounting period. Activity in the Federal letters of credit resulted in a receivable balance of \$34,313,781 and \$10,294,680 at September 30, 2014 and 2013, respectively.

Property and Equipment

Property and equipment are recorded at cost. Donated assets are recorded at the fair value of the property at the date of contribution. Depreciation is computed primarily using the straight-line method over the estimated useful lives of the related asset, ranging from three to five years.

Guidelines for disposals of assets acquired with Federal funds are determined by the contract. Leasehold improvements are amortized on the straight-line basis over the shorter of the useful life of the improvements or the remaining term of the lease.

Family Health International

Notes to Financial Statements (continued)

1. Significant Accounting Policies (continued)

Deferred Revenue

FHI 360 operates its programs with funds from various grants and contracts. At September 30, 2014 and 2013, FHI 360 received funds in excess of expenditures on certain grants and contracts, which resulted in deferred revenue. Total deferred revenue at September 30, 2014 and 2013 was \$46,641,109 and \$47,194,810, respectively.

Income Taxes

FHI 360 is recognized as an organization exempt from Federal income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3) whereby only unrelated business income, as defined by Section 512(a)(1) of the Code, is subject to Federal income tax.

Management has analyzed the tax positions taken by FHI 360 and has concluded that as of September 30, 2014 and 2013, there are no uncertain tax positions taken or are to be taken. Accordingly, no interest or penalties related to uncertain tax positions have been accrued in the accompanying financial statements.

Advertising Costs – Recruitment

FHI 360 expenses the costs of advertising when incurred. Advertising expense was \$488,372 and \$533,804 for the years ended September 30, 2014 and 2013, respectively. Advertising relates primarily to employee recruitment.

Foreign Currency Translation

The U.S. dollar (dollars) is the functional currency for FHI 360's operations worldwide. Transactions in currencies other than dollars are translated into dollars at the rates of exchange in effect during the month of the transaction. Property and equipment purchased with non-U.S. currency are translated into US dollars at the exchange rate in effect at the time of purchase. Current assets and liabilities denominated in non-U.S. currency are translated into dollars at the exchange rate in effect at the date of the statement of financial position. Net transaction and translation gains and losses are included in the accompanying statements of activities and changes in net assets.

Family Health International

Notes to Financial Statements (continued)

1. Significant Accounting Policies (continued)

Operating and Non-operating Results

Operating support and revenue and operating expenses reflect the normal income and expense from receiving and using resources for program activities and support functions. Other non-operating changes in net assets reflect activities not central to FHI 360's mission.

Fair Value of Financial Instruments

FHI 360's financial instruments consist of cash and cash equivalents, restricted cash and short-term investments. Short-term investments held by third parties are recorded at their fair values. All other financial instruments are stated at cost which approximates fair value.

Unrestricted Net Assets

Unrestricted net assets represent funds that are not subject to donor-imposed stipulations and are fully available, at the discretion of management and the Board of Directors for FHI 360, to utilize in any of its programs or supporting services.

Temporarily Restricted Net Assets

Temporarily restricted net assets represent funds that are subject to donor-imposed stipulations and may or will be met either by actions and/or the passage of time. Expirations of temporarily restricted net assets are reported as reclassifications between the applicable classes of net assets.

Fair Value Measurements

Fair value is determined as the exchange price that would be received on the measurement date to sell an asset or the price paid to transfer a liability in the principal market or most advantageous market available to the entity in an orderly transaction between market participants. The fair value hierarchy ranks the inputs that are used to measure fair value into three levels, as follows:

- Level 1 – Quoted market prices for identical assets or liabilities to which an entity has access at the measurement date.

Family Health International

Notes to Financial Statements (continued)

1. Significant Accounting Policies (continued)

- Level 2 – Inputs and information other than quoted market indices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include:
 - Quoted prices for similar assets or liabilities in active markets;
 - Quoted prices for identical or similar assets in markets that are not active;
 - Observable inputs other than quoted prices for the asset or liability; and
 - Inputs derived principally from, or corroborated by, observable market data by correlation or by other means.
- Level 3 – Unobservable inputs for the asset or liability. Unobservable inputs should be used to measure fair value to the extent that observable inputs are not available.

Securities with fixed maturities (debt securities and certificates of deposit), other than U.S. Treasury securities, generally do not trade on a daily basis. The fair value estimates of such fixed maturity securities are based on observable market information rather than market quotes. Accordingly, the estimates of fair value for such fixed maturity securities are included in the debt securities amount disclosed in Level 2 hierarchy.

FHI 360 does not currently hold any Level 3 financial instruments.

Reclassifications

Certain items in the 2013 financial statements have been reclassified to conform to the 2014 financial statement presentation.

Family Health International

Notes to Financial Statements (continued)

1. Significant Accounting Policies (continued)

Impact of New Accounting Pronouncements

In 2013, FASB issued ASU 2013-06, *Not-for-Profit Entities (Topic 958): Services Received from Personnel of an Affiliate*. This ASU requires a recipient not-for-profit entity to recognize all services received from personnel of an affiliate that directly benefit the recipient not-for-profit entity. Those services should be measured at the cost recognized by the affiliate for the personnel providing those services. However, if measuring a service received from personnel of an affiliate at cost will significantly overstate or understate the value of the service received, the recipient not-for-profit entity may elect to recognize that service received at either (1) the cost recognized by the affiliate for the personnel providing that service or (2) the fair value of that service. ASU 2013-06 is effective for FHI 360 for the year ended September 30, 2015. Management does not believe the adoption 2013-06 will have a material impact on the financial statements.

In May 2014, the FASB issued new guidance related to *Revenue from Contracts with Customers*. This guidance supersedes the revenue recognition requirements in Accounting Standards Codification Topic 605, *Revenue Recognition*, and most industry-specific guidance throughout the Accounting Standards Codification. The guidance requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance also expands the footnote disclosure requirements around contracts with customers. An entity can either adopt retrospectively to each prior reporting period presented, or elect a modified retrospective approach with the cumulative effect of initially applying the update recognized at the date of initial application. The guidance will be effective for the FHI 360 in 2020. FHI 360 is currently evaluating the potential impact of the adoption of the guidance on FHI 360's financial statements.

Family Health International

Notes to Financial Statements (continued)

1. Significant Accounting Policies (continued)

Prior Period Financial Revision

During the preparation of the annual financial statements, management discovered an error in the calculation of the deferred rent liability in connection with operating leases related to FHI 360's office facility in Washington, DC. The error relates to prior periods and resulted in an overstatement of the deferred rent liability of \$9,922,166 at September 30, 2013, and an understatement of unrestricted net assets for the same amount. In accordance with ASC 250 *Accounting Changes and Error Corrections*, FHI 360 evaluated the materiality of this error on prior period financial statements and determined that it did not result in a material misstatement to the financial condition, results of operations, or liquidity for the period presented. FHI 360 also determined that the effect of recording this correction during 2014 would have been material to the financial statements. As a result, the 2013 financial statements have been revised to correct the error in accordance with ASC 250, as shown in the table below.

	As Reported	As Revised
Deferred rent liability	\$ 10,344,904	\$ 422,740
Unrestricted net assets	\$ 72,341,980	\$ 82,264,146

2. Accounts Receivable

Accounts receivable included the following at September 30:

	2014	2013
Accounts receivable	\$ 35,091,906	\$ 38,611,541
Unbilled accounts receivable	16,501,288	17,782,067
Employee advances	894,886	1,135,072
Allowance for doubtful accounts	(127,924)	(318,714)
	\$ 52,360,156	\$ 57,209,966

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Notes to Financial Statements (continued)

3. Short-Term Investments

The following is a summary of the fair value measurements of FHI 360's short-term investments within the fair value hierarchy at September 30:

	Fair Value			
	Level 1	Level 2	Level 3	Total
September 30, 2014				
Cash, bank deposit program, and money-market funds	\$ 11,980,707	\$ –	\$ –	\$ 11,980,707
Corporate fixed income	–	251,543	–	251,543
Total short-term investments	<u>\$ 11,980,707</u>	<u>\$ 251,543</u>	<u>\$ –</u>	<u>\$ 12,232,250</u>

	Fair Value			
	Level 1	Level 2	Level 3	Total
September 30, 2013				
Cash, bank deposit program, and money-market funds	\$ 17,487,817	\$ 138,218	\$ –	\$ 17,626,035
Corporate fixed income	–	250,955	–	250,955
Certificates of deposit	–	102,452	–	102,452
Total short-term investments	<u>\$ 17,487,817</u>	<u>\$ 491,625</u>	<u>\$ –</u>	<u>\$ 17,979,442</u>

Investments held by FHI 360 at September 30, consisted of the following:

	2014		2013	
	Cost	Fair Value	Cost	Fair Value
Cash, bank deposit program, and money-market funds	\$ 11,942,489	\$ 11,980,707	\$ 17,587,817	\$ 17,626,035
Corporate fixed income	250,000	251,543	250,000	250,955
Certificates of deposit	–	–	108,246	102,452
Total short-term investments	<u>\$ 12,192,489</u>	<u>\$ 12,232,250</u>	<u>\$ 17,946,063</u>	<u>\$ 17,979,442</u>

Investment income for the years ended September 30, 2014 and 2013 was \$86,716 and \$56,861, respectively, consisting of interest, dividends and net realized and unrealized gains.

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Notes to Financial Statements (continued)

4. Property and Equipment, net

Property and equipment, net include the following at September 30:

	2014	2013
Leasehold improvements	\$ 20,920,952	\$ 18,459,253
Vehicles, equipment, and software	10,816,069	11,577,030
Fine art inventory	665,909	665,909
Accumulated depreciation/amortization	(17,425,219)	(15,258,043)
Total property and equipment, net	<u>\$ 14,977,711</u>	<u>\$ 15,444,149</u>

Total depreciation expense for the years ended September 30, 2014 and 2013, was \$4,208,104 and \$4,986,110, respectively.

5. Accrued Expenses

In carrying out the activities under various contracts and grants awarded to FHI 360, FHI 360 utilizes sub-awardees to achieve the objectives of these agreements. As of September 30, 2014 and 2013, FHI 360 recorded accrued expenses in the amount of \$45,774,817 and \$24,878,041, respectively, in which payments due to the sub-awardees are included.

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Notes to Financial Statements (continued)

6. Notes Payable and Leases

The details concerning notes payable at September 30 are as follows:

	2014	2013
Note payable to Wells Fargo with interest at 1.75% payable monthly, due April, 2014	\$ —	\$ 5,000,000
Note payable to FHI Foundation with interest at daily LIBOR rate plus one hundred (100) basis points (1.00%), payable monthly	—	2,500,000
Short-term portion of capital lease due to e-Plus Group, Inc., with interest at 6.43% payable monthly, due June 1, 2018	610,916	346,984
Long-term portion of capital lease due to e-Plus Group, Inc., with interest at 6.43% payable monthly, due June 1, 2018	1,632,123	1,656,686
Line of credit with PNC Bank, due 2017	8,533,821	—
Total notes payable and capital leases	\$ 10,776,860	\$ 9,503,670

The aggregate amounts of principal maturities for the next five years are as follows:

Year	Amount
2015	\$ 610,916
2016	692,365
2017	9,109,051
2018	364,518
2019	—
	\$ 10,776,860

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Notes to Financial Statements (continued)

6. Notes Payable and Leases (continued)

FHI 360 rents its facilities, computers, and various equipment under rental agreements. Some leases contain escalation clauses. At September 30, 2014, future minimum lease payments under these non-cancelable operating leases are as follows:

2015	\$ 20,524,851
2016	19,211,258
2017	19,544,304
2018	19,937,043
2019	20,349,057
Thereafter	<u>161,166,643</u>
Total	<u>\$ 260,733,156</u>

Future minimum rental income under subleases is as follows:

2015	\$ 1,359,191
2016	1,358,813
2017	1,402,462
2018	1,363,564
2019	1,085,104
Thereafter	<u>2,061,118</u>
Total	<u>\$ 8,630,252</u>

Total occupancy expense for the years ended September 30, 2014 and 2013 was \$23,977,386 and \$28,080,786, respectively, which includes total rent expense of \$20,263,435 and \$22,422,727, respectively.

7. Pension Plans and Foreign Severance Liabilities

FHI 360 has a noncontributory, defined-contribution pension plan (the Plan) covering substantially all U.S. employees who have met certain eligibility requirements. Under the provisions of the Plan, FHI 360 contributes 12% of each employee's base compensation to various investment vehicles designated by the employee.

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Notes to Financial Statements (continued)

7. Pension Plans and Foreign Severance Liabilities (continued)

The employees' ownership in investments of the Plan vests at the rate of 20% per year of continuous service. For employees terminated before 100% vesting is achieved, unvested amounts are used to offset future contributions by FHI 360. Pension expense amounted to \$12,639,216 and \$12,113,812 for the years ended September 30, 2014 and 2013, respectively.

FHI 360 established an international pension plan for non-U.S. citizen expatriates. The plan is administered by AEGON/La Mondiale. Contribution and vesting provisions are consistent with the U.S. based Plan. Total payments for the years ended September 30, 2014 and 2013, were \$988,628 and \$814,339, respectively.

The accrued field office severance, leave, retirement balances, and related taxes withheld included the following at September 30:

	<u>2014</u>	<u>2013</u>
Field retirement	\$ 2,069,767	\$ 2,012,995
Field leave	3,072,894	3,241,451
Field severance	9,840,886	12,567,218
Taxes withheld	522,221	597,062
Total	<u>\$ 15,505,768</u>	<u>\$ 18,418,726</u>

FHI 360 accrues severance pay for Foreign Service Nationals (FSNs) in countries where the host country requires payment of severance pay upon separation. The accrual is based upon each FSN's years of service with FHI 360, and FHI 360 increases the severance accrual each year based on the additional year of service. The severance costs are charged to the federal award each year as the additional years of service are accrued. The severance payments are made whether the termination is voluntary or involuntary, with the exception of an employee being terminated with cause.

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Notes to Financial Statements (continued)

8. Medical Insurance

FHI 360 provides health care related benefits covering substantially all U.S. employees who have met certain eligibility requirements. Domestic employees have two options. They can elect coverage under FHI 360's self-funded plan or, as of January 1, 2012, they can participate in a high deductible health plan which provides individual health savings accounts. The self-insured plan includes a stop-loss policy which provides coverage for claims in excess of \$125,000 for each individual participant with a total cost payment cap to FHI 360 of 125% of all expected claims as projected by the insurer at the start of the plan year (January 1). Premiums for the self-insured plan are recorded as medical expenses with an offset to a medical claims liability account on a monthly basis. Expatriate employees are covered by a traditional premium based plan with Cigna International. Total expenses for health benefits were \$12,062,428 and \$10,610,235 for the years ended September 30, 2014 and 2013, respectively.

Estimated liabilities recorded for incidents incurred but not reported are \$843,000 and \$378,000 as of September 30, 2014 and 2013, respectively.

9. Direct Cost Sharing – U.S. Government Funded Agreements

FHI 360 has 37 various awards with remaining cost-sharing requirements as of September 30, 2014. FHI 360 enters into subawards with subrecipients who assist FHI 360 in meeting the goals and objectives of FHI 360's awards. When appropriate, FHI 360 includes a cost share requirement in subawards.

Subrecipients can meet a cost share requirement by donating materials, or by incurring costs in support of the project that are not reimbursed through the subaward. The costs incurred and the estimated fair value of the materials is reported on a quarterly basis. Cost share contributions may also come from other sources, including FHI 360 projects that are not funded by the U.S. government. FHI 360 continually monitors awards with cost sharing requirements to ensure compliance.

Family Health International

Notes to Financial Statements (continued)

9. Direct Cost Sharing-U.S. Government Funded Agreements (continued)

FHI 360 had total remaining cost share requirements of \$21,501,764 and \$11,151,178 at September 30, 2014 and 2013, respectively.

10. Related-Party Transactions

In December 1990, FHI 360 established a separate non-profit foundation, Family Health International Foundation (the Foundation), to support the work of FHI 360. Contributions to FHI 360 from the Foundation were \$1,000,000 and \$9,000,000 in 2014 and 2013, respectively. In addition, the Foundation loaned FHI 360 \$0 and \$5,000,000 during the year ended September 30, 2013. At September 30, 2014 and 2013, zero and \$2,500,000, respectively, related to this loan was outstanding. This loan amount is classified as a note payable by FHI 360.

FHI Solutions LLC (Solutions) is a single-member limited liability company of FHI 360. The mission of Solutions is to support activities and programs in the areas of education; health, population and nutrition; environment and agriculture; civil society and other areas of human development.

FHI 360 incorporated Achieving Health Nigeria Initiative (AHNI) under Nigerian law on June 23, 2009, as an organization affiliated with FHI 360. The services provided to FHI 360 by AHNI during fiscal years 2014 and 2013, totaled \$5,699,491 and \$2,269,131, respectively, under two sub-agreements, Strengthening Integrated Delivery of HIV/AIDS Services (SIDHAS) for \$2,745,381 and \$1,742,312, respectively, and National Agency for the Control of AIDS (NACA) Global Fund Phase I for \$2,954,110 and \$526,819, respectively.

FHI 360 incorporated Family Health International South Africa (FHISA) on March 20, 2007, under section 21 of the South Africa Companies Act, as a not-for-profit entity. FHI 360 operates through FHISA within South Africa as a Country and Regional Office. Revenues of FHISA were \$5,720,160 and \$3,003,610 for the year ended September 30, 2014 and 2013, respectively.

FHI 360 incorporated Family Health India (FHIndia) on March 10, 2008, under section 25 of the (India) Companies Act of 1956. FHIndia is intended to operate in India to supplement the activities of FHI 360's India Country Office.

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Notes to Financial Statements (continued)

10. Related-Party Transactions (continued)

During fiscal year 2014 and 2013, FHIndia received funding of \$12,633 and \$25,841, respectively, from the Avantha Foundation as part of the corporate social responsibility of a leading paper manufacturing company, Ballarpur Industries. FHIndia provided technical assistance to ensure continuum of care services to employees who were living with HIV in and around the factory in Chandrapur, Maharashtra state, India.

FHI 360 incorporated Gold Star Kenya on June 26, 2010, under section 10 of the Non-Governmental Organizations Co-ordination Act (Kenya). Gold Star Kenya is intended to operate in Kenya to supplement the activities of FHI's Kenya Country Office. The services provided by Gold Star Kenya during the year ended September 30, 2014 and 2013 totaled \$381,189 and \$1,085,307, respectively.

The accompanying financial statements present FHI 360 as a stand-alone organization and do not include the accounts of the Foundation, FHI Solutions, AHNI, FHISA, FHIndia, or Gold Star Kenya.

11. Contingencies

The ultimate determination of amounts received under contracts with governmental agencies is generally based upon allowable costs reported to and audited by the U.S. government. Until such audits have been completed and a final settlement reached, there exists a contingency to refund any amounts received in excess of allowable costs. Management believes that no material unrecorded loss will result from such audits.

12. Subsequent Events

Subsequent events have been evaluated for disclosure through June 30, 2015, the date FHI 360's financial statements as of and for the years ended September 30, 2014 and 2013, were available to be issued. There are no additional events that have occurred such that adjustments to the amounts presented or disclosed in the notes of the financial statements are warranted.

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