



MERCY SHIPS AND AFFILIATES

Consolidated and Combined
Financial Statements
With Independent Auditors' Report

December 31, 2020 and 2019

MERCY SHIPS AND AFFILIATES

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Mercy Ships and Affiliates
Lindale, Texas

Report on the Consolidated and Combined Financial Statements

We have audited the accompanying consolidated and combined financial statements of Mercy Ships and Affiliates, which comprise the consolidated and combined statement of financial position as of December 31, 2020, and the related consolidated and combined statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the consolidated and combined financial statements.

Management's Responsibility for the Consolidated and Combined Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated and combined financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated and 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 consolidated and 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 audits to obtain reasonable assurance about whether the consolidated and combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated and combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated and combined financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated and 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 consolidated and combined financial statements.

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

Board of Directors
Mercy Ships and Affiliates
Lindale, Texas

Opinion

In our opinion, the consolidated and combined financial statements referred to above present fairly, in all material respects, the consolidated and combined financial position of Mercy Ships and Affiliates as of December 31, 2020, and the consolidated and combined changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited Mercy Ships and Affiliates' 2019 consolidated and combined financial statements, and we expressed an unmodified audit opinion on those audited consolidated and combined financial statements in our report dated May 1, 2020. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2019, is consistent, in all material respects, with the audited consolidated and combined financial statements from which it has been derived.

Capin Crouse LLP

Grapevine, Texas
May 21, 2021

MERCY SHIPS AND AFFILIATES

Consolidated and Combined Statement of Financial Position

December 31, 2020

With Summarized Financial Information for December 31, 2019

	2020	2019
ASSETS:		
Cash and cash equivalents	\$ 91,820,308	\$ 67,881,570
Cash held for others—ship bank	1,142,291	1,503,354
Certificate of deposit	5,213,605	5,123,359
Investments	72,775,487	27,320,426
Pledges receivable—net	18,562,098	35,640,361
Other receivables	7,348,733	4,620,815
Inventory	6,801,880	5,497,362
Prepaid expenses and other assets	3,021,787	2,469,878
Cash and cash equivalents held for long-term purposes	3,838,600	32,030,561
Property and equipment—net	108,739,118	107,381,672
Total Assets	\$ 319,263,907	\$ 289,469,358
LIABILITIES AND NET ASSETS:		
Liabilities:		
Accounts payable and accrued expenses	\$ 7,660,544	\$ 8,064,380
Ship bank payable	1,150,408	1,212,645
Paycheck Protection Program loan	2,884,300	-
Other liabilities	2,125,543	2,200,896
	13,820,795	11,477,921
Net assets:		
Net assets without donor restrictions	192,519,678	152,893,244
Net assets with donor restrictions:		
Restricted by purpose or time	111,736,434	123,911,193
Restricted in perpetuity	1,187,000	1,187,000
	112,923,434	125,098,193
	305,443,112	277,991,437
Total Liabilities and Net Assets	\$ 319,263,907	\$ 289,469,358

See notes to consolidated and combined financial statements

MERCY SHIPS AND AFFILIATES

Consolidated and Combined Statement of Activities

For the Year Ended December 31, 2020
With Summarized Financial Information for the Year Ended December 31, 2019

	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	2020 Total	2019 Total
SUPPORT AND REVENUE:				
Contributions	\$ 63,219,051	\$ 36,291,377	\$ 99,510,428	\$ 104,844,059
Contributions for staff support	2,530,162	-	2,530,162	3,808,445
Gift-in-kind contributions	3,844,861	-	3,844,861	5,998,423
Contributed services	7,858,479	-	7,858,479	17,843,352
Fee revenue	354,119	-	354,119	1,596,723
Sales and other revenue	4,031,806	14,364	4,046,170	6,396,207
Gain (loss) from translation adjustments	1,902,264	-	1,902,264	(228,110)
Total Support and Revenue	83,740,742	36,305,741	\$ 120,046,483	140,259,099
NET ASSETS RELEASED:				
Purpose restrictions	48,480,500	(48,480,500)	-	-
EXPENSES:				
Program services:				
Ship and field operations	64,396,551	-	64,396,551	70,392,262
Supporting activities:				
General and administrative	9,671,469	-	9,671,469	8,673,004
Fundraising	21,158,118	-	21,158,118	20,376,612
	30,829,587	-	30,829,587	29,049,616
Total Expenses	95,226,138	-	95,226,138	99,441,878
Change in Net Assets Before Change in Cumulative Translation Adjustments	36,995,104	(12,174,759)	24,820,345	40,817,221
Cumulative Translation Adjustments	2,631,330	-	2,631,330	(754,047)
Change in Net Assets	39,626,434	(12,174,759)	27,451,675	40,063,174
Net Assets, Beginning of Year	152,893,244	125,098,193	277,991,437	237,928,263
Net Assets, End of Year	\$ 192,519,678	\$ 112,923,434	\$ 305,443,112	\$ 277,991,437

See notes to consolidated and combined financial statements

MERCY SHIPS AND AFFILIATES

Consolidated and Combined Statement of Functional Expenses

For the Year Ended December 31, 2020

	Program		Supporting Activities		Total Expenses
	Ship and Field Operations	General and Administrative	Fundraising	Fundraising	
Advertising and marketing	\$ 3,970,939	\$ 834,543	\$ 7,115,569	\$ 11,921,051	
Auto expense	124,443	11,749	16,504	152,696	
Conference, seminar, and trade shows	28,018	93,301	214,031	335,350	
Contract labor	7,247,546	1,183,565	1,934,245	10,365,356	
Contributed salary expense	7,858,479	-	-	7,858,479	
Cost of goods sold	105,135	17,924	2,692	125,751	
Depreciation	3,941,181	86,054	99,047	4,126,282	
Distributed inventory	5,552,901	204,750	67,414	5,825,065	
Dry docking and related expenses	2,222,475	-	-	2,222,475	
Food purchases	492,963	11,736	117	504,816	
Freight and customs	310,658	9,446	6,596	326,700	
Fuel and lube oil	687,758	13	38	687,809	
Gift expense—other charities	1,167,446	2,072	249,022	1,418,540	
Insurance	495,265	73,983	14,460	583,708	
Interest	21,756	27,311	83,402	132,469	
Legal and professional fees	395,611	86,862	150,431	632,904	
Meals and entertainment	71,878	10,329	11,909	94,116	
Miscellaneous	1,048,650	233,359	218,742	1,500,751	
Postage and printing	1,325,642	463,319	4,740,875	6,529,836	
Rents	711,586	130,284	552,177	1,394,047	
Repairs and maintenance	1,089,206	116,167	66,475	1,271,848	
Service charges	-	1,048,907	-	1,048,907	
Small equipment and furniture	4,013,229	82,272	21,556	4,117,057	
Staff support and expenses	16,338,088	4,483,022	5,066,134	25,887,244	
Supplies	2,314,934	243,256	204,259	2,762,449	
Taxes and fees	49,171	26,898	22,249	98,318	
Telecommunications	829,324	24,628	16,870	870,822	
Travel	1,229,697	116,488	245,774	1,591,959	
Utilities	752,572	49,231	37,530	839,333	
Total Expenses	\$ 64,396,551	\$ 9,671,469	\$ 21,158,118	\$ 95,226,138	

See notes to consolidated and combined financial statements

MERCY SHIPS AND AFFILIATES

Consolidated and Combined Statement of Functional Expenses

For the Year Ended December 31, 2019

	Program	Supporting Activities		Total Expenses
	Ship and Field Operations	General and Administrative	Fundraising	
Advertising and marketing	\$ 3,067,839	\$ 643,813	\$ 5,182,285	\$ 8,893,937
Auto expense	175,976	20,395	55,084	251,455
Conference, seminar, and trade shows	80,837	50,741	75,739	207,317
Contract labor	7,093,632	1,207,293	3,083,455	11,384,380
Contributed salary expense	17,406,923	109,516	326,913	17,843,352
Cost of goods sold	148,596	48,844	24,107	221,547
Depreciation	3,691,010	96,562	101,918	3,889,490
Distributed inventory	5,096,877	133,731	13,102	5,243,710
Dry docking and related expenses	3,447,065	-	-	3,447,065
Food purchases	962,248	23,588	931	986,767
Freight and customs	342,817	14,403	17,224	374,444
Fuel and lube oil	1,885,875	18	53	1,885,946
Gift expense—other charities	85,058	1,851	4,360	91,269
Insurance	486,595	69,181	19,854	575,630
Interest	29,148	40,801	53,673	123,622
Legal and professional fees	123,461	79,232	51,552	254,245
Meals and entertainment	263,661	16,833	49,426	329,920
Miscellaneous	1,239,535	133,526	154,799	1,527,860
Postage and printing	1,376,140	477,332	4,874,330	6,727,802
Rents	550,415	163,067	740,649	1,454,131
Repairs and maintenance	1,226,510	129,573	39,364	1,395,447
Service charges	-	810,226	-	810,226
Small equipment and furniture	1,410,233	129,342	23,727	1,563,302
Staff support and expenses	16,315,590	3,726,409	4,760,116	24,802,115
Supplies	1,198,453	133,929	95,552	1,427,934
Taxes and fees	47,507	25,376	11,938	84,821
Telecommunications	697,802	25,318	29,014	752,134
Travel	1,754,913	290,326	545,028	2,590,267
Utilities	187,546	71,778	42,419	301,743
Total Expenses	\$ 70,392,262	\$ 8,673,004	\$ 20,376,612	\$ 99,441,878

See notes to consolidated and combined financial statements

MERCY SHIPS AND AFFILIATES

Consolidated and Combined Statement of Cash Flows

For the Year Ended December 31, 2020
With Summarized Financial Information for the Year Ended December 31, 2019

	2020	2019
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 27,451,675	\$ 40,063,174
Adjustments to reconcile change in net assets to net cash provided (used) by operating activities:		
Depreciation	4,126,282	3,889,486
Unrealized gains on investments	(487,585)	(1,101,883)
Gain on sale of property and equipment	(121,245)	(25,000)
(Gain) loss from translation adjustments	(2,631,330)	754,047
Bad debt expense	-	823,884
Contributions received for long-term purposes	(1,313,644)	(38,637,625)
Changes in operating assets and liabilities:		
Other receivables	(2,727,918)	(2,963,271)
Inventory	(1,304,518)	(663,566)
Prepaid expenses and other assets	(551,909)	1,487,953
Accounts payable and accrued expenses	(403,836)	(728,467)
Ship bank payable	(62,237)	21,871
Other liabilities	(75,353)	268,519
Net Cash Provided by Operating Activities	<u>21,898,382</u>	<u>3,189,122</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments	(45,057,722)	(26,327,524)
Purchases of property and equipment	(5,448,747)	(7,949,459)
Net Cash Used by Investing Activities	<u>(50,506,469)</u>	<u>(34,276,983)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from contributions for long-term purposes	18,391,907	33,497,086
Proceeds from Paycheck Protection Program loan	2,884,300	-
Net Cash Provided by Financing Activities	<u>21,276,207</u>	<u>33,497,086</u>
Effect of Exchange Rate Changes on Cash	<u>2,717,594</u>	<u>(762,161)</u>
Change in Cash, Cash Equivalents and Cash Held for Long-term Purposes	(4,614,286)	1,647,064
Cash, Cash Equivalents and Cash Held for Long-term Purposes, Beginning of Year	<u>101,415,485</u>	<u>99,768,421</u>
Cash, Cash Equivalents and Cash Held for Long-term Purposes, End of Year	<u>\$ 96,801,199</u>	<u>\$ 101,415,485</u>

The following table provides a reconciliation of cash, cash equivalents, and cash held for long-term purposes:

	2020	2019
Cash and cash equivalents	\$ 91,820,308	\$ 67,881,570
Cash held for others—ship bank	1,142,291	1,503,354
Cash Held for Long-term Purposes	3,838,600	32,030,561
	<u>\$ 96,801,199</u>	<u>\$ 101,415,485</u>

See notes to consolidated and combined financial statements

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

1. NATURE OF ORGANIZATION:

Mercy Ships (the Organization) is a ship-based international health care organization that follows the 2000 year old model of Jesus, bringing hope and healing to the world's underserved poor by mobilizing people and resources worldwide. Through its hospital ship and related healthcare and capacity building programs and partnerships, the Organization provides surgical interventions, training and capacity building, and other healthcare services without regard to ethnicity, gender, political affiliation, or religious preference.

The financial statements are referred to as consolidated and combined financial statements on the cover page as well as the opinion. Consolidated and combined information is reflected in all other references to the following statements or items: financial statements, statements of financial position, statements of activities, statements of cash flows, and notes to financial statements. If any of these statements are not consolidated or combined, they will be identified accordingly. In addition, all references to Mercy Ships on these statements are a reflection of Mercy Ships and Affiliates, unless otherwise identified.

PRINCIPLES OF CONSOLIDATION

The accompanying financial statements include the accounts of Mercy Ships, Community of Faith, LLC, and Mercy Ships International, all Texas nonprofit corporations, and Africa Mercy-Malta Ltd., a Maltese maritime corporation. These affiliates are under common control as defined by accounting principles generally accepted in the United States of America and are consolidated in the financial statements.

PRINCIPLES OF COMBINATION

The accompanying financial statements also include the accounts of Mercy Ships Foundation, a Texas nonprofit, Mercy Ships Australia Ltd., an Australian non-profit limited by Guarantee, Mercy Ships Belgium VZW, a Belgium non-profit corporation, Mercy Ships Deutschland e.V., a German non-profit corporation, Stichting Mercy Ships Holland, a Netherlands charitable organization, Foundation Mercy Ships-Norge, a Norwegian non-profit corporation, Mercy Ships Sweden, a Fundraising Foundation, Association Mercy Ships, a Swiss non-profit Mercy Ships Global Association, a Swiss non-profit association and Mercy Ships-U.K. Ltd., a U.K. non-profit limited by Guarantee. All of these affiliates operate independently with their own separate boards of directors and work together collaboratively to achieve their respective charitable purposes. The Mercy Ships International board is a collaborative board that includes representatives from both the consolidated and combined affiliates. This board does not control any one affiliate but rather works collaboratively with them to ensure that their respective charitable programs are carried out in a consistent and coordinated manner with those of Mercy Ships International and one another, subject to the applicable laws of their originating jurisdictions. Due to lack of common board control, these affiliates are not consolidated with Mercy Ships International. However, given the collaborative nature of this structure, these affiliates are included in these financial statements on a combined basis.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

1. NATURE OF ORGANIZATION, continued:

The consolidated and combined affiliates (collectively, Mercy Ships) are part of the consolidated and combined financial statements. All material intercompany accounts and transactions have been eliminated in the consolidated and combined financial statements. The following affiliates have been excluded from the financial statements, due to immateriality: Mercy Ships Canada Society, a Canadian non-profit corporation, Mercy Ships Denmark, Mercy Ships France, Mercy Ships Korea, Mercy Ships New Zealand, Mercy Ships South Africa, and Mercy Ships Spain. Mercy Ships provides funds for and receives funds from the non-combined organizations. The related revenues from and expenditures with these organizations are netted in the statement of activities within sales and other revenue.

The consolidated affiliates of Mercy Ships are nonprofit religious organizations under Section 501(c)(3) of the Internal Revenue Code (the Code) and are publicly supported organizations under Sections 170(b)(1) and 509(a) of the Code. They are not considered to be private foundations under Section 509(a) of the Code.

The combined affiliates of Mercy Ships that are organized and operating outside of the United States are tax-exempt based on the various laws of the country in which they operate. These affiliates are generally not subject to any Federal or State income tax including any tax liabilities due to unrelated business income.

2. SIGNIFICANT ACCOUNTING POLICIES:

Mercy Ships maintains its accounts and prepares its consolidated and combined financial statements on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. The preparation of the consolidated and combined financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of any contingent assets and liabilities at the date of the consolidated and combined financial statements, and the reported revenues and expenses during the reporting periods. Actual results could differ from the estimates. The significant accounting policies followed are described below to enhance the usefulness of the consolidated and combined financial statements to the reader.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of checking and money market accounts. Mercy Ships considers all highly liquid investment instruments purchased with an original maturity of three months or less to be cash equivalents. At December 31, 2020 and 2019, Mercy Ship's cash balances exceeded federally insured limits by approximately \$55,000,000 and \$73,000,000, respectively. Mercy Ships purchased investments during the year ended December 31, 2020, to mitigate credit risk and does not believe the remaining cash balance to be at substantial risk of loss due to the lack of federal insurance coverage. Mercy Ships has not experienced any losses in such accounts.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

2. SIGNIFICANT ACCOUNTING POLICIES, continued:

CASH HELD FOR OTHERS—SHIP BANK

Mercy Ships maintains a bank on board its ship for the convenience of its crew members. The funds are shown separately on the consolidated and combined statements of financial position. Accordingly, a corresponding liability, ship bank payable, is recorded on the consolidated and combined statements of financial position.

CERTIFICATE OF DEPOSIT

Mercy Ships maintains a certificate of deposit with an original maturity date exceeding 90 days. The certificate is recorded at cost plus accrued interest.

INVESTMENTS

Mercy Ships' investment portfolio consists corporate bonds, which are carried at fair value. Gains and losses on investments are recorded in the statement of activities as increases in net assets without donor restrictions, unless their use is restricted by donor stipulation. Donated investments are recorded at fair value at the date of donation.

PLEDGES RECEIVABLE

Unconditional promises to give are reported as income to Mercy Ships when made and have been recorded at their pledged amounts. Subsequent to December 31, 2020, collections on pledges receivables totaled \$607,535.

INVENTORY

Inventory consists primarily of medical supplies, food, fuel, and lubricating oil. If purchased, these items are stated at the lower of cost or net realizable value on the first-in, first-out basis. If donated, items are valued at the lower of their estimated fair market values as of the date of receipt or current market value. As of December 31, 2020 and 2019, management determined no allowance for obsolete inventory was needed for the inventory on-hand.

PROPERTY AND EQUIPMENT—NET

Land, buildings, and equipment are stated at cost, or if donated, at fair value as of the date of the gift. Purchases or donations in excess of \$25,000 are capitalized with lesser amounts expensed. All capital assets, other than land, are depreciated using the straight-line method with useful lives ranging from 3-25 years. Assets not placed into service consist of capital expenditures for the new ship that are currently not being depreciated; however, will be depreciated based on the Organization's depreciation policy, once these assets are operable.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

2. SIGNIFICANT ACCOUNTING POLICIES, continued:

NET ASSETS

The following classes of net assets are maintained:

Net assets without donor restrictions include those currently available at the discretion of Mercy Ships' board of directors for use in its associated ministries and those resources invested in property and equipment, net of any related debt.

Net assets with donor restrictions include assets of Mercy Ships related to gifts with explicit donor-imposed restrictions that have not been met as to the specified purpose or to later periods of time or after specified dates. These include donor restrictions requiring that net assets be held in perpetuity, with use of all or part of the income earned on related investments for specific purposes.

The management of Mercy Ships has interpreted the Texas Uniform Prudent Management of Institutional Funds Act (TUPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Mercy Ships classifies as net assets with donor restrictions in perpetuity (a) the original value of the 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 remaining portion of the donor-restricted endowment fund that is not classified in net assets with donor restrictions in perpetuity is classified as net assets with donor restrictions until those amounts are appropriated for expenditure by Mercy Ships in a manner consistent with the standard prudence prescribed by TUPMIFA.

In accordance with TUPMIFA, Mercy Ships considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of Mercy Ships and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of Mercy Ships
7. The investment policies of Mercy Ships

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

2. SIGNIFICANT ACCOUNTING POLICIES, continued:

SUPPORT, REVENUE, AND EXPENSES

Contributions are recorded when made, which may be when cash or other assets are received or unconditionally promised. Mercy Ships reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or a purpose restriction is accomplished, the associated net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated and combined statements of activities as satisfaction of purpose restrictions. Support for Mercy Ships is primarily derived from contributions from individuals, church congregations, and corporations.

Mercy Ships receives various donated products such as medical and pharmaceutical supplies, and food to supply the ship. The products are donated primarily by corporations. The receipt of donated products by Mercy Ships is reflected as gift-in-kind contributions and the distribution is reflected as distributed inventory. The donated products are valued in a manner consistent with Association of Evangelical Relief and Development Organizations Interagency Gift-in-Kind Standards.

Of the \$3,844,861 and \$5,998,423 gift-in-kind contributions reflected in the consolidated and combined statements of activities for the years ended December 31, 2020 and 2019, respectively, 100% was used by Mercy Ships in its own programs in both years.

Contributed services are recognized if the services received require specialized skills or certifications that are provided by individuals possessing those skills and would typically need to be purchased if not provided by donation. The amount of contributed services recognized as support and expenses consisted of the following:

	December 31,	
	2020	2019
Program services—professional and medical	\$ 7,858,479	\$ 17,406,923
General and administrative support staff	-	109,516
Fundraising	-	326,913
	<u>\$ 7,858,479</u>	<u>\$ 17,843,352</u>

Mercy Ships also receives contributed services related to ship berthing within the ports. Due to such services not meeting the requirement for recording under GAAP, these contributed services are not included within the consolidated and combined statements of activities.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

2. SIGNIFICANT ACCOUNTING POLICIES, continued:

SUPPORT, REVENUE, AND EXPENSES, continued

Fee revenue, sales, and other revenue are recognized when earned. Fee revenue received in advance of the goods and services being provided, are recorded as deferred revenue. Expenses are reported when costs are incurred in accordance with the accrual basis of accounting.

ADVERTISING AND PROMOTIONAL COSTS

Advertising and promotional costs are expensed when they are incurred. Mercy Ships expended approximately \$11,940,000 and \$8,894,000 promoting its mission for the years ended December 31, 2020 and 2019, respectively.

ALLOCATION OF EXPENSES

Expenses are recorded when incurred in accordance with the accrual basis of accounting. The costs of providing various program services and supporting activities have been summarized on a functional basis in the consolidated and combined statements of activities. Accordingly, certain costs such as depreciation and salaries have been allocated among the program services and supporting activities benefited. The consolidated and combined statements of functional expenses report certain categories of expenses that are attributable to more than one program or supporting function. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated included depreciation expense and utilities that are based on square footage, as well as salaries and benefits which are allocated based on estimates of time and effort.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

3. LIQUIDITY AND FUNDS AVAILABLE:

The following table reflects Mercy Ship's financial assets as of December 31, 2020 and 2019, reduced by amounts not available for general expenditure within one year. Financial assets are considered unavailable when illiquid or not convertible to cash within one year, or because the governing board has set aside the funds for specific contingency reserves and projects or a long-term investment as board designated endowments.

	December 31,	
	2020	2019
Financial assets:		
Cash and cash equivalents	\$ 91,820,308	\$ 67,881,570
Cash held for others—ship bank	1,142,291	1,503,354
Investments	72,775,487	27,320,426
Certificate of deposit	5,213,605	5,123,359
Other receivables	7,348,733	4,620,815
Pledges receivable—net	18,562,098	35,640,361
Cash and cash equivalents held for long-term purposes	3,838,600	32,030,561
Financial assets, at year-end	<u>200,701,122</u>	<u>174,120,446</u>
Less those unavailable for general expenditure within one year:		
Funds restricted for capital projects	(78,790,825)	(73,296,501)
Cash held for others—ship bank	(1,142,291)	(1,503,354)
Pledges receivable, expected to be collected in more than one year	(2,673,025)	(7,518,152)
Pledges receivable, restricted for capital projects	(17,170,165)	(28,122,209)
Donor restricted endowment	(1,187,000)	(1,187,000)
Unappropriated endowment income	(91,725)	(77,361)
Unavailable	<u>(101,055,031)</u>	<u>(111,704,577)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>\$ 99,646,091</u>	<u>\$ 62,415,869</u>

As part of the Mercy Ships' liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. Mercy Ships has two lines of credit with financial institutions, both in the amount of \$5,000,000, maturing June 30, 2021 and November 23, 2021, respectively. To date, Mercy Ships has not made any draws on the line of credits. These funds could be used to fund operations if required.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

4. PLEDGES RECEIVABLE—NET:

Pledges receivable—net, consist of:

	December 31,	
	2020	2019
Due in less than one year	\$ 18,092,285	\$ 28,122,209
Due in one to five years	1,571,419	9,003,272
	19,663,704	37,125,481
Less: present value discount	(108,864)	(236,190)
Less: allowance for uncollectible promises	(992,742)	(1,248,930)
	<u>\$ 18,562,098</u>	<u>\$ 35,640,361</u>

During the years ended December 31, 2020 and 2019, Mercy Ships received new pledges receivable of \$0 and \$23,794,323, respectively; approximately \$0 and \$415,000, respectively, of these pledges being from board members, and received payments of \$15,358,767 and \$19,249,305, respectively, toward these pledges. Mercy Ships accounts for the present value of pledges receivable using a risk-adjusted discount rate range of 0.5-1.5%. An allowance for uncollectible pledges receivable is recorded based upon collection history.

5. INVENTORY:

Inventory consists of the following:

	December 31,	
	2020	2019
Medical supplies	\$ 5,873,319	\$ 4,792,424
Fuel	63,720	223,164
Food	255,462	132,598
Other	609,378	349,176
	<u>\$ 6,801,880</u>	<u>\$ 5,497,362</u>

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

6. PROPERTY AND EQUIPMENT–NET:

Property and equipment consists of:

	December 31,	
	2020	2019
Land and buildings	\$ 12,361,801	\$ 11,615,963
Ship and related improvements	68,242,854	67,738,349
Tools and equipment	4,023,600	3,641,318
Vehicles	1,584,524	1,390,610
Medical equipment	4,626,053	4,359,563
	<u>90,838,832</u>	<u>88,745,803</u>
Less accumulated depreciation	<u>(56,641,651)</u>	<u>(52,218,604)</u>
	34,197,181	36,527,199
Assets not placed into service	<u>74,541,937</u>	<u>70,854,473</u>
Property and equipment–net	<u>\$ 108,739,118</u>	<u>\$ 107,381,672</u>

Assets not placed into service is related to the construction and equipping of the Global Mercy, a second hospital ship. Estimated future payments for the Global Mercy's completion is approximately \$97,000,000. Completion is expected to occur by March 2022. These costs will be considered incurred and capitalized accordingly when construction is completed, Mercy Ships accepts the vessel, and is contractually obligated to pay the remaining costs.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

7. DISCLOSURE OF FAIR VALUE MEASUREMENTS:

The disclosure of the estimated fair value of financial investments at December 31, 2020 and 2019, is made in accordance with the requirements of the *Fair Value Measurements and Disclosure* topic of the FASB Accounting Standards Codification. Mercy Ships' investments consist of corporate bonds. The fair value of these financial instruments is based on yields currently available on comparable securities of issuers with similar credit ratings.

Mercy Ships uses appropriate valuation techniques to determine fair value based on inputs available. When available, Mercy Ships measures fair value using Level 1 inputs because they generally provide the most reliable evidence of fair value. Level 1 inputs indicate there is a quoted market price available for identical assets. Level 2 inputs indicate there are market prices available for similar assets. Level 3 inputs are only used when Level 1 or Level 2 inputs are not available and indicate there are not readily available market prices. Fair value of assets measured on a recurring basis are as follows:

As of December 31, 2020 and 2019, Mercy Ships had \$72,775,487 and \$27,230,426, respectively, of investments and all investments are valued using Level 2 inputs.

Investment income consist of:

	Year Ended December 31,	
	2020	2019
Unrealized gains	\$ 487,585	\$ 1,101,883
Investment income	44,194	24,455
	<u>\$ 531,779</u>	<u>\$ 1,126,338</u>

8. PAYCHECK PROTECTION PROGRAM LOAN:

As part of the response to the impact of COVID-19, Mercy Ships applied for a Paycheck Protection Program (PPP) Loan, administered by the Small Business Administration (SBA), under the Coronavirus Aid, Relief, and Economic Security (CARES) Act, which was signed into law in March 2020. Mercy Ships was approved for a loan in the amount of \$2,884,300 on April 29, 2020. The PPP loan provides for potential loan forgiveness up to the full amount of the loan provided Mercy Ships overcomes (meets) certain loan stipulations. If the loan is not forgiven, it bears annual interest of 1% and repayment is due in full on April 29, 2022.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

9. NET ASSETS WITHOUT DONOR RESTRICTIONS:

Net assets without donor restrictions consist of:

	December 31,	
	2020	2019
Available for operations	\$ 64,854,827	\$ 41,914,345
Equity in property and equipment–net	106,620,681	105,465,409
Equity in inventory–net	6,801,880	5,497,362
Board designated operating reserve	14,225,000	-
Quasi endowments	17,290	16,128
	<u>\$ 192,519,678</u>	<u>\$ 152,893,244</u>

10. NET ASSETS WITH DONOR RESTRICTIONS BY PURPOSE OR TIME:

Net assets with donor restrictions by purpose or time consist of:

	December 31,	
	2020	2019
Capital project–new ship:		
Funds received, not spent	\$ 78,790,825	\$ 73,296,501
Pledges made, not received	19,843,190	35,640,361
	98,634,015	108,936,862
M/V Africa Mercy	1,672,140	4,366,785
Maxillofacial/plastic surgery projects	2,125,952	1,527,216
Mercy vision projects	2,118,385	2,083,306
Orthopedic projects	1,031,371	1,256,278
Women’s health projects	1,518,340	1,261,169
Non-surgical projects	159,558	895,284
General surgery projects	3,814,787	3,096,943
Dental projects	564,582	404,993
Other ministry projects (including unappropriated endowment income)	97,304	82,357
	<u>\$ 111,736,434</u>	<u>\$ 123,911,193</u>

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

11. ENDOWMENT FUNDS AND RELATED ASSETS:

Assets held for endowment funds consist of:

	December 31,	
	2020	2019
Cash and cash equivalents	\$ 1,296,015	\$ 1,280,489

Net assets with donor restrictions in perpetuity consist of:

	December 31,	
	2020	2019
Crew assistance fund	\$ 107,000	\$ 107,000
Operations	80,000	80,000
Technical training	1,000,000	1,000,000
	<u>\$ 1,187,000</u>	<u>\$ 1,187,000</u>

The endowment net asset composition by type of fund as of December 31, 2020:

	Without donor restrictions	With donor restrictions		Total
		gains (losses) and other	Original gift amount	
Donor restricted endowment funds	\$ -	\$ 91,725	\$ 1,187,000	\$ 1,278,725
Board-designated endowment funds	17,290	-	-	17,290
	<u>\$ 17,290</u>	<u>\$ 91,725</u>	<u>\$ 1,187,000</u>	<u>\$ 1,296,015</u>

Changes in endowment net assets for the year ended December 31, 2020:

	Without donor restrictions	With donor restrictions		Total
		gains (losses) and other	Original gift amount	
Endowment net assets, beginning of year	\$ 16,128	\$ 77,361	\$ 1,187,000	\$ 1,280,489
Investment income	1,162	14,364		15,526
Endowment net assets, end of year	<u>\$ 17,290</u>	<u>\$ 91,725</u>	<u>\$ 1,187,000</u>	<u>\$ 1,296,015</u>

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

11. ENDOWMENT FUNDS AND RELATED ASSETS, continued:

The endowment net asset composition by type of fund as of December 31, 2019:

	Without donor restrictions	With donor restrictions		Total
		gains (losses) and other	Original gift amount	
Donor restricted endowment funds	\$ -	\$ 77,361	\$ 1,187,000	\$ 1,264,361
Board-designated endowment funds	16,128	-	-	16,128
	<u>\$ 16,128</u>	<u>\$ 77,361</u>	<u>\$ 1,187,000</u>	<u>\$ 1,280,489</u>

Changes in endowment net assets for the year ended December 31, 2019:

	Without donor restrictions	With donor restrictions		Total
		gains (losses) and other	Original gift amount	
Endowment net assets, beginning of year	\$ 15,154	\$ 47,857	\$ 1,187,000	\$ 1,250,011
Investment income	974	29,504	-	30,478
Endowment net assets, end of year	<u>\$ 16,128</u>	<u>\$ 77,361</u>	<u>\$ 1,187,000</u>	<u>\$ 1,280,489</u>

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or TUPMIFA requires Mercy Ships to retain as a fund of perpetual duration. In accordance with accounting principles generally accepted in the United States of America, deficiencies of this nature are reported in net assets without donor restrictions. As of December 31, 2020 and 2019, there are no deficiencies resulting from unfavorable market fluctuations, respectively.

12. DEFINED CONTRIBUTION PENSION PLAN:

Mercy Ships provides a 403(b) defined contribution retirement plan to eligible employees. As of April 1 2019, all full-time employees were eligible to participate on the first day of the month following their hire date. Eligible employees can contribute toward tax sheltered and/or Roth elections up to the maximum allowed by the IRS for the plan year. In 2019, Mercy Ships began matching 100% of employee contributions to the plan up to 3% of employee's gross annual wage. Employer matching contributions as of December 31, 2020 and 2019, were approximately \$240,000 and \$180,000, respectively.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

13. TRANSFERS FROM AFFILIATES:

Mercy Ships' international affiliates are certified by various charity boards within their countries. To satisfy requirements of these boards, the following information is presented for the purpose of disclosing the amount of funds transferred from each affiliate and disbursed to pay for program and ship operational expenses and long-term liabilities of Mercy Ships. These amounts are considered intercompany transactions for the purposes of the consolidated and combined financial statements and are therefore eliminated upon combination.

The amount of funds transferred from the affiliates was as follows:

	Grants - Accrual Basis		Grants - Cash Basis	
	2020	2019	2020	2019
Australia	\$ 2,866,927	\$ 1,616,359	\$ 1,616,359	\$ -
Belgium	4,730,199	2,618,788	3,953,471	2,477,970
Germany	1,764,392	1,760,302	1,764,392	1,760,302
Holland	4,499,273	4,053,171	4,881,916	4,803,631
Norway*	1,218,584	3,292,727	2,409,931	2,166,578
Sweden	2,656,830	1,855,065	2,328,624	1,855,065
Switzerland	9,059,685	7,611,697	8,194,954	8,082,223
United Kingdom	6,833,812	5,028,394	6,697,217	5,456,249
	<u>\$ 33,629,701</u>	<u>\$ 27,836,503</u>	<u>\$ 31,846,865</u>	<u>\$ 26,602,017</u>

*Includes funds donated by Norad.

MERCY SHIPS AND AFFILIATES

Notes to Consolidated and Combined Financial Statements

December 31, 2020

December 31, 2019 (Summarized Financial Information)

14. NON-U.S. OPERATIONS:

Mercy Ships' international affiliates are located in various countries. Non-U.S. operations are subject to risks inherent in operating under different legal systems and various political and economic environments. Among the risks are changes in existing tax laws, possible limitations on non-U.S. investment and income repatriation, government price or non-U.S. exchange controls, and restrictions on currency exchange. For the years ended December 31, 2020 and 2019, net assets of non-U.S. operations were 6.2% and 5.8% of Mercy Ships' total net assets, respectively.

Most of Mercy Ships' international affiliates use the local currency as the functional currency. The consolidated and combined financial statements of Mercy Ships' international affiliates have been translated into U.S. dollars. The consolidated and combined statements of financial position accounts have been translated using the exchange rate in effect at the consolidated and combined statements of financial position date. Consolidated and combined statements of activities amounts have been translated using the average exchange rate for the year. These adjustments for the years ended December 31, 2020 and 2019, are reflected accordingly on the consolidated and combined statements of activities.

As of the report date, there continues to be fluctuations in the value of the U.S. dollar relative to several non-U.S. currencies in which Mercy Ships operates. It is not practicable to determine the effects of these rate changes on Mercy Ships' consolidated and combined financial statements.

15. COMMITMENTS AND CONTINGENCIES:

In January 2020, the World Health Organization has declared the outbreak of a novel coronavirus as a "Public Health Emergency of International Concern," ultimately classifying the resulting COVID-19 as a pandemic. Federal, state and local governments have mandated various restrictions, including travel restrictions, restrictions on public gatherings, stay at home advisories, and quarantining of people who may have been exposed to the virus.

In reaction to the COVID-19 pandemic, Mercy Ships ceased ship based activities due to the risk posed by the virus for patients and crew. This resulted in a reduced programmatic spending in 2020. Aside from ship activities ceasing, Mercy Ships remained active in 12 African countries through land based projects with strategic partners. These activities included, but were not limited to, direct medical services, medical capacity building, infrastructure improvements, and donations of PPE. Management plans for these activities to continue throughout 2021. Mercy Ships International board has resolved that the African Mercy vessel will return to African field service in January 2022. In addition, the inaugural field service of the Global Mercy is also expected in 2022.

16. SUBSEQUENT EVENTS:

Subsequent events have been evaluated through May 21, 2021, which represents the date the consolidated and combined financial statements were available to be issued. Subsequent events after that date have not been evaluated.

SUPPLEMENTAL INFORMATION

**INDEPENDENT AUDITORS' REPORT
ON SUPPLEMENTARY INFORMATION**

Board of Directors
Mercy Ships and Affiliates
Lindale, Texas

We have audited the consolidated and combined financial statements of Mercy Ships and Affiliates, as of and for the years ended December 31, 2020 and 2019, and our report thereon dated May 21, 2021, which expressed an unmodified opinion on those consolidated and combined financial statements, appears on pages 1 and 2. Our audit was conducted for the purpose of forming an opinion on the consolidated and combined financial statements as a whole. The consolidating and combining statements of financial position and activities are presented for purposes of additional analysis of the consolidated and combined financial statements rather than to present the financial position and results of operations of the individual organizations, and it is not a required part of the consolidated and combined 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 and combined financial statements. The consolidating and combining information has been subjected to the auditing procedures applied in the audit of the consolidated and combined 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 and combined financial statements or to the consolidated and combined 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 and combined financial statements as a whole.

Capin Crouse LLP

Grapevine, Texas
May 21, 2021

MERCY SHIPS AND AFFILIATES

Consolidating and Combining Statement of Financial Position

December 31, 2020

	Mercy Ships	Mercy Ships Foundation	Mercy Ships International	Africa Mercy- Malta Ltd.	Mercy Ships National Offices	Eliminations	Total
ASSETS:							
Cash and cash equivalents	\$ 64,797,006	\$ 5,594,337	\$ 20,178	\$ -	\$ 25,247,387	\$ -	\$ 95,658,908
Cash held for others—ship bank	1,142,291	-	-	-	-	-	1,142,291
Certificate of deposit	5,213,605	-	-	-	-	-	5,213,605
Investments	-	72,775,487	-	-	-	-	72,775,487
Pledges receivable—net	91,399	18,770,699	-	-	-	(300,000)	18,562,098
Other receivables	12,663,738	-	-	-	2,581,391	(7,896,396)	7,348,733
Inventory	6,791,617	-	-	-	10,263	-	6,801,880
Prepaid expenses and other assets	3,106,933	-	-	-	493,344	(578,490)	3,021,787
Property and equipment—net	77,544,417	2,879,138	-	25,541,017	2,774,546	-	108,739,118
Total Assets	\$ 171,351,006	\$ 100,019,661	\$ 20,178	\$ 25,541,017	\$ 31,106,931	\$ (8,774,886)	\$ 319,263,907
LIABILITIES AND NET ASSETS:							
Liabilities:							
Accounts payable and accrued expenses	\$ 3,990,213	\$ 626,010	\$ -	\$ -	\$ 9,966,948	\$ (6,922,627)	\$ 7,660,544
Ship bank payable	1,150,408	-	-	-	-	-	1,150,408
Intercompany payable	-	-	11,462	962,307	-	(973,769)	-
Paycheck Protection Program Loan	2,884,300	-	-	-	-	-	2,884,300
Other liabilities	6,053	-	-	-	2,119,490	-	2,125,543
	<u>8,030,974</u>	<u>626,010</u>	<u>11,462</u>	<u>962,307</u>	<u>12,086,438</u>	<u>(7,896,396)</u>	<u>13,820,795</u>
Net Assets:							
Net assets without donor restrictions	144,481,353	5,308,896	8,716	24,578,710	19,020,493	(878,490)	192,519,678
Net asset with donor restrictions	18,838,679	94,084,755	-	-	-	-	112,923,434
	<u>163,320,032</u>	<u>99,393,651</u>	<u>8,716</u>	<u>24,578,710</u>	<u>19,020,493</u>	<u>(878,490)</u>	<u>305,443,112</u>
Total Liabilities and Net Assets	\$ 171,351,006	\$ 100,019,661	\$ 20,178	\$ 25,541,017	\$ 31,106,931	\$ (8,774,886)	\$ 319,263,907

MERCY SHIPS AND AFFILIATES

Consolidating and Combining Statement of Activities

Year Ended December 31, 2020

	Mercy Ships	Mercy Ships Foundation	Mercy Ships International	Africa Mercy- Malta Ltd.	Mercy Ships National Offices	Eliminations	Total
SUPPORT AND REVENUE:							
Contributions	\$ 53,715,798	\$ 987,129	\$ -	\$ -	\$ 44,807,501	\$ -	\$ 99,510,428
Contributions for staff support	1,802,735	-	-	-	727,427	-	2,530,162
Gift-in-kind contributions	2,783,030	-	-	-	1,061,831	-	3,844,861
Contributed services	7,858,479	-	-	-	-	-	7,858,479
Fee revenue	354,119	-	-	-	-	-	354,119
Sales and other revenue	1,058,885	1,998,730	85	-	1,168,470	(180,000)	4,046,170
Gain from translation adjustments	585,230	-	-	-	1,317,034	-	1,902,264
Grant revenue	51,092,971	10,260,984	-	-	158,718	(61,512,673)	-
Total Support and Revenue	119,251,247	13,246,843	85	-	49,240,981	(61,692,673)	120,046,483
EXPENSES:							
Non-grant expenses	76,977,216	845,155	2,400	2,673,987	14,907,380	(180,000)	95,226,138
Grant expenses	10,260,984	16,953,467	-	-	34,298,222	(61,512,673)	-
Total Expenses	87,238,200	17,798,622	2,400	2,673,987	49,205,602	(61,692,673)	95,226,138
Change in Net Assets Before Change in Cumulative Translation Adjustments	32,013,047	(4,551,779)	(2,315)	(2,673,987)	35,379	-	24,820,345
Cumulative Translation Adjustments	-	-	-	-	2,631,330	-	2,631,330
Change in Net Assets	32,013,047	(4,551,779)	(2,315)	(2,673,987)	2,666,709	-	27,451,675
Net Assets, Beginning of Year	131,306,985	103,945,430	11,031	27,252,697	16,353,784	(878,490)	277,991,437
Net Assets, End of Year	\$ 163,320,032	\$ 99,393,651	\$ 8,716	\$ 24,578,710	\$ 19,020,493	\$ (878,490)	\$ 305,443,112