



Audited Financial Statements

December 31, 2017

Independent Auditor's Report

To the Board of Directors of
Pencil, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of Pencil, Inc. which comprise the statement of financial position as of December 31, 2017, and the related statements of activities, functional expenses, and cash flows for the year 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 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 financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

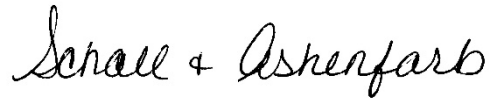
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about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

An audit involves performing procedures to obtain audit 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 organization'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 organization'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 Pencil, Inc. as of December 31, 2017, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.



Schall & Ashenfarb
Certified Public Accountants, LLC

March 5, 2018

PENCIL, INC.
STATEMENT OF FINANCIAL POSITION
AT DECEMBER 31, 2017

Assets

Cash and cash equivalents	\$534,994
Investments (Note 3)	1,237,170
Government grants receivable	3,318
Pledges receivable	309,970
Prepaid expenses and other assets	3,404
Security deposit	42,667
Fixed assets, net (Note 4)	<u>42,521</u>
 Total assets	 <u><u>\$2,174,044</u></u>

Liabilities and Net Assets

Liabilities:	
Accounts payable and accrued expenses	\$22,635
Grants payable	20,000
Deferred rent	<u>28,393</u>
Total liabilities	<u>71,028</u>
Net assets:	
Unrestricted	1,708,516
Temporarily restricted (Note 5)	<u>394,500</u>
Total net assets	<u>2,103,016</u>
 Total liabilities and net assets	 <u><u>\$2,174,044</u></u>

The attached notes and auditor's report are an integral part of these financial statements.

PENCIL, INC.
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2017

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Public support and revenue:			
Contributions	\$757,235	\$416,200	\$1,173,435
Government grants	545,000		545,000
Special events (net of expenses with a direct benefit to donor) (Note 6)	1,121,650		1,121,650
In-kind contributions (Note 7)	220,947		220,947
Interest and other income	16,782		16,782
Net assets released from restrictions	613,200	(613,200)	0
Total public support and revenue	<u>3,274,814</u>	<u>(197,000)</u>	<u>3,077,814</u>
Expenses:			
Program services	<u>2,047,028</u>		<u>2,047,028</u>
Supporting services:			
Management and general	314,912		314,912
Fundraising	<u>742,799</u>		<u>742,799</u>
Total supporting services	<u>1,057,711</u>	0	<u>1,057,711</u>
Total expenses	<u>3,104,739</u>	<u>0</u>	<u>3,104,739</u>
Change in net assets from operating activities	<u>170,075</u>	<u>(197,000)</u>	<u>(26,925)</u>
Non-operating activities:			
Loss on sale of investments	(359)		(359)
Unrealized loss on investments	<u>(11,991)</u>		<u>(11,991)</u>
Total non-operating activities	<u>(12,350)</u>	<u>0</u>	<u>(12,350)</u>
Change in net assets	157,725	(197,000)	(39,275)
Net assets - beginning of year	<u>1,550,791</u>	<u>591,500</u>	<u>2,142,291</u>
Net assets - end of year	<u><u>\$1,708,516</u></u>	<u><u>\$394,500</u></u>	<u><u>\$2,103,016</u></u>

The attached notes and auditor's report are an integral part of these financial statements.

PENCIL, INC.
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED DECEMBER 31, 2017

	Supporting Services			Total Supporting Services	Total Expenses
	Program Services	Management and General	Fundraising		
Salaries	\$1,157,402	\$121,308	\$351,056	\$472,364	\$1,629,766
Payroll taxes and benefits	288,472	28,838	83,455	112,293	400,765
Occupancy	226,908	23,782	68,824	92,606	319,514
Program supplies and material	1,881			0	1,881
Office supplies and postage	4,523	474	1,372	1,846	6,369
Travel, training and meetings (including in-kind)(Note 7)	89,111	8,860		8,860	97,971
Telephone and information technology	60,929	6,386	18,480	24,866	85,795
Equipment	24,517	2,570	7,436	10,006	34,523
Depreciation	41,794	4,380	12,677	17,057	58,851
Professional fees (including in-kind)(Note 7)		77,347		77,347	77,347
Consulting (including in-kind)(Note 7)	115,914	30,076	63,051	93,127	209,041
Staff recruiting		1,395		1,395	1,395
Insurance	16,668	1,746	5,056	6,802	23,470
Bank charges and admin fees	11,108	1,165	3,369	4,534	15,642
Indirect special events			125,657	125,657	125,657
Miscellaneous	7,801	6,585	2,366	8,951	16,752
Total expenses	\$2,047,028	\$314,912	\$742,799	\$1,057,711	\$3,104,739

The attached notes and auditor's report are an integral part of these financial statements.

PENCIL, INC.
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2017

Cash flows from operating activities:	
Change in net assets	(\$39,275)
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Loss on sale of investments	359
Unrealized loss on investments	11,991
Depreciation	58,851
Changes in assets and liabilities:	
Government grants receivable	431,682
Pledges receivable	155,911
Prepaid expenses and other assets	21,691
Security deposit	304
Accounts payable and accrued expenses	(13,529)
Grants payable	(10,300)
Deferred rent	(45,175)
Net cash flows provided by operating activities	<u>572,510</u>
Cash flows from investing activities:	
Proceeds from the sale of investments	77,000
Purchase of investments	(349,752)
Transfers from investment account	50,000
Purchases of fixed assets	(7,222)
Net cash flows used for investing activities	<u>(229,974)</u>
Net increase in cash and cash equivalents	342,536
Cash and cash equivalents - beginning of year	<u>192,458</u>
Cash and cash equivalents - end of year	<u><u>\$534,994</u></u>
Supplemental information:	
Interest and taxes paid	<u><u>\$0</u></u>

The attached notes and auditor's report are an integral part of these financial statements.

PENCIL, INC.
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2017

Note 1 - Organization

Pencil, Inc. ("Pencil") was founded in 1995 to develop and coordinate meaningful corporate and community involvement in New York City public education. These financial statements do not reflect programs created by Pencil, Inc. or the contributions raised for those programs as they are run directly by the New York City schools. Pencil, Inc. derives its revenue from soliciting contributions from the general public in New York City, and from the annual fundraising event.

Pencil was incorporated in the State of New York and has been notified by the Internal Revenue Service that it is exempt from Federal income tax under Section 501(c)(3) of the Internal Revenue Code and has not been determined to be a private foundation as defined in Section 509(a).

Note 2 - Summary of Significant Accounting Policies

a. Basis of Accounting

The financial statements have been prepared on the accrual basis of accounting which is the process of recording revenue and expenses when earned or incurred, rather than when received or paid.

b. Basis of Presentation and Revenue Recognition Principles

Pencil reports information regarding their financial position and activities in the following classes of net assets:

- *Unrestricted* – represents all activity without donor-imposed restrictions as well as activity with donor-imposed restrictions, which expire within the same period.
- *Temporarily restricted* – relates to contributions of cash and other assets with donor stipulations that make clear the assets restriction, either due to a program nature or by passage of time.

c. Recognition of Income

Contributions are reported as an increase in unrestricted net assets, unless they contain a restriction by the donor for a specific program or time period. 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. However, if a restriction is satisfied in the period the contribution has been made, it is recorded as unrestricted

Contributions of non-cash assets are recorded at fair value.

Government grants are recorded as revenue when earned based on incurring expenses that are reimbursable under the terms of the grant. The difference between cash received and revenue earned is reflected as government grants receivable or refundable advances.

d. Cash and Cash Equivalents

Cash and cash equivalents include cash held in checking accounts and money market funds, but exclude cash held as part of the investment portfolio.

e. Concentration of Credit Risk

Financial instruments which potentially subject Pencil to concentration of credit risk consist of cash, money market accounts and investment securities which are placed with financial institutions that management deems to be creditworthy. The market value of investments is subject to market fluctuations.

Management believes that the investment policy is prudent for the long-term welfare of Pencil. At year end and at certain times during the year, a significant portion of the funds were in excess of federally insured levels; however, Pencil has not experienced any losses from these accounts due to failure of any financial institution.

f. Pledges Receivable

Pencil records unconditional promises to give in the period pledged at net realizable value if due in less than one year. Long-term pledges are recorded at fair value based on a risk adjusted discount rate, when material. At December 31, 2017, all pledges receivable are expected to be received in less than one year.

Conditional contributions are recognized when the conditions on which they depend are substantially met.

All receivables are assessed for collectability. Based on a review of several factors, including the credit worthiness of the donor and historical experience, no allowance for doubtful accounts has been established.

g. Investments

Investments are recorded at fair value, which refers to the price that would be received to sell an asset or paid to transfer a liability (i.e. "exit price") in an orderly transaction between market participants at the measurement date. Realized and unrealized gains and losses are recognized in the statement of activities.

h. Fixed Assets

Purchases of furniture, equipment, and leasehold improvements that have a useful life of greater than one year are capitalized at cost or, if donated, at their fair value at the date of the gift. Property and equipment is depreciated using the straight-line method over the estimated useful life of the asset.

i. Grants Payable

Pencil received contributions where the donor specifies a particular school as the ultimate beneficiary. Those donations are treated as agency transactions and recorded advances until they are paid out.

- j. Deferred Rent
Pencil records rent expense on the straight-line method and recognizes deferred rent for the cumulative amount that expenses exceed actual payments. In latter stages of the lease, deferred rent will be reduced as the amount of payments exceeds the expense recorded.
- k. In-Kind Contributions
Donated services are recognized in circumstances where those services create or enhance non-financial assets or require specialized skills, are provided by individuals possessing those skills and would typically need to be purchased if not provided in-kind. Donated materials are recorded at the estimated fair value at the date of donation (See Note 7).
- Board members and other individuals volunteer their time and perform a variety of tasks that assist Pencil. These services have not been recorded in the financial statements, as they do not meet the criteria outlined above.
- l. Advertising
The cost of advertising is expensed as incurred.
- m. Management Estimates
The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from those estimates.
- n. Expense Allocation
The costs of providing various programs and other activities have been summarized on a functional basis in the financial statements. Accordingly, certain costs have been allocated among the programs and supporting services benefited. Management and general expenses include those expenses that are not directly identifiable with any other specific function but provide for the overall support and direction of Pencil.
- o. Accounting for Uncertainty of Income Taxes
Pencil does not believe its financial statements include any material, uncertain tax positions. Tax filings for periods ending September 30, 2014 and later are subject to examination by applicable taxing authorities.
- p. Subsequent Events
Management has evaluated for potential recognition and disclosure events subsequent to the date of the statement of financial position through March 5, 2018, the date the financial statements were available to be issued. No events have occurred subsequent to the statement of financial position date through our evaluation date that would require adjustment to or disclosure in the financial statements.
- q. New Accounting Pronouncement
On August 18, 2016, the Financial Accounting Standards Board (FASB) issued an Accounting Standards Update (ASU) No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. The ASU, which becomes effective for the

December 31, 2018 year, with early implementation permitted, focuses on improving the current net asset classification requirements and information presented in financial statements and notes that is useful in assessing a not-for-profit's liquidity, financial performance and cash flows.

FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*. The ASU, which becomes effective for the December 31, 2019 year, focuses on a principle-based model. It highlights the identification of performance obligations of the contract, determining the price and allocating that price to the performance obligation so that revenue is recognized as each performance obligation is satisfied.

FASB issued ASU No. 2016-02, *Leases*. The ASU which becomes effective for the December 31, 2020 year, requires the full obligation of long term leases to be recorded as a liability with a corresponding "right to use asset" on the statement of financial position.

Pencil has not yet evaluated the impact these standards will have on future financial statements.

Note 3 - Investments

Investments are recorded at fair value. Accounting standards have established a fair value hierarchy giving the highest priority to quoted market prices in active markets and the lowest priority to unobservable data.

The fair value hierarchy is categorized into three levels based on the inputs as follows:

Level 1 – Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that Pencil has the ability to access.

Level 2 – Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly.

Level 3 – Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Investments can be summarized as follows:

	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
Certificates of deposit		\$484,154	\$484,154
Exchange traded funds:			
Short-term bonds	\$115,778		115,778
Corporate fixed income:			
Financial services		25,733	25,733
Communication services		25,156	25,156
Energy		26,242	26,242
Consumer cyclical		51,914	51,914
Healthcare		<u>25,384</u>	<u>25,384</u>
Subtotal	<u>115,778</u>	638,583	754,361
Money market funds and other cash		<u>482,809</u>	<u>482,809</u>
Total	<u>\$115,778</u>	<u>\$1,121,392</u>	<u>\$1,237,170</u>

Level 1 securities are valued at the closing price reported on the active market they are traded on. Level 2 securities are valued using observable market inputs for securities that are similar to those owned. This method produces a fair value calculation that may not be indicative of net realizable value or reflective of future values. The use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in different fair value measurements.

Note 4 - Fixed Assets

Fixed assets can be summarized as follows:

		<u>Useful Life</u>
Computer hardware and software	\$113,329	<i>5 years</i>
Furniture and equipment	198,962	<i>5 years</i>
Leasehold improvements	591,669	<i>5 years</i>
Website database and program	<u>387,840</u>	<i>3 years</i>
	1,291,800	
Less: accumulated depreciation	<u>(1,249,279)</u>	
Total	<u>\$42,521</u>	

Note 5 - Temporarily Restricted Net Assets

Temporarily restricted net assets can be summarized as follows:

	Balance <u>1/1/17</u>	<u>Contributions</u>	Released from <u>Restrictions</u>	Balance <u>12/31/17</u>
Program restrictions:				
Partnership program	\$275,000	\$259,500	(\$297,000)	\$237,500
Career awareness	40,000	0	(40,000)	0
Internship Program	<u>121,000</u>	<u>156,700</u>	<u>(123,200)</u>	<u>154,500</u>
Total program restrictions	436,000	416,200	(460,200)	392,000
Time restrictions	<u>155,500</u>	<u>0</u>	<u>(153,000)</u>	<u>2,500</u>
Total	<u>\$591,500</u>	<u>\$416,200</u>	<u>(\$613,200)</u>	<u>\$394,500</u>

Note 6 - Special Events

Pencil hosts an annual fundraising event. The special event proceeds and related expenses summarized as follows:

Gross revenue	\$1,252,030
Less: expenses with a direct benefit to donors	<u>(130,380)</u>
	1,121,650
Less: other event expenses	<u>(119,216)</u>
Total revenue	<u>\$1,002,434</u>

Note 7 - In-Kind Contributions

In-kind contributions were allocated as follows:

	<u>Programs</u>	Management and <u>General</u>	<u>Fundraising</u>	<u>Total</u>
Travel, training and meetings	\$47,355	\$5,925	\$0	\$53,280
Professional fees	0	59,847	0	59,847
Consulting	<u>73,400</u>	<u>25,620</u>	<u>8,800</u>	<u>107,820</u>
Total	<u>\$120,755</u>	<u>\$91,392</u>	<u>\$8,800</u>	<u>\$220,947</u>

Note 8 - Retirement Plan

Pencil has adopted a tax deferred 401(k) retirement plan for their employees. All employees are eligible to participate and can designate a percentage of their salaries, subject to regulatory limits, to be contributed to the plan on a pre-tax basis. Effective, April 1, 2017, Pencil began providing matching contributions by contributing up to 1% of employee's salary to the plan. During 2017 Pencil made contributions totaling \$7,007 to the plan.

Note 9 - Commitments

Pencil has a lease for office space which was set to expire on July 31, 2018, but was extended until 2023. Future minimum payments are as follows:

Year ending:	December 31, 2018	\$308,493
	December 31, 2019	314,663
	December 31, 2020	320,957
	December 31, 2021	327,376
	December 31, 2022	333,923
Thereafter		<u>197,042</u>
Total		<u>\$1,802,454</u>