



Audited Financial Statements

September 30, 2014



INDEPENDENT AUDITORS' 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 September 30, 2014, 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.

Auditors' Responsibility

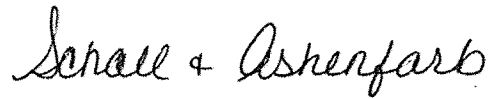
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about 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 auditors' 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 September 30, 2014, 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

May 19, 2015

PENCIL, INC.
STATEMENT OF FINANCIAL POSITION
AT SEPTEMBER 30, 2014

Assets

Cash and cash equivalents	\$84,463
Grants and pledges receivable (Note 3)	1,095,561
Investments (Note 4)	1,936,848
Prepaid expenses and other assets	25,932
Security deposit	42,971
Fixed assets, net (Note 5)	<u>233,575</u>
 Total assets	 <u><u>\$3,419,350</u></u>

Liabilities and Net Assets

Liabilities:	
Accounts payable and accrued expenses	\$176,443
Advances	52,309
Deferred rent	154,000
Deferred service fee income	2,500
Total liabilities	<u>385,252</u>
 Net assets:	
Unrestricted	2,402,456
Temporarily restricted (Note 6)	<u>631,642</u>
Total net assets	<u>3,034,098</u>
 Total liabilities and net assets	 <u><u>\$3,419,350</u></u>

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

PENCIL, INC.
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2014

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Public support and revenue:			
Contributions	\$900,626	\$819,745	\$1,720,371
Special events (net of expenses with direct benefit to donors) (Note 7)	1,264,821		1,264,821
Fee income	21,500		21,500
In-kind contributions (Note 8)	126,763		126,763
Interest and other income	66,619		66,619
Loss on uncollectable pledges	(164,901)	(430,099)	(595,000)
Net assets released from restrictions	920,232	(920,232)	0
Total public support and revenue	<u>3,135,660</u>	<u>(530,586)</u>	<u>2,605,074</u>
Expenses:			
Program services	2,957,495		2,957,495
Supporting services:			
Management and general	502,098		502,098
Fundraising	726,126		726,126
Total supporting services	<u>1,228,224</u>	<u>0</u>	<u>1,228,224</u>
Total expenses	<u>4,185,719</u>	<u>0</u>	<u>4,185,719</u>
Change in net assets from operating activities	<u>(1,050,059)</u>	<u>(530,586)</u>	<u>(1,580,645)</u>
Non-operating activities:			
Investment gains (Note 4)	118,322		118,322
Total non-operating activities	<u>118,322</u>	<u>0</u>	<u>118,322</u>
Change in net assets	(931,737)	(530,586)	(1,462,323)
Net assets - beginning of period	<u>3,334,193</u>	<u>1,162,228</u>	<u>4,496,421</u>
Net assets - end of period	<u>\$2,402,456</u>	<u>\$631,642</u>	<u>\$3,034,098</u>

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

PENCIL, INC.
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED SEPTEMBER 30, 2014

	<u>Supporting Services</u>				<u>Total Expenses</u>
	<u>Program Services</u>	<u>Management and General</u>	<u>Fundraising</u>	<u>Total Supporting Services</u>	
Salaries	\$1,779,900	\$198,823	\$372,939	\$571,762	\$2,351,662
Payroll taxes and benefits	432,565	48,319	90,635	138,954	571,519
Occupancy	267,029	24,275	55,487	79,762	346,791
Advertising and outreach		3,008		3,008	3,008
Program supplies and material	22,861			0	22,861
Office supplies and postage	49,724	4,520	10,332	14,852	64,576
Travel and entertainment	46,489	21,426	16,215	37,641	84,130
Telephone	12,493	1,136	2,596	3,732	16,225
Equipment	18,078	1,644	3,756	5,400	23,478
Depreciation	70,375	6,398	14,623	21,021	91,396
Professional fees (including in-kind) (Note7)	51,862	47,466	10,776	58,242	110,104
Consulting	172,603	103,834	48,089	151,923	324,526
Staff recruiting		1,901		1,901	1,901
Insurance	19,466	1,770	4,045	5,815	25,281
Bank charges and admin fees		36,301		36,301	36,301
Indirect special events			93,713	93,713	93,713
Miscellaneous	14,050	1,277	2,920	4,197	18,247
Total expenses	<u><u>\$2,957,495</u></u>	<u><u>\$502,098</u></u>	<u><u>\$726,126</u></u>	<u><u>\$1,228,224</u></u>	<u><u>\$4,185,719</u></u>

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

PENCIL, INC.
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED SEPTEMBER 30, 2014

Cash flows from operating activities:	
Change in net assets	(\$1,462,323)
Adjustments to reconcile change in net assets to net cash provided by/(used for) operating activities:	
Realized and unrealized gain on investments	(118,322)
Depreciation expense	91,396
Decrease in assets:	
Grants and pledges receivable	661,708
Prepaid expenses and other assets	6,358
Increase/(decrease) in liabilities:	
Accounts payable and accrued expenses	58,407
Advances	(26,318)
Deferred rent	3,000
	<u> </u>
Net cash flows used for operating activities	<u>(786,094)</u>
 Cash flows from investing activities:	
Purchase of investments	(752,223)
Proceeds from the sale of investments	702,276
Transfers into investment account	(364,533)
Transfers from investment account	1,270,000
Purchases of property and equipment	(12,745)
	<u> </u>
Net cash flows provided by investing activities	<u>842,775</u>
 Net increase in cash and cash equivalents	56,681
 Cash and cash equivalents - beginning of year	<u>27,782</u>
 Cash and cash equivalents - end of year	<u><u>\$84,463</u></u>
 Interest and taxes paid	 <u><u>\$0</u></u>

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

PENCIL, INC.
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2014

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 fund-raising event.

Pencil was incorporated in the State of New York and is exempt from Federal and state income taxes under Section 501(c)(3) of the Internal Revenue Code. Pencil has been designated as an organization which is not a private foundation.

In 2013, Pencil switched its year-end to the fiscal period September 30.

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.

Donor-restricted support is reported as an increase in unrestricted net assets, unless it contains a restriction by the donor for a specific program or time period. However, if a restriction is satisfied in the period the contribution has been made, it is recorded as unrestricted. 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.

c. 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.

d. 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; however 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.

e. Grants and 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.

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

Based on a review of specific accounts and based on historical trends, management has deemed that no allowance for doubtful accounts is necessary. Write-offs will be made when all collection efforts have been made and a pledge is probable of not being collected. Write-offs totaling \$595,000 were made during the year ended September 30, 2014, which included the write-off of a \$500,000 multi-year pledge. The write-offs have been reflected as a loss from uncollectable pledges on the statement of activities.

f. 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.

g. 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.

h. Advances

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

- i. 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.

- j. In-Kind Services
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 8 for details).

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.

- k. Advertising
The cost of advertising is expensed as incurred.

- l. 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.

- m. 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.

- n. Accounting for Uncertainty of Income Taxes
Pencil does not believe its financial statements include any material, uncertain tax positions. Tax filings for periods ending June 30, 2011 and later are subject to examination by applicable taxing authorities.

- o. Subsequent Events
Management has evaluated for potential recognition and disclosure events subsequent to the date of the statement of financial position through May 19, 2015, 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.

Note 3 - Pledges Receivable

Pledges receivable are due as follows:

For the year ended: September 30, 2015	\$1,033,061
September 30, 2016	<u>62,500</u>
Total	<u>\$1,095,561</u>

Note 4 - Investments

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.

At September 30, 2014, investments consisted of the following:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>
Money market funds and other cash	\$43,661	\$43,661	\$0
Certificates of deposit	484,665	0	484,665
Exchange traded funds	1,105,784	1,105,784	0
Fixed income	<u>302,738</u>	<u>0</u>	<u>302,738</u>
Total	<u>\$1,936,848</u>	<u>\$1,149,445</u>	<u>\$787,403</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.

During the year ended September 30, 2014, investment income consisted of:

Realized gains on sale of investments	\$22,478
Unrealized gains	<u>95,844</u>
Total	<u>\$118,322</u>

Note 5 - Property and Equipment

At September 30, 2014, property and equipment consisted of the following:

	<u>Life</u>	<u>Amount</u>
Computer hardware and software	5 years	\$98,312
Furniture and equipment	5 years	198,225
Leasehold improvements	5 years	589,869
Website database and program	3 years	<u>387,840</u>
Total property and equipment - cost		1,274,246
Less: accumulated depreciation		<u>(1,040,671)</u>
Total property and equipment - net		<u>\$233,575</u>

Note 6 - Temporarily Restricted Net Assets

The following summarizes the changes in temporarily restricted net assets:

	<u>Balance</u> <u>10/1/13</u>	<u>Contributions</u>	<u>Loss from</u> <u>Uncollectable</u> <u>Pledges</u>	<u>Released</u> <u>from</u> <u>Restrictions</u>	<u>Balance</u> <u>9/30/14</u>
Program restrictions:					
Partnership program	\$64,568	\$35,000	\$0	(\$76,675)	\$22,893
Career awareness	101,626	221,455	0	(269,987)	53,094
Technology & comm.	79,849	0	0	(79,849)	0
STEM learning	39,749	0	0	(27,245)	12,504
Fellows program	27,061	313,290	0	(188,851)	151,500
Financial success initiative	3,651	0	0	(2,625)	1,026
Downtown initiative	<u>75,000</u>	<u>0</u>	<u>0</u>	<u>(75,000)</u>	<u>0</u>
Total program restrictions	391,504	569,745	0	(720,232)	241,017
Time restrictions	<u>770,724</u>	<u>250,000</u>	<u>(430,099)</u>	<u>(200,000)</u>	<u>390,625</u>
Total	<u>\$1,162,228</u>	<u>\$819,745</u>	<u>(\$430,099)</u>	<u>(\$920,232)</u>	<u>\$631,642</u>

Note 7 - Fundraising Events

Pencil hosts an annual fundraising event. The special event proceeds are summarized as follows:

Gross revenue	\$1,416,771
Less: direct expense to donor	<u>(151,950)</u>
Net	1,264,821
Less: indirect expenses	<u>(93,713)</u>
Total	<u>\$1,171,108</u>

Note 8 - In-Kind Contributions

In-kind services of \$126,763 were allocated as follows:

	<u>Programs</u>	Management and <u>General</u>	<u>Fundraising</u>	<u>Total</u>
Occupancy	\$24,377	\$2,216	\$5,066	\$31,659
Professional fees	<u>51,862</u>	<u>32,466</u>	<u>10,776</u>	<u>95,104</u>
Total	<u>\$76,239</u>	<u>\$34,682</u>	<u>\$15,842</u>	<u>\$126,763</u>

A member of the board of directors is a partner in a law firm that donated legal services valued at approximately \$20,000. The revenue and related expense from this donation is recorded in the accompanying statement of activities.

Note 9 - 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. No contributions by Pencil are made to the plan.

Note 10 - Commitments

Pencil has a lease for office space which expires July 31, 2018. Future minimum payments are as follows:

<u>Year ending</u>	<u>Amount</u>
September 30, 2015	\$289,258
September 30, 2016	295,044
September 30, 2017	300,945
Thereafter	<u>254,953</u>
Total	<u>\$1,140,200</u>

Pencil rents office space from a company owned by a person who was a member of the Board of Directors for a portion of the year. Rent paid to that company for the fiscal year was \$269,765.