

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

FINANCIAL STATEMENTS

September 30, 2016
(With Comparative Totals for September 30, 2015)

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

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INDEPENDENT AUDITOR'S REPORT

January 23, 2017

To the Board of Trustees
The Pewabic Society, Inc.

Report on the Financial Statements

We have audited the accompanying financial statements of The Pewabic Society, Inc. (the "Society," a Michigan non-profit Corporation), which comprise the statement of financial position as of September 30, 2016, and the related statements of activities and cash flows for the year then ended, as well as the related notes to the financial statements.

Management's Responsibility for the Financial Statements

The Society's 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 Society'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 Society's internal control. Accordingly, we express no such opinion.

INDEPENDENT AUDITOR'S REPORT (CONTINUED)

Auditor's Responsibility (continued)

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 The Pewabic Society, Inc. as of September 30, 2016, 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.

Report on Summarized Comparative Information

We have previously audited the Society's financial statements as of, and for the year ended, September 30, 2015, and our report dated January 28, 2016 expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of, and for the year ended, September 30, 2015 is consistent, in all material respects, with the audited financial statements from which it has been derived.


CERTIFIED PUBLIC ACCOUNTANTS
Detroit, Michigan

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

STATEMENTS OF FINANCIAL POSITION

September 30, 2016
(With Comparative Totals as of September 30, 2015)

	<u>2016</u>	<u>2015</u>
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 356,753	\$ 511,954
Accounts receivable (net of allowance of \$2,361 and \$2,484 in 2016 and 2015, respectively)	21,253	22,357
Pledges receivable (net of allowance of \$-0- and \$3,500 in 2016 and 2015, respectively)	-0-	31,500
Grants receivable (no allowance considered necessary)	241,243	84,268
Inventories (Note E)	372,605	308,676
Prepaid expenses	578	5,506
	<u>992,432</u>	<u>964,261</u>
Total Current Assets		
Other Assets:		
Property and equipment, net (Note F)	2,538,033	2,108,555
Beneficial interest in assets held by Community Foundation for Southeast Michigan, at fair value (Note G)	79,494	67,772
Museum collection (Note A)	150,197	150,197
Trademarks	4,015	4,015
	<u>2,771,739</u>	<u>2,330,539</u>
Total Other Assets		
	<u><u>\$ 3,764,171</u></u>	<u><u>\$ 3,294,800</u></u>
Total Assets		

See notes to financial statements.

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

STATEMENTS OF FINANCIAL POSITION (CONTINUED)

September 30, 2016
(With Comparative Totals as of September 30, 2015)

	<u>2016</u>	<u>2015</u>
LIABILITIES AND NET ASSETS		
Current Liabilities:		
Accounts payable	\$ 174,775	\$ 184,161
Notes payable - current portion (Note J)	22,878	17,179
Accrued payroll and vacation (Note M)	136,785	111,856
Customer deposits	123,437	62,799
Deferred revenue	13,373	14,866
Gift certificates	22,257	16,413
	<u>493,505</u>	<u>407,274</u>
Total Current Liabilities		
Long-Term Liabilities:		
Notes payable (net of current portion) (Note J)	459,021	453,235
	<u>459,021</u>	<u>453,235</u>
Total Liabilities		
	<u>952,526</u>	<u>860,509</u>
Net Assets:		
Unrestricted:		
Board-designated (Note D)	2,056,134	1,638,141
Undesignated	531,574	523,353
	<u>2,587,708</u>	<u>2,161,494</u>
Total Unrestricted Net Assets		
Temporarily restricted (Note B)	203,937	252,797
Permanently restricted (Note C)	20,000	20,000
	<u>223,937</u>	<u>272,797</u>
Total Net Assets		
	<u>2,811,645</u>	<u>2,434,291</u>
Total Liabilities and Net Assets		
	<u>\$ 3,764,171</u>	<u>\$ 3,294,800</u>

See notes to financial statements.

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

STATEMENTS OF ACTIVITIES

**For the Year Ended September 30, 2016
(With Comparative Totals for the Year Ended September 30, 2015)**

	2016			Total	
	Unrestricted	Temporarily Restricted	Permanently Restricted	2016	2015
Public Support, Revenue, and Gains:					
Public support:					
Contributions	\$ 814,867	\$ 213,606	\$ -0-	\$ 1,028,473	\$ 785,353
Memberships and events	156,027			156,027	130,520
Net assets released from restrictions (Note B)	269,882	(269,882)		-0-	-0-
Total Public Support	1,240,776	(56,276)	-0-	1,184,500	915,873
Revenue and gains:					
Gallery sales and commissioned projects (Note K)	2,163,899			2,163,899	1,972,859
Educational	249,988			249,988	227,214
Other revenue and gains	8,153	7,416		15,569	1,762
Total Revenue and Gains	2,422,040	7,416	-0-	2,429,456	2,201,835
Total Public Support, Revenue, and Gains	3,662,816	(48,860)	-0-	3,613,956	3,117,708
Expenses:					
Program services:					
Art design studio	442,870			442,870	403,056
Gallery	1,585,642			1,585,642	1,278,816
Education	549,441			549,441	429,290
Museum	20,792			20,792	19,698
Exhibitions	74,279			74,279	30,849
Total Program Services	2,673,024	-0-	-0-	2,673,024	2,161,709
Supporting services:					
Administrative and general	208,668			208,668	247,179
Development, membership, and campus expansion	354,910			354,910	314,167
Total Supporting Services	563,578	-0-	-0-	563,578	561,346
Total Expenses	3,236,602	-0-	-0-	3,236,602	2,723,055
Net Increase (Decrease) in Net Assets	426,214	(48,860)	-0-	377,354	394,653
Net Assets, Beginning of Year	2,161,494	252,797	20,000	2,434,291	2,039,638
Net Assets, End of Year	\$ 2,587,708	\$ 203,937	\$ 20,000	\$ 2,811,645	\$ 2,434,291

See notes to financial statements.

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

STATEMENTS OF CASH FLOWS

For the Year Ended September 30, 2016
(With Comparative Totals for the Year Ended September 30, 2015)

	<u>2016</u>	<u>2015</u>
Cash Flows from Operating Activities:		
Net increase in net assets	\$ 377,354	\$ 394,653
Adjustments to reconcile net increase in net assets to net cash from operating activities:		
Depreciation	114,037	95,641
Net realized and unrealized (gains) losses in beneficial interest in assets held by Community Foundation for Southeast Michigan	(7,416)	3,629
Noncash fees paid from Endowment Funds	694	434
(Increase) decrease in:		
Accounts receivable	1,104	5,638
Pledges receivable	31,500	22,500
Grants receivable	(156,975)	6,548
Inventories	(63,929)	(8,192)
Prepaid expenses	4,928	7,723
Increase (decrease) in:		
Accounts payable	(9,386)	48,882
Accrued payroll and vacation	24,929	(24,147)
Customer deposits	60,638	2,402
Deferred revenue	(1,493)	2,185
Gift certificates	5,844	1,916
	<u>381,829</u>	<u>559,812</u>
Cash Flows from Investing Activities:		
Acquisition of property and equipment	(543,515)	(212,092)
Contributions to Endowment Funds	(5,000)	(15,000)
	<u>(548,515)</u>	<u>(227,092)</u>
Net Cash Provided (Used) by Investing Activities	<u>\$ (548,515)</u>	<u>\$ (227,092)</u>

See notes to financial statements.

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

STATEMENTS OF CASH FLOWS (CONTINUED)

For the Year Ended September 30, 2016
(With Comparative Totals for the Year Ended September 30, 2015)

	<u>2016</u>	<u>2015</u>
Cash Flows from Financing Activities:		
Payments on notes payable	\$ (18,425)	\$ (16,586)
Proceeds issued on notes payable	29,910	-0-
	<u>11,485</u>	<u>(16,586)</u>
Net Cash Provided (Used) by Financing Activities		
	<u>11,485</u>	<u>(16,586)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(155,201)	316,134
Cash and Cash Equivalents Balance, Beginning of Year	<u>511,954</u>	<u>195,820</u>
Cash and Cash Equivalents Balance, End of Year	<u>\$ 356,753</u>	<u>\$ 511,954</u>
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the year for interest	<u>\$ 17,635</u>	<u>\$ 18,227</u>

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

September 30, 2016

NOTE A – NATURE OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Organization

The Pewabic Society, Inc. (the “Society”) is a Michigan non-profit Corporation established to preserve the heritage of the arts and craft movement in America through the handcrafting of ceramic art, through its stewardship of the National Historic Landmark Pottery Building, which is a living museum, and through education programs. The Society’s mission is focused on: (a) creating ceramic art, which continues the legacy of artist and founder Mary Chase Stratton, (b) designing and fabricating architectural tile, (c) educating students of all ages in the ceramic arts, and (d) creating artistic and audience development for ceramic artists through its galleries, exhibitions program, and special events. The Society’s revenue is derived principally from contributions, gallery sales, and commissioned tile projects; these revenue sources sustain the Society’s mission.

Basis of Accounting

The accompanying financial statements are prepared on the accrual basis of accounting.

Cash Equivalents

For purposes of the statements of cash flows, the Society considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

Accounts Receivable

Accounts receivable are comprised primarily of amounts due on commissioned and gallery projects. The Society provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance. The allowance for doubtful accounts is established based on a specific assessment of the accounts receivable balance at the end of the year. All amounts deemed to be uncollectible after management has made reasonable collection attempts are charged against the allowance for doubtful accounts in the period the determination is made.

Pledges Receivable

The Society’s pledges receivable are comprised primarily of amounts committed from individuals and foundations for the Society’s activities. Support is recognized when a pledge representing an unconditional promise to give is received; in the absence of such promise, support is recognized when the intent to give is collected. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE A – NATURE OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Grants Receivable

The Society receives grants from various funding sources. An allowance for doubtful accounts is established on a specific assessment of the amounts still owed at the end of the year. All amounts deemed uncollectible are charged against the allowance for doubtful accounts in the period the determination is made. Management did not consider an allowance for doubtful accounts necessary as of September 30, 2016 and 2015.

Inventories

Inventories consist of work-in-process and finished products and are stated at the lower of cost, determined by the first-in, first-out method, or market. The Society makes an allocation of manufacturing expenses to work-in-process and finished products, as well as charging direct labor costs.

Property and Equipment

Property and equipment are stated at cost. Donated property and equipment are recorded at approximate fair value at the date of the gift. Improvements and renewals are capitalized, while ordinary maintenance and repairs are expensed. Management annually reviews these assets to determine whether carrying values have been impaired. Depreciation is computed on the straight-line basis over the estimated useful lives of the related assets, which range from three to 25 years.

Museum Collection

The Society's museum collection consists of various art objects that are held for exhibition on site. Purchased items are capitalized at cost, while donated items are recorded at estimated fair value at the date of receipt from the donor.

Contributed Services

Many individuals volunteer their time that assists the Society in running its programs and fund raising campaigns. Contributed services meeting the requirements for recognition in the financial statements totaled \$94,598 and \$300 for the years ended September 30, 2016 and 2015, respectively.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE A – NATURE OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Donated Items and Materials

Donated items and materials totaled \$11,765 and \$16,364 for the years ended September 30, 2016 and 2015, respectively.

Public Support and Revenue

Contributions

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions. The Society reports contributions of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires (that is, when a stipulated time restriction ends or a purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and are reported in the statements of activities as net assets released from restrictions.

Gallery Sales

Sales of gallery items are recognized as revenue at the time of sale.

Commissioned Projects

Revenue from commissioned projects is recognized at the time the project is completed and is either picked up or shipped, as applicable.

Educational

Revenue from educational activities is recognized in the period in which the activity occurs.

Deferred Revenue

Deferred revenue represents advance payments primarily relating to an educational event. Such deferred amounts are recognized as revenue in the period in which the event occurs.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE A – NATURE OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Customer Deposits

The Society receives up-front payments on commissioned projects and records such payments as customer deposit liabilities. Such deposits are recognized as revenue in the period in which the corresponding project is completed and shipped or picked up.

Functional Allocation of Expenses

Expenses by function have been allocated between program and supporting service classifications based upon management's estimates of time devoted to the specific activities.

Advertising

The Society uses advertising to promote its programs among the audiences it serves. Advertising costs are expensed as incurred. Advertising expense for the years ended September 30, 2016 and 2015 was \$216,400 and \$99,945, respectively.

Investments

The Society's investments are stated at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (an exit price). See Note G for information about the valuation of investments in endowment funds.

Purchases and sales of securities are recorded on a trade-date basis. Gains and losses on sales of securities are based on average costs. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Net appreciation includes the Society's gains and losses on investments bought and sold, as well as held, during the year.

Tax-Exempt Status

No provision has been established for income taxes since the Society is exempt from federal income taxes under section 501(c)(3) of the Internal Revenue Code ("IRC") and is not classified as a private foundation by the Internal Revenue Service. The Society's management is not aware of any unrecognized tax benefits as of September 30, 2016 or 2015.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE A – NATURE OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Use of Estimates

The preparation of 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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Fair Value Measurements

The Society uses fair value measurements in the preparation of its financial statements, which utilize various inputs, including those that can be readily observable, corroborated, or are generally unobservable. The Society utilizes market-based data and valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Additionally, the Society applies assumptions that market participants would use in pricing an asset or liability, including assumptions about risk.

The measurement of fair value includes a hierarchy based on the quality of inputs used to measure fair value. Financial assets and liabilities are categorized into this three-level fair value hierarchy based on the inputs to the valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets and liabilities and the lowest priority to unobservable inputs.

The various levels of the fair value hierarchy are described as follows:

- Level 1 - Financial assets and liabilities whose values are based on unadjusted quoted market prices for identical assets and liabilities in an active market that the Society has the ability to access
- Level 2 - Financial assets and liabilities whose values are based on quoted prices in markets that are not active or model inputs that are observable for substantially the full term of the asset or liability
- Level 3 - Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE A – NATURE OF ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fair Value Measurements (continued)

The use of observable market data, when available, is required in making fair value measurements. When inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurement.

Concentration of Credit Risk

Financial instruments which potentially subject the Society to concentrations of credit risk consist principally of cash, cash equivalents, and grants and accounts receivable.

Cash and cash equivalents are maintained at financial institutions and, at times, balances may exceed the federally insured limit of \$250,000 per depositor at each financial institution. Cash and cash equivalents on deposit in excess of the federally insured limit as of September 30, 2016 approximated \$110,000. Grants receivable are due from various funding sources. Accounts receivable are due from various entities primarily for amounts due on commissioned and gallery projects, as well as educational projects.

Comparative Financial Information

The financial statements include prior-year summarized comparative information in total but not by class of net assets. Accordingly, such information should be read in conjunction with the Society's financial statements as of, and for the year ended, September 30, 2015, from which the summarized information was derived.

Subsequent Events

The Society has evaluated subsequent events through January 23, 2017, the date that the accompanying financial statements were available to be issued.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE B – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available as of September 30, 2016 and 2015 for the following purposes or periods:

	<u>2016</u>	<u>2015</u>
Restricted for specific purposes:		
Capital projects	\$ 59,174	\$ 102,377
Educational projects	85,269	102,648
	<u>144,443</u>	<u>205,025</u>
Endowment Funds restricted for use in future periods	<u>59,494</u>	<u>47,772</u>
	<u>\$ 203,937</u>	<u>\$ 252,797</u>

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors, as follows:

	<u>2016</u>	<u>2015</u>
Purpose restrictions accomplished for the following purposes:		
Capital projects	\$ 113,203	\$ 146,831
Educational projects	155,985	105,928
Other projects	-0-	18,750
	<u>269,188</u>	<u>271,509</u>
Time restrictions on Endowment Funds expired by passage of specified time	<u>694</u>	<u>4,063</u>
	<u>\$ 269,882</u>	<u>\$ 275,572</u>

NOTE C – PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets totaling \$20,000 as of September 30, 2016 and 2015 consist of a donor-imposed restriction that requires the gift be maintained in perpetuity. Investment income is available to the Society for educational programs.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE D – BOARD-DESIGNATED NET ASSETS

The Society's Board of Trustees has designated \$2,056,134 and \$1,638,141 of unrestricted net assets as not being available for general operations without prior Board approval as of September 30, 2016 and 2015, respectively. The Board-designated net asset balance approximates the net book value of property, less long-term and other debt.

NOTE E - INVENTORIES

Inventories consist of the following components as of September 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Work-in-process	\$ 111,360	\$ 99,913
Finished goods	<u>261,245</u>	<u>208,763</u>
	<u>\$ 372,605</u>	<u>\$ 308,676</u>

NOTE F - PROPERTY AND EQUIPMENT

Property and equipment consist of the following as of September 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Land and land improvements	\$ 1,485,803	\$ 1,485,803
Buildings	471,856	471,856
Building improvements	727,369	485,017
Construction in progress	182,157	122,891
Machinery and equipment	<u>884,962</u>	<u>643,065</u>
	3,752,147	3,208,632
Less: Accumulated depreciation	<u>(1,214,114)</u>	<u>(1,100,077)</u>
	<u>\$ 2,538,033</u>	<u>\$ 2,108,555</u>

Depreciation expense totaled \$114,037 and \$95,641 for the years ended September 30, 2016 and 2015, respectively.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE G - CHARITABLE ENDOWMENT FUNDS

The Society has established the Pewabic Pottery Fund and the Pewabic Education Fund (collectively, the “Endowment Funds”) as component funds of the Community Foundation for Southeast Michigan (the “Foundation”). The Endowment Funds are assets of the Foundation. The majority of the Endowment Funds’ assets is invested in registered investment companies and collective trust funds.

The Foundation actively solicits contributions that can be designated to the Society. The Foundation transfers earnings on the Endowment Funds to the Society periodically in the form of grants so long as the Society continues to meet its tax-exempt purpose. The portion of the Endowment Funds that was funded by the Society, plus the net earnings on those balances, represents a reciprocal transfer and is, therefore, included in the Society’s financial statements. The Pewabic Pottery Fund provides general support for the Society, while the Pewabic Education Fund provides support to the Society’s educational programs.

The total fair value of the Endowment Funds as of September 30, 2016 and 2015 is \$110,889 and \$96,371, respectively; the portion included in the Society’s financial statements as of September 30, 2016 and 2015 is \$79,494 and \$67,772, respectively. The portion of each fund included in the Society’s financial statements, and the portion of each fund excluded from the Society’s financial statements, as of September 30, 2016 and 2015 are as follows:

	<u>Pewabic Pottery Fund</u>	<u>Pewabic Education Fund</u>	<u>Total</u>
2016			
Portion included in Society's financial statements	\$ 49,455	\$ 30,039	\$ 79,494
Portion excluded from Society's financial statements	<u>31,395</u>	<u> </u>	<u>31,395</u>
Total Fair Value of Endowment Funds	<u>\$ 80,850</u>	<u>\$ 30,039</u>	<u>\$ 110,889</u>

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE G - CHARITABLE ENDOWMENT FUNDS (CONTINUED)

	<u>Pewabic Pottery Fund</u>	<u>Pewabic Education Fund</u>	<u>Total</u>
2015			
Portion included in Society's financial statements	\$ 40,310	\$ 27,462	\$ 67,772
Portion excluded from Society's financial statements	<u>28,599</u>	<u> </u>	<u>28,599</u>
Total Fair Value of Endowment Funds	<u>\$ 68,909</u>	<u>\$ 27,462</u>	<u>\$ 96,371</u>

The portion of the Endowment Funds included in the Society's financial statements as of September 30, 2016 and 2015 is classified as follows:

	<u>Pewabic Pottery Fund</u>	<u>Pewabic Education Fund</u>	<u>Total</u>
2016			
Temporarily restricted	\$ 49,455	\$ 10,039	\$ 59,494
Permanently restricted	<u> </u>	<u>20,000</u>	<u>20,000</u>
	<u>\$ 49,455</u>	<u>\$ 30,039</u>	<u>\$ 79,494</u>
2015			
Temporarily restricted	\$ 40,310	\$ 7,462	\$ 47,772
Permanently restricted	<u> </u>	<u>20,000</u>	<u>20,000</u>
	<u>\$ 40,310</u>	<u>\$ 27,462</u>	<u>\$ 67,772</u>

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE G - CHARITABLE ENDOWMENT FUNDS (CONTINUED)

Reconciliations of the fair value of the assets in the Endowment Funds included in the Society's financial statements for the years ended September 30, 2016 and 2015, which also represent the fair value reconciliations of the Society's Level 3 assets that are measured at fair value on a recurring basis for those years, are as follows:

	<u>Temporarily Restricted</u>			<u>Permanently Restricted</u>	
	<u>Pewabic Pottery Fund</u>	<u>Pewabic Education Fund</u>	<u>Total</u>	<u>Pewabic Education Fund</u>	<u>Total</u>
2016					
Changes in Endowment Funds' (Level 3) Assets:					
Net realized and unrealized gains	\$ 4,540	\$ 2,876	\$ 7,416	\$ -0-	\$ 7,416
Contributions	5,000		5,000		5,000
Less: Administrative expenses	(395)	(299)	(694)		(694)
Net Increase in Endowment Funds' (Level 3) Assets	9,145	2,577	11,722	-0-	11,722
Balance, Beginning of Year	40,310	7,462	47,772	20,000	67,772
Balance, End of Year	\$ 49,455	\$ 10,039	\$ 59,494	\$ 20,000	\$ 79,494
Net gains for the year included in changes in net assets attributable to the change in unrealized gains or losses relating to assets still held as of September 30, 2016	\$ 4,540	\$ 2,876	\$ 7,416	\$ -0-	\$ 7,416
2015					
Changes in Endowment Funds' (Level 3) Assets:					
Net realized and unrealized gains (losses)	\$ (2,173)	\$ (1,456)	\$ (3,629)	\$ -0-	\$ (3,629)
Contributions	15,000		15,000		15,000
Less: Administrative expenses	(235)	(199)	(434)		(434)
Net Increase (Decrease) in Endowment Funds' (Level 3) Assets	12,592	(1,655)	10,937	-0-	10,937
Balance, Beginning of Year	27,718	9,117	36,835	20,000	56,835
Balance, End of Year	\$ 40,310	\$ 7,462	\$ 47,772	\$ 20,000	\$ 67,772
Net gains (losses) for the year included in changes in net assets attributable to the change in unrealized gains or losses relating to assets still held as of September 30, 2015	\$ (2,173)	\$ (1,456)	\$ (3,629)	\$ -0-	\$ (3,629)

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE G - CHARITABLE ENDOWMENT FUNDS (CONTINUED)

The Society's Board of Trustees has interpreted existing law and the agreements with the Foundation as not requiring the preservation of the fair value of any deposits to the Endowment Funds, except for amounts previously donated to the Society to be maintained in perpetuity that were subsequently deposited into the Endowment Funds. As a result of this interpretation, the Society classifies in permanently restricted net assets the original value of the initial deposit donated to the Society for use in the Pewabic Education Fund. Although the income generated by the portion of the Endowment Funds may be used to support various activities of the Society, the remaining portion of the Endowment Funds that is not classified in permanently restricted net assets is subject to a time restriction and, therefore, is classified in temporarily restricted net assets.

The Society's policy is to spend assets from the Endowment Funds as they are distributed by the Foundation. The Foundation invests the assets of the Endowment Funds as part of a pooled endowment with similar funds held on behalf of other non-profit organizations. The assets of the Foundation's pooled endowment are invested in a manner intended to maximize investment returns over a diversified portfolio in order to achieve a moderate level of investment risk.

NOTE H – FAIR VALUE

The Society's fair value hierarchy for those assets measured at fair value on a recurring basis as of September 30, 2016 and 2015 is summarized as follows:

	Fair Value Measurements			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
2016				
Assets:				
Beneficial interest in assets held by Community Foundation for Southeast Michigan	\$ -0-	\$ -0-	\$ 79,494	\$ 79,494
Cash and cash equivalents	356,753			356,753
	\$ 356,753	\$ -0-	\$ 79,494	\$ 436,247

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE H – FAIR VALUE (CONTINUED)

	<u>Fair Value Measurements</u>			
	<u>Quoted Prices in Active Markets for Identical Assets (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>	<u>Significant Unobservable Inputs (Level 3)</u>	<u>Total</u>
2015				
Assets:				
Beneficial interest in assets held by Community Foundation for Southeast Michigan	\$ -0-	\$ -0-	\$ 67,772	\$ 67,772
Cash and cash equivalents	<u>511,954</u>			<u>511,954</u>
	<u>\$ 511,954</u>	<u>\$ -0-</u>	<u>\$ 67,772</u>	<u>\$ 579,726</u>

The fair value reconciliations of the Society's Level 3 assets that are measured at fair value on a recurring basis for the years ended September 30, 2016 and 2015 are presented in Note G.

NOTE I - LINE OF CREDIT

The Society has available a \$400,000 line of credit with a bank, entered into on September 17, 2014. The line bears interest at a rate which is indexed to the bank's prime commercial rate; the effective rate is 3.25 percent as of September 30, 2016. Interest is payable monthly, and the line of credit is secured by the Society's accounts receivable, inventory, and property and equipment. As of September 30, 2016 and 2015, there was no outstanding balance on the line of credit.

NOTE J – NOTES PAYABLE

The Society has a note payable to a bank as of September 30, 2016 and 2015, entered into on September 17, 2014, which is due in monthly installments of \$2,901, including interest at 3.75 percent per annum. The note payable is collateralized by the Society's real estate.

The Society also has a note payable to an automotive credit institution as of September 30, 2016, entered into on June 30, 2016, which is due in monthly installments of \$415 for six years and is interest-free. This note payable was issued in conjunction with the purchase of a vehicle.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE J – NOTES PAYABLE (CONTINUED)

Future maturities are summarized as follows as of September 30, 2016:

For the Year Ending September 30:	
2017	\$ 22,878
2018	23,570
2019	24,289
2020	24,995
2021	382,428
2022	<u>3,739</u>
	<u>\$ 481,899</u>

Total interest expense on the note payable was \$17,635 and \$18,227 for the years ended September 30, 2016 and 2015, respectively.

NOTE K - GALLERY SALES AND COMMISSIONED PROJECTS

Gallery sales and commissioned projects are comprised of the following amounts for the years ended September 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Gallery sales and commissioned projects	\$ 2,204,958	\$ 1,999,989
Less: Returns and discounts	<u>(41,059)</u>	<u>(27,130)</u>
	<u>\$ 2,163,899</u>	<u>\$ 1,972,859</u>

Cost of sales related to gallery sales and commissioned projects is allocated among the Society's various program services and total \$1,197,116 and \$1,095,416 for the years ended September 30, 2016 and 2015, respectively.

NOTE L - LEASES

The Society leases certain equipment and facilities under operating leases which expire at various dates through September 2018.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE L - LEASES (CONTINUED)

Future minimum rental commitments as of September 30, 2016 are as follows:

For the Year Ending September 30:	
2017	\$ 1,990
2018	<u>1,990</u>
Total Minimum Lease Payments	<u>\$ 3,980</u>

Rental expense for the years ended September 30, 2016 and 2015 was \$2,536 and \$2,215, respectively.

NOTE M - EMPLOYEE BENEFIT PLANS

Effective September 1, 2015, the Society established a defined contribution retirement plan under section 401(k) of the IRC available to substantially all employees. Under the plan, eligible employees are allowed to contribute up to 90 percent of their base salary. The Society may, for any plan year, in its sole discretion, make an employer contribution to be credited to the account of each participant up to the legal limit prescribed by the IRC.

Prior to September 1, 2015, the Society had a defined contribution retirement plan under section 403(b) of the IRC available to substantially all employees. Participants could make basic contributions of their compensation to this plan up to the legal limit prescribed by the IRC; there was no provision for employer contributions under this plan.

Employer contributions to these plans, which have been accrued, totaled \$19,299 and \$4,774 for the years ended September 30, 2016 and 2015, respectively, and are included in accrued payroll and vacation in the accompanying statements of financial position.

NOTE N - NEW ACCOUNTING PRONOUNCEMENTS

The Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, *Revenue from Contracts with Customers*, in May 2014. The objectives of this ASU are to improve upon revenue recognition requirements by providing a single comprehensive model to determine the measurement of revenue and timing of recognition. The core principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE N - NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

This ASU also requires expanded qualitative and quantitative disclosures regarding the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. ASU 2014-09 applies to the Society's financial statements for the year ending September 30, 2020 and is to be applied retrospectively. Early adoption prior to the year ending September 30, 2018 is not permitted. The Society's management has not determined the impact on its financial statements as a result of implementing ASU 2014-09.

The FASB issued ASU 2016-02, *Leases (Topic 842)*, in February 2016. ASU 2016-02 requires the recognition by lessees of assets and liabilities that arise from all lease transactions, except for leases with a lease term of 12 months or less. The lessee accounting model under ASU 2016-02 retains two types of leases: finance leases, which are to be accounted for in substantially the same manner as the existing accounting for capital leases, and operating leases, which are to be accounted for (both in the statement of activities and the statement of cash flows) in a manner consistent with existing accounting for operating leases. ASU 2016-02 also requires expanded qualitative and quantitative disclosures regarding the amount, timing, and uncertainty of cash flows arising from leases. ASU 2016-02 applies to the Society's financial statements for the year ending September 30, 2021, with earlier implementation permitted. The Society's management has not determined the impact on its financial statements as a result of implementing ASU 2016-02.

The FASB issued ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*, in August 2016. ASU 2016-14 modifies the requirements related to financial statement presentation for non-profit organizations. The major provisions of ASU 2016-14 are as follows:

- Information about net assets and changes in net assets will be reported for two classes of net assets: *net assets with donor restrictions* and *net assets without donor restrictions*.
- Reporting of expenses by both function and nature in one location will be required for all non-profit organizations.
- Either the direct method or the indirect method for presenting operating cash flows may continue to be used, but the requirement for those entities using the direct method to prepare a reconciliation with the indirect method will be eliminated.
- Quantitative information that communicates the availability of the organization's financial assets as of the statement of financial position date to meet cash needs for general expenditures within one year will be required to be presented on the face of the financial statements or in the notes to the financial statements.
- Qualitative information on how the organization manages its liquid available resources and liquidity risks will be required to be disclosed in the notes to the financial statements.

THE PEWABIC SOCIETY, INC.
(A Michigan Non-Profit Corporation)

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

September 30, 2016

NOTE N - NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

- Reporting of the “underwater” amounts of donor-restricted endowment funds in net assets with donor restrictions and enhanced disclosures about “underwater” endowments will be required.
- Other enhanced disclosures regarding board designations and appropriations, the nature of net assets with donor restrictions, and functional expense allocation methods will also be required.

ASU 2016-14 applies to the Society’s financial statements for the year ending September 30, 2019, with earlier implementation permitted, and is to be applied retrospectively, with certain disclosure exceptions in the year of implementation. The Society’s management has not determined the impact on its financial statements as a result of implementing ASU 2016-14.