PRISON FELLOWSHIP MINISTRIES AND AFFILIATE

AUDITED CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED JUNE 30, 2014 AND 2013

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Independent Auditor's Report

Board of Directors
Prison Fellowship Ministries and Affiliate
Lansdowne, Virginia

We have audited the accompanying consolidated financial statements of **Prison Fellowship Ministries and Affiliate** (a nonprofit organization), which comprise the Consolidated Statements of Financial Position as of June 30, 2014 and 2013, and the related Consolidated Statements of Activities and Changes in Net Assets, Functional Expenses, and Cash Flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 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 consolidated 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 audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 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 financial statements.

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

Independent Auditor's Report (continued)

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of **Prison Fellowship Ministries and Affiliate** as of June 30, 2014 and 2013, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Aronson LLC

Rockville, Maryland
October 6, 2014

Certified Public Accountants & Management Consultants

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Consolidated Statements of Financial Position
($ in Thousands)

June 30		**2014**		2013
Assets				
Cash and cash equivalents	**$**	**1,116**	$	1,919
Cash and cash equivalents held for long-term use		**2,786**		3,160
Investments		**15,631**		17,459
Assets held in charitable remainder trusts		**212**		200
Total investments		**18,629**		20,819
Contributions receivable, net		**480**		590
Program advances and other receivables		**1,015**		1,358
Prepaid expenses and other assets		**345**		317
Inventory of publications and supplies		**442**		445
Beneficial interest in trusts		**717**		845
Cash surrender value of life insurance policies		**103**		96
Property, buildings and equipment, net		**17,538**		18,223
Total assets	**$**	**40,385**	$	44,612
Liabilities and Net Assets				
Liabilities				
Line of credit	**$**	**150**	$	-
Accounts payable and accrued expenses		**1,704**		1,507
Accrued salaries and benefits		**1,089**		883
Deferred revenue		**111**		81
Annuities payable		**4,483**		4,587
Liability under trust agreements		**106**		104
Total liabilities		**7,643**		7,162
Net assets				
Unrestricted		**23,647**		26,433
Temporarily restricted		**5,617**		7,565
Permanently restricted		**3,478**		3,452
Total net assets		**32,742**		37,450
Total liabilities and net assets	**$**	**40,385**	$	44,612

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

Prison Fellowship Ministries and Affiliate

Consolidated Statement of Activities and Changes in Net Assets
($ in Thousands)

For the Year Ended June 30, 2014	Unrestricted	Temporarily Restricted	Permanently Restricted	2014 Total
Support and revenue				
Contributions	$ 32,287	$ 2,956	$ -	$ 35,243
Investment return	954	328	-	1,282
Loss on sale and disposal of property	(53)	-	-	(53)
Other revenue	1,315	-	-	1,315
In-kind contributions	56	-	-	56
Net assets released from restrictions	5,287	(5,287)	-	-
Total support and revenue	39,846	(2,003)	-	37,843
Expenses				
Program services:				
Program ministry	19,668	-	-	19,668
Public education	5,077	-	-	5,077
International prison ministry	3,590	-	-	3,590
Total program services	28,335	-	-	28,335
Supporting services:				
Management and general	5,427	-	-	5,427
Fundraising	9,043	-	-	9,043
Total supporting services	14,470	-	-	14,470
Total expenses	42,805	-	-	42,805
Change in net assets from operations	(2,959)	(2,003)	-	(4,962)
Unrealized net market gain (loss) on investments	554	(16)	-	538
Change in value of split-interest agreements	(381)	71	26	(284)
Change in net assets	(2,786)	(1,948)	26	(4,708)
Net assets, beginning of year	26,433	7,565	3,452	37,450
Net assets, end of year	$ 23,647	$ 5,617	$ 3,478	$ 32,742

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

Prison Fellowship Ministries and Affiliate

Consolidated Statement of Activities and Changes in Net Assets
($ in Thousands)

For the Year Ended June 30, 2013	Unrestricted	Temporarily Restricted	Permanently Restricted	2013 Total
Support and revenue				
Contributions	$ 32,928	$ 6,147	$ 132	$ 39,207
Investment return	432	92	-	524
Loss on sale and disposal of property	(4)	-	-	(4)
Other revenue	1,845	-	-	1,845
In-kind contributions	129	-	-	129
Net assets released from restrictions	5,404	(5,404)	-	-
Total support and revenue	40,734	835	132	41,701
Expenses				
Program services:				
Program ministry	18,083	-	-	18,083
Public education	5,260	-	-	5,260
International prison ministry	1,710	-	-	1,710
Total program services	25,053	-	-	25,053
Supporting services:				
Management and general	5,294	-	-	5,294
Fundraising	8,700	-	-	8,700
Total supporting services	13,994	-	-	13,994
Total expenses	39,047	-	-	39,047
Change in net assets from operations	1,687	835	132	2,654
Unrealized net market gain on investments	313	101	-	414
Change in value of split-interest agreements	(328)	9	56	(263)
Change in net assets	1,672	945	188	2,805
Net assets, beginning of year	24,761	6,620	3,264	34,645
Net assets, end of year	$ 26,433	$ 7,565	$ 3,452	$ 37,450

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

Prison Fellowship Ministries and Affiliate

Consolidated Statement of Functional Expenses
($ in Thousands)

	Program Services				Supporting Services			
For the Year Ended June 30, 2014	**Program Ministry**	**Public Education**	**International Prison Ministry**	**Total**	**Management and General**	**Fundraising**	**Total**	**2014 Total**
Salaries and related expenses	$ 11,882	$ 1,640	$ -	$ 13,522	$ 3,410	$ 2,544	$ 5,954	**$ 19,476**
Other expenses								
Consulting	1,168	410	-	1,578	220	143	363	**1,941**
Donations	753	-	3,590	4,343	1	2	3	**4,346**
Materials and supplies	1,784	75	-	1,859	223	99	322	**2,181**
Occupancy	309	52	-	361	148	64	212	**573**
Other	839	114	-	953	498	95	593	**1,546**
Postage	501	674	-	1,175	125	1,716	1,841	**3,016**
Printing	159	752	-	911	127	1,947	2,074	**2,985**
Professional fees	161	1,165	-	1,326	263	2,078	2,341	**3,667**
Repair and maintenance	111	20	-	131	50	27	77	**208**
Telephone	241	58	-	299	59	41	100	**399**
Travel	1,266	59	-	1,325	159	204	363	**1,688**
	19,174	5,019	3,590	27,783	5,283	8,960	14,243	**42,026**
Depreciation and amortization	494	58	-	552	144	83	227	**779**
Total expenses	**$ 19,668**	**$ 5,077**	**$ 3,590**	**$ 28,335**	**$ 5,427**	**$ 9,043**	**$ 14,470**	**$ 42,805**

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

Consolidated Statement of Functional Expenses
($ in Thousands)

For the Year Ended June 30, 2013	Program Services: Program Ministry	Program Services: Public Education	Program Services: International Prison Ministry	Program Services: Total	Supporting Services: Management and General	Supporting Services: Fundraising	Supporting Services: Total	2013 Total
Salaries and related expenses	$ 10,957	$ 1,507	$ -	$ 12,464	$ 3,099	$ 2,375	$ 5,474	$ 17,938
Other expenses								
Consulting	861	352	-	1,213	197	300	497	1,710
Donations	394	1	1,710	2,105	2	-	2	2,107
Materials and supplies	2,005	61	-	2,066	234	107	341	2,407
Occupancy	369	46	-	415	89	48	137	552
Other	534	83	-	617	72	102	174	791
Postage	478	723	-	1,201	95	1,530	1,625	2,826
Printing	150	861	-	1,011	99	1,866	1,965	2,976
Professional fees	242	1,432	-	1,674	1,010	2,021	3,031	4,705
Repair and maintenance	216	26	-	242	53	31	84	326
Telephone	262	64	-	326	76	45	121	447
Travel	933	43	-	976	121	182	303	1,279
	17,401	5,199	1,710	24,310	5,147	8,607	13,754	38,064
Depreciation and amortization	682	61	-	743	147	93	240	983
Total expenses	$ 18,083	$ 5,260	$ 1,710	$ 25,053	$ 5,294	$ 8,700	$ 13,994	$ 39,047

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

Prison Fellowship Ministries and Affiliate

Consolidated Statements of Cash Flows
($ in Thousands)

For the Years Ended June 30,	**2014**	2013
Cash flows from operating activities		
Change in net assets	**$ (4,708)**	$ 2,805
Adjustments to reconcile change in net assets to net cash (used) provided by operating activities		
Depreciation and amortization	**779**	983
Change in contributions receivable discount and allowance	**129**	122
Contributed securities	**-**	(1,913)
Contributions of beneficial interests in trusts	**-**	(12)
Realized and unrealized gains on investments	**(1,519)**	(693)
Actuarial loss on annuity obligations	**381**	327
Loss on sale and disposal of property	**53**	4
Change in cash surrender value of life insurance policies	**(7)**	(12)
Receipt of permanently restricted contributions	**-**	(132)
(Increase) decrease in:		
Contributions receivable	**(19)**	1,016
Program advances and other receivables	**343**	(352)
Prepaid expenses and other assets	**(28)**	(32)
Inventory of publications and supplies	**3**	8
Beneficial interest in trusts	**128**	75
Increase (decrease) in:		
Accounts payable and accrued expenses	**197**	(1,166)
Accrued salaries and benefits	**206**	229
Deferred revenue	**30**	1
Liability under trust agreements	**2**	(4)
Net cash (used) provided by operating activities	**(4,030)**	1,254
Cash flows from investing activities		
Transfers from cash and cash equivalents held for long-term use	**374**	1,179
Proceeds from sale of property	**2**	2
Acquisitions of property and equipment	**(149)**	(640)
Proceeds from sale of investments	**14,662**	18,653
Purchase of investments	**(11,327)**	(19,773)
Net cash provided (used) by in investing activities	**3,562**	(579)
Cash flows from financing activities		
Proceeds from investments subject to annuity agreements	**154**	156
Payment of annuity obligations	**(639)**	(653)
Proceeds from draws on line of credit	**2,600**	-
Repayment of line of credit	**(2,450)**	-
Receipt of permanently restricted contributions	**-**	132
Net cash used by financing activities	**(335)**	(365)

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

Consolidated Statements of Cash Flows (continued)
($ in Thousands)

For the Years Ended June 30,		**2014**		2013
Net change in cash and cash equivalents		**(803)**		310
Cash and cash equivalents, beginning of year		**1,919**		1,609
Cash and cash equivalents, end of year	**$**	**1,116**	$	1,919
Supplemental disclosures				
Cash paid for interest	**$**	**5**	$	-
Payment of charitable trust obligations from assets held in charitable trusts	**$**	**15**	$	23
Noncash transactions				
Contributions of securities	**$**	**672**	$	1,913
Contributions of beneficial interests in trusts	**$**	**-**	$	12

The accompanying Notes to Consolidated Financial Statements are an integral part of these financial statements.

1. Organization and significant accounting policies

Organization: Prison Fellowship Ministries, a corporation organized under the laws of the District of Columbia, is a not-for-profit organization founded in 1976.

It is an expression of the Church, bringing peace to a broken world through works of grace, acts of justice and telling truth. Its charitable purposes include building and resourcing a movement of Christians committed to living and defending the Christian worldview; advocating for the reform of the justice system so communities will be safer, victims are respected and offenders are transformed; and serving and equipping the Church to fulfill the Great Commission among prisoners, ex-prisoners and their families.

It is a publicly supported organization exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code ("IRC"). It also performs ministry through one other related not-for-profit operating entity organized as a Virginia non-stock corporation:

- Prison Fellowship Ministries Foundation ("PFMF"), which manages and administers planned giving programs to support Prison Fellowship Ministries. In addition, PFMF owns property in Lansdowne, Virginia used by Prison Fellowship Ministries as office space.

Prison Fellowship Ministries provides administrative and monetary support to PFMF.

As of June 26, 2013, the Chuck Colson Center for Christian Worldview ("The Colson Center"), (formerly known at BreakPoint Inc.), a previously consolidated entity, was merged with Prison Fellowship Ministries. The Colson Center continues to provide a Christian worldview ministry that seeks to build and resource a movement of Christians committed to living and defending Christian worldview in all areas of life.

The consolidated financial statements presented here include the accounts of Prison Fellowship Ministries and PFMF (together, the "Organization," the "Ministry," and/or "PFM"). All significant intercompany transactions have been eliminated.

Funding for PFM is obtained primarily from private contributors.

Basis of accounting: PFM maintains its records using the accrual basis of accounting, where support is recognized when earned and expenses are recognized when incurred.

Financial Statement Presentation: PFM classifies net assets into three categories: unrestricted, temporarily restricted and permanently restricted. All contributions are considered to be available for unrestricted use unless specifically restricted by the donor.

Temporarily restricted net assets are contributions with temporary donor-imposed time and/or program restrictions. These temporary restrictions require that resources be used for specific purposes and/or in a later period or after a specified date. Temporarily restricted net assets become unrestricted when the time restrictions expire or the funds are used for their restricted purpose and are reported in the Consolidated Statement of Activities and Changes in Net Assets as net assets released from restrictions. When a restriction on a contribution is met in the same period in which the contribution was received, the contribution is reported in the statement of activities and changes in net assets as temporarily restricted revenue and as net assets released from restrictions.

Permanently restricted net assets represent amounts to be held in perpetuity.

As of June 30, 2014 and 2013, unrestricted net assets included $70 of donor advised funds. These funds are unrestricted by the donor, but have been earmarked by the Board for the purpose of issuing grants.

Cash and Cash Equivalents: PFM considers all highly liquid investments purchased with an original maturity of 90 days or less to be cash and cash equivalents. PFM maintains cash balances that may exceed federally insured limits at certain times during the year, but does not believe that this results in any significant credit risk.

Investments: The fair value of all debt and equity (common stock, mutual funds and money market mutual funds) securities with a readily determinable market value are based on published market prices. The alternative investments are limited partnerships formed for the purpose of investing in a variety of investment vehicles including but not limited to limited partnerships, limited liability companies, offshore corporations and other foreign investment vehicles, registered investment companies and direct investments in marketable securities and derivative instruments.

PFM's alternative investments, which are not readily marketable, are carried at estimated fair values as provided by the investment managers. The alternative investments have limitations on liquidity which may result in limitations on redemptions including, but not limited to, early redemption fees. Withdrawal rights may range from monthly to annually, after a notice period, usually for a period of up to two years from the date of the initial investment or an additional investment. PFM reviews and evaluates the values provided by the investment managers and agrees with the valuation methods and assumptions used in determining the fair value of these investments. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these securities existed.

PFM records investments received with a donor-imposed restriction that limits their use to long-term purposes as temporarily or permanently restricted investments.

Fair value measurement: PFM values certain assets at fair value in accordance with a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

Level 1. Observable inputs such as quoted prices in active markets for identical assets or liabilities;

Level 2. Inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and

Level 3. Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect assumptions that market participants would use in pricing the asset or liability based on the best information available in the circumstances.

Inputs are used in applying the various valuation techniques and broadly refer to the assumptions that market participants use to make valuation decisions, including assumptions about risk. Inputs may include price information, volatility statistics, specific and broad credit data, liquidity statistics, and other factors. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. However, the determination of what constitutes "observable" requires significant judgment by the entity.

PFM considers observable data to be that market data that is readily available, regularly distributed or updated, reliable and verifiable, not proprietary, and provided by independent sources that are actively involved in the relevant market. The categorization of a financial instrument within the hierarchy is based upon the pricing transparency of the instrument and does not necessarily correspond to the entity's perceived risk of that instrument.

Charitable Trusts: Assets held in charitable trusts are investments and are stated at fair value. The liability under trust agreements is calculated as the present value of the estimated future payments. The present value calculation uses a discount rate of 7.2% and life expectancy tables from the Internal Revenue Service. The change in value of split interest agreements includes the investment income and realized and unrealized gains and losses on the assets held in charitable trusts and actuarial adjustments to the calculated liabilities.

Contributions Receivable: The face amount of contributions receivable is reduced by an allowance for doubtful accounts. The allowance for doubtful accounts reflects the best estimate of probable losses determined principally on the basis of historical experience and specific allowances for known troubled accounts. All contributions or portions thereof that are deemed to be uncollectible or that require an excessive collection cost are written off to the allowance for doubtful accounts. As of June 30, 2014 and 2013, the allowance for doubtful accounts was $117 and $218, respectively.

Program advances and other receivables: Consist of amounts received postmarked by, but not deposited until after June 30, unsettled security sales and advance payments paid to vendors before expenses were incurred.

Inventory: Inventory consists of programmatic marketing materials, Angel Tree program materials, pamphlets, books and training materials available for sale and for ministry purposes and similar items. Inventory is valued at average cost based upon the first-in, first-out method.

Beneficial Interest in Trusts: PFM is named as the beneficiary in remainder and perpetual trusts held by third parties. The trusts are invested in cash equivalents, equity and fixed income funds, and other assets. Remainder trusts are measured at the present value of the future distributions expected to be received over the term of the agreement, discounted at a rate of 6%, which reflects current market conditions, adjusted for the life expectancy of the lead beneficiary using IRS actuarial tables. Perpetual trusts are measured using the fair value of amounts contributed to the trusts, multiplied by PFM's share of the total assets.

Fixed Assets: Land is carried at cost; all other property and equipment in excess of two thousand dollars in value is carried at cost less accumulated depreciation. Depreciation of property and equipment is computed on the straight-line basis over the estimated useful lives of the assets: buildings and improvements, 10 - 40 years; furniture and equipment, five years; vehicles, five years; and computer hardware and software, three years.

Annuities Payable: The liability for annuities is based on actuarially determined present values considering the income beneficiaries and applicable discount rates based on federal tables. An actuarial adjustment is recognized in the Consolidated Statement of Activities and Changes in Net Assets for the change in the value.

Contributions: PFM records pledges as contributions at net present value when there is documentation or other evidence for the amount, timing and nature of the contribution. Donated securities and in-kind contributions are recorded as contributions at their estimated fair market value on the date that control is relinquished by the donor. Other contributions, if not previously pledged, are recognized as support when cash is received. PFM reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets.

PFM records any contribution to another organization as an expense in the year an unconditional promise to give is made.

Donated Services: The work of PFM is multiplied many times over through the efforts of thousands of volunteers, who annually donate significant time to the Organization's programs and services. No amounts have been recorded in the consolidated financial statements for these donated services, in accordance with current accounting standards.

Allocation of costs: PFM classifies costs between the various program services and support services in order to clearly, consistently and accurately reflect its activities. Management reviews the allocation methods each year to ensure their propriety. Various factors – including the implementation of new programs or support systems, the general economic environment or the scheduling of capital fund raising projects – will have an effect on the overall allocation of costs between program services and support services. While it is the Ministry's intention to minimize the funds expended toward support services so that program services may be maximized, year-by-year fluctuations in the allocation should be expected.

Costs are allocated as follows:

Program Services

Program Ministry - Assisting local church congregations, volunteers and collaborating partners in ministry activity, including in-prison events (Bible studies and seminars; InnerChange Freedom Initiative® operations; Operation Starting Line® evangelism; mentoring and ongoing discipleship); re-entry support (mentoring, community-of-care building and case management); and Angel Tree® (including both Christmas ministry and activities beyond Christmas – such as supporting summer camping programs). The majority of these costs relate to salaries, benefits, travel and operating expenses for staff who recruit, train and assist local churches and volunteers to deliver ministry, and for necessary materials and resources for that ministry.

Public Education - Costs related to communicating the various issues in which PFM is involved to churches, volunteers, donors and the general public. This is performed through various media and includes direct mail, publications, internet, The Colson Center blogs, public meetings and conferences and radio programming (e.g., BreakPoint® and The Point®).

Additionally, certain costs of donor communications are recorded as public education when they meet specific requirements under generally accepted accounting principles (see "Costs of Joint Activities" below).

International Prison Ministry - Donations made to Prison Fellowship International ("PFI") for grants for specific PFI purposes and projects (see Note 14).

Supporting Services

Management and General - Support costs (administration, finance, information technology, human resources, etc.) not directly attributable to specific programs. Costs attributable to specific programs are reported as part of program services.

Fundraising - Costs of specific activities to generate financial contributions (e.g., fundraising appeals) are classified as *fundraising* costs. See "Costs of Joint Activities" (below) for additional information on allocations to other categories when a donor communication serves more than one purpose.

Costs of Joint Activities: PFM records the costs of joint activities that have elements of fundraising and one or more other functions (such as program or management and general) in conformity with U.S. Generally Accepted Accounting Principles (US GAAP), which establishes accounting standards for recording costs associated with joint activities. US GAAP requires that the criteria of purpose, audience and content be met in order to allocate any portion of the costs of joint activities to a functional area other than fundraising. See Note 13 for the dollar amounts of joint cost activities reported in the financial statements.

Advertising: Costs incurred for advertising are expensed as incurred. For the years ended June 30, 2014 and 2013, advertising costs approximated $45 and $46, respectively.

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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Tax Status: The Internal Revenue Service has recognized PFM and PFMF as Section 501(c)(3) not-for-profit corporations exempt from Federal income taxes as provided under the Internal Revenue Code and applicable regulations of the Commonwealth of Virginia. Therefore, PFM has made no provision for income taxes. Both PFM and PFMF are classified as public charities.

Uncertainty in income taxes: PFM evaluates uncertainty in income tax positions based on a more-likely-than-not recognition standard. If that threshold is met, the tax position is then measured at the largest amount that is greater than 50% likely of being realized upon ultimate settlement. As of June 30, 2014 and 2013, there are no accruals for uncertain tax positions. If applicable, the Organization records interest and penalties as a component of income tax expense. Tax years from 2011 through the current year remain open for examination by tax authorities.

Subsequent events: Management has evaluated subsequent events for disclosure in these financial statements through October 6 2014, which was the date the financial statements were available to be issued.

($ in Thousands)

New accounting pronouncements: Effective July 1, 2013, PFM adopted ASU 2012-05, *Not-for-Profit Entities: Classification of the Sale Proceeds of Donated Financial Assets in the Statement of Cash Flows*. ASU 2012-05 defines the appropriate financial reporting for the receipt of donated securities in the Consolidated Statements of Cash Flows. Donated securities with no donor-imposed restrictions are to be included in the Operating section of the statement, while donated securities with donor-imposed long-term restrictions should be included in the financing section. This update was prospectively applied to the year ended June 30, 2014.

2. Investments

Investments (including assets held in charitable remainder trusts) as of June 30, 2014 and 2013, are as follows:

	2014	2013
Cash and equivalents held for long-term use	**$ 2,786**	$ 3,160
Money market funds	**7**	6
Equities	**8,538**	9,705
Mutual funds:		
Equity funds	**197**	374
Fixed income funds	**484**	93
Fixed income securities:		
Federal government bonds and notes	**2,844**	3,161
Mortgage backed securities	**295**	2,950
Corporate bonds	**2,978**	577
International bonds	**495**	293
Alternative investments:		
Global hedge funds	**-**	498
REIT	**3**	-
Land trusts	**2**	2
Total investments	**$ 18,629**	$ 20,819

Investment income from all investment sources for the years ended June 30 is as follows:

	2014	2013
Investment income:		
Interest and dividends	**$ 301**	$ 245
Net realized and unrealized gains	**1,519**	693
Total investment income	**$ 1,820**	$ 938

($ in Thousands)

3. Fair value

Investments were recorded at fair value on a recurring basis as of June 30, 2014 based on the following level of hierarchy:

	Fair Value Measurements			
June 30, 2014	Total	Level 1	Level 2	Level 3
Beneficial interest in trusts	**$ 717**	**$ -**	**$ -**	**$ 717**
Investments:				
Cash and cash equivalents held for long-term use	**$ 2,786**	**$ 2,786**	**$ -**	**$ -**
Money market funds	**7**	**7**	**-**	**-**
Equities	**8,538**	**8,538**	**-**	**-**
Mutual funds:				
Equity funds	**197**	**197**	**-**	**-**
Fixed income funds	**484**	**484**	**-**	**-**
Fixed income securities:				
Federal government bonds and notes	**2,844**	**-**	**2,844**	**-**
Mortgage backed securities	**295**	**-**	**295**	**-**
Corporate bonds	**2,978**	**-**	**2,978**	**-**
International bonds	**495**	**-**	**495**	**-**
Alternative investments:				
REIT	**3**	**-**	**-**	**3**
Land trusts	**2**	**-**	**-**	**2**
Total investments	**$ 18,629**	**$ 12,012**	**$ 6,612**	**$ 5**

The following is a reconciliation of the beginning and ending balances for assets measured at fair value using significant unobservable inputs (Level 3) during the period ended June 30, 2014:

	Total	**Global Hedge Funds**	**Land Trusts**	**REIT**	**Beneficial Interest in Trusts**
Beginning balance	**$ 1,345**	**$ 498**	**$ 2**	**$ -**	**$ 845**
Total realized losses	**(37)**	**(37)**	**-**	**-**	**-**
Total unrealized gains	**78**	**-**	**-**	**-**	**78**
Sales	**(461)**	**(461)**	**-**	**-**	**-**
Additions - contributed	**3**	**-**	**-**	**3**	**-**
Disbursement of trust funds	**(206)**	**-**	**-**	**-**	**(206)**
Total	**$ 722**	**$ -**	**$ 2**	**$ 3**	**$ 717**

($ in Thousands)

Investments were recorded at fair value on a recurring basis as of June 30, 2013 based on the following level of hierarchy:

June 30, 2013	Total	Level 1	Level 2	Level 3
Beneficial interest in trusts	$ 845	$ -	$ -	$ 845
Investments:				
Cash and cash equivalents held for long-term use	$ 3,160	$ 3,160	$ -	$ -
Money market funds	6	6	-	-
Equities	9,705	9,705	-	-
Mutual funds:				
Equity funds	374	374	-	-
Fixed income funds	93	93	-	-
Fixed income securities:				
Federal government bonds and notes	3,161	-	3,161	-
Mortgage backed securities	2,950	-	2,950	-
Corporate bonds	577	-	577	-
International bonds	293	-	293	-
Alternative investments:				
Global hedge funds	498	-	-	498
Land trusts	2	-	-	2
Total	$ 20,819	$ 13,338	$ 6,981	$ 500

The following is a reconciliation of the beginning and ending balances for assets measured at fair value using significant unobservable inputs (Level 3) during the period ended June 30, 2013:

	Total	**Global Hedge Funds**	**Land Trusts**	**Beneficial Interest in Trusts**
Beginning balance	$ 2571	$ 1,661	$ 2	$ 908
Total realized gains	5	5	-	-
Total unrealized gains	117	60	-	57
Sales	(1,228)	(1,228)	-	-
Additions	11	-	-	11
Disbursement of trust funds	-	-	-	(20)
Reclassification	(111)	-	-	(111)
Total	$ 1,345	$ 498	$ 2	$ 845

Level 2 values were developed utilizing quoted prices for identical or similar assets in markets that are not active, that is, markets in which there are a few transactions for the asset, the prices are not current, or price quotations vary substantially either over time or amount, or in which little information is released publicly.

Level 3 alternative investments are based on net asset values as reported by the investment managers. The majority of the alternative investments are “fund of funds” investments. Net asset values are established based on the fair value of the underlying assets, which generally either have quoted prices or are developed using discounted cash flow models.

Level 3 beneficial interests consist of remainder trusts and perpetual trusts, which are invested in cash equivalents, equity and fixed income funds, and other assets. Remainder trusts are measured at the present value of the future distributions expected to be received over the term of the agreement, discounted at a rate of 6%, which reflects current market conditions, adjusted for the life expectancy of the lead beneficiary using IRS actuarial tables. Perpetual trusts are measured using the fair value of amounts contributed to the trusts, multiplied by PFM’s share of the total assets.

The table below presents additional information for PFM’s investments, as of June 30, 2014, whose fair value is estimated using the practical expedient of reported net asset value (NAV). These disclosures are required for all investments that are eligible to be valued using the practical expedient, regardless of whether the practical expedient has been applied.

	Fair Value at 6/30/2014	Fair Value at 6/30/2013	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Global Hedge Funds	**$ -**	**$ 498**	**$ -**	**Variable**	**0-100 days**

These funds include investments in a variety of investment vehicles including but not limited to limited partnerships, limited liability companies, offshore corporations and other foreign investment vehicles, registered investment companies and direct investments in marketable securities and derivative instruments. The fund objective was to preserve capital and to generate long-term appreciation and returns across a market cycle of between five to seven years.

($ in Thousands)

4. Contributions receivable

The following comprised contributions receivable as of June 30:

	2014	2013
Due less than 1 year	**$ 576**	$ 668
Due from 1 to 5 years	**22**	169
Total gross contributions receivable	**598**	837
Less:		
Allowance for doubtful accounts	**(117)**	(218)
Discounts on pledges due from 2 to 5 years	**(1)**	(29)
Contributions receivable, net	**$ 480**	$ 590

Contributions receivable are discounted to their present value using rates between 1.83% and 2.19%.

As of June 30, 2014, two donors had contributions receivables balance outstanding which represented 55% of total gross contributions receivable.

As of June 30, 2013, three donors had contributions receivables balance outstanding which represented 79% of total gross contributions receivable.

5. Conditional promises to give

In May 2014, the PFM received a conditional promise to give that is designed to provide funds through matching contributions. The maximum amount of the contributions can be up to $2,250 and will be paid when matching commitments are received by PFM.

($ in Thousands)

6. Property, buildings and equipment

Property, buildings and equipment is as follows at June 30:

		2014		2013
Land	**$**	**3,306**	$	3,306
Building and improvements		**19,575**		19,592
Furniture and equipment		**2,596**		3,202
Vehicles		**44**		44
Computer hardware		**770**		878
Computer software		**5,457**		5,472
Total		**31,748**		32,494
Less: Accumulated depreciation and amortization		**(14,632)**		(14,657)
		17,116		17,837
Construction in progress		**422**		386
Property, buildings and equipment, net	**$**	**17,538**	$	18,223

7. Split interest agreements

Charitable gift annuities: PFM has established a Planned Giving Fund to account for gift annuities and charitable trusts. Under the gift annuities program, in return for a contribution PFM agrees to pay the donor an annuity for the donor's lifetime. The liability for future payments to donors at 2014 and 2013, based on an independent actuarial valuation, is $4,483 and $4,587, respectively.

The liability is calculated using mortality rates from the 1983 Individual Annuity Mortality Table ("IAMT") for annuities issued prior to July 2000, and from the 2000 IAMT for annuities issued on or after July 1, 2000. A discount rate of 6.5% is used for annuities issued prior to July 2002, and 5% for those issued on or after July 1, 2002.

PFM sets its interest rate commitments under its gift annuities program based on those set by the American Council of Gift Annuities (“ACGA”) at the time of issuance. The ACGA rates are based on specific assumptions regarding, among other things, net investment returns and expected life span so that, upon the annuitant’s death, half of the original contribution remains available for PFM’s general operations. Because of the nature of gift annuities, it is possible that the total payments to an annuitant over his/her lifespan can exceed the net investment income and expected residual value of the segregated assets, if lower than expected long-term investment returns and/or higher than expected life spans are experienced. Management believes there are sufficient assets to meet the expected future obligations without using assets intended for daily operations.

Charitable trusts: As of June 30, 2014 and 2013, PFM maintained assets totaling $212 and $200, respectively, in conjunction with charitable remainder annuity trusts and charitable remainder unitrusts. Under these agreements, PFM is designated as the trustee and is required to make payments equal to a percentage of the net fair market value of the trust as of the valuation date over either the donor’s estimated life or a certain number of years, as specified in the trust agreement. Upon termination of the trust, PFM will receive the remaining assets. The trust assets are initially recorded at fair market value as of the date of donation. The liability for future payments to donors at June 30, 2014 and 2013 was $106 and $104, respectively.

Beneficial interest in trusts: PFM was named a beneficiary in two charitable remainder trusts held by third parties. The value of PFM’s interest in the trusts totaled $476 and $631, as of June 30, 2014 and 2013, respectively, and is included in temporarily restricted net assets. The changes in the fair value of the trust assets are recognized as temporarily restricted net asset. Distributions received from the trusts are recognized as unrestricted net assets unless purpose restricted by the donor.

PFM was named a beneficiary in four perpetual trust held by third parties. The value of PFM’s interest in the trusts totaled of $241 and $214, as of June 30, 2014 and 2013, respectively, and is included in permanently restricted net assets and the endowment. The changes in the fair value of the trust assets are recognized as permanently restricted net asset. Distributions received from the trusts are recognized as unrestricted net assets unless purpose restricted by the donor.

($ in Thousands)

8. Line of credit

PFM has a line of credit that was renewed on March 22, 2013, totaling $4,500, and is secured by a covenant not to encumber or convey PFM's Lansdowne, Virginia real property. This addendum will expire on March 25, 2015. At June 30, 2014 and 2013, there was $150 and $0 outstanding on the line of credit, respectively. The line of credit bears interest at the one-year LIBOR rate, plus 1.95%. The interest rate was 3.25% as of June 30, 2014 and 2013. Under the terms of the line of credit agreement, PFM must maintain a minimum tangible net worth of $25,000.

9. Concentration of credit risk

Financial instruments which potentially subject PFM to concentrations of credit risk consist primarily of cash, cash equivalents, investments and contributions receivable. PFM maintains substantially all of its cash, cash equivalents and investments in high credit-quality financial institutions. The total cash and investments balance in the financial institutions are insured by the Federal Deposit Insurance Corporation up to $250 and Securities Investor Protection Corporation up to $500. At June 30, 2014 and 2013, substantially all of PFM's cash, cash equivalents and investment balances were uninsured. For the composition of investment balances at June 30, 2014 and 2013, see Note 2.

10. Retirement plan

PFM maintains a defined contribution plan that covers all qualifying employees, as defined within the plan agreement. The plan is based on mandatory employee contributions of 2% of annual salary with PFM's discretionary contributions equaling 3% of annual salary for the years ended June 30, 2014 and 2013. Employees are 100% vested in contributions they make to the defined contribution plan and investment income earned thereon. Contributions by PFM on their behalf and investment income earned are immediately vested.

Total PFM contributions were $419 and $333 for the years ended June 30, 2014 and 2013, respectively.

11. Obligations under operating leases

PFM has entered into various operating lease agreements, primarily for office space and office equipment. Operating lease expense incurred under these operating leases were $72 and $68 in 2014 and 2013, respectively.

PFM's future minimum payments for the equipment under non-cancelable operating leases as of June 30, 2014, are as follows:

Year Ending June 30	Total
2015	$ 43
2016	12
2017	4
Total	$ 59

($ in Thousands)

12. Sublease rental income

PFM has entered into sublease rental agreements with three organizations for office space, office equipment and for the use of a portion of the building that is not otherwise occupied by PFM. Sublease rental income recognized by PFM was $1,041 and $1,105 in 2014 and 2013, respectively, and is included in other revenue on the Statements of Activities and Changes in Net Assets.

PFM's future sublease receipts for the use of the facilities as of June 30, 2014, are as follows:

Year Ending June 30		Total
2015	$	920
2016		786
2017		538
Total	$	2,244

13. Allocation of joint costs

During 2014 and 2013, PFM incurred joint costs of $7,067 and $7,128, respectively, for informational materials, primarily related to direct mailings that included fundraising appeals. Pursuant to GAAP, these costs were allocated to the functional areas as follows:

		2014		2013
Program services	**$**	**1,884**	$	2,159
Supporting services:				
Fundraising		**4,951**		4,755
Management and general		**232**		214
Total	**$**	**7,067**	$	7,128

14. Related parties

PFM is a chartered member and affiliated organization of Prison Fellowship International ("PFI"), the association of Prison Fellowship organizations in 124 countries. The assets, liabilities, and net assets of PFI are not consolidated with those of PFM. PFM provides monetary support to PFI consisting of grants and donations for specific program support. An agreement was signed in June 2013 to demonstrate and implement a visible and meaningful commitment to unity between the two organizations. The agreement addresses trademarks, office location, fundraising and funding.

($ in Thousands)

The total amount of monetary support provided to PFI was $3,670 and $1,710 in 2014 and 2013, respectively. As of June 30, 2014 and 2013, PFM had a contribution payable due in less than one year to PFI of approximately $40 and $0, respectively, which is included in accounts payable in the accompanying Consolidated Statements of Financial Position. As of June 30, 2014 and 2013, PFI owed PFM, $29 and $39, respectively, for operating and administrative costs included by PFM on behalf of PFI.

15. Risk and uncertainties

PFM invests in various investments. Investments are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investments, it is at least reasonably possible that changes in the values of investments will occur in the near term and that such changes could materially affect the amounts reported in the Consolidated Statement of Financial Position.

16. Temporarily restricted net assets

Temporarily restricted net assets at June 30, 2014 and 2013, are as follows:

	2014	2013
Program assistance	**$ 4,030**	$ 5,829
Time restricted for periods after June 30	**1,121**	1,575
Cumulative unappropriated endowment income – time restricted	**466**	161
Total	**$ 5,617**	$ 7,565

For the years ended June 20, 2014 and 2013, net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by the passage of time releasing time restrictions:

	2014	2013
Program assistance	**$ 4,453**	$ 3,382
Time restrictions expired	**827**	2,022
Endowment unappropriated earnings	**7**	-
Total	**$ 5,287**	$ 5,404

17. Permanently restricted net assets

Permanently restricted net assets consist of donations made with the restriction that the principal be maintained in perpetuity. The income earned on this principal can be used in the unrestricted operations of PFM; it is held as temporarily restricted pending distribution by the Board of Directors. Permanently restricted net assets at June 30, 2014 and 2013, are $3,478 and $3,452, respectively.

18. Endowment funds

The Organization had donor-restricted endowment funds totaling $3,478 and $3,452 at June 30, 2014 and 2013. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of the Relevant Law

The PFM Board of Directors has interpreted the Commonwealth of Virginia Uniform Prudent Management of institutional Funds Act ("UPMIFA") 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, PFM classifies as permanently restricted net assets (a) the original value of 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 permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the organization 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 the organization and donor-restricted endowment fund;
3. General economic conditions;
4. The possible effect of inflation and deflation;
5. The expected total return from income and appreciation of investments;
6. Other resources of the organization; and
7. The investment policies of the Organization.

($ in Thousands)

Endowment net assets composition by type of fund as of June 30, 2014:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ -	$ -	$ 3,478	$ 3,478
Change in value of split-interest agreements	-	41	-	41
Endowment income reserved by Board for endowment	-	466	-	466
Total funds	$ -	$ 507	$ 3,478	$ 3,985

Changes in endowment net assets for the fiscal year ended June 30, 2014:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ -	$ 202	$ 3,452	$ 3,654
Contributions	-	-	-	-
Investment return:				
Investment income	-	55	-	55
Net appreciation (realized and unrealized)	-	257	-	257
Total investment return	-	312	-	312
Appropriations of Endowment assets for expenditure	-	(7)	-	(7)
Change in value of perpetual trusts	-	-	26	26
Endowment net assets, end of year	$ -	$ 507	$ 3,478	$ 3,985

($ in Thousands)

Endowment net assets composition by type of fund as of June 30, 2013:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ -	$ -	$ 3,452	$ 3,452
Change in value of split-interest agreements	-	41	-	41
Endowment income reserved by Board for endowment	-	161	-	161
Total funds	$ -	$ 202	$ 3,452	$ 3,654

Changes in endowment net assets for the fiscal year ended June 30, 2013:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ -	$ 41	$ 3,264	$ 3,305
Contributions	-	-	132	132
Investment return:				
Investment income	-	42	-	42
Net appreciation (realized and unrealized)	-	119	-	119
Total investment return	-	161	-	161
Appropriations of endowment assets for expenditure	-	-	-	-
Change is value of split-interest agreements	-	-	56	56
Endowment net assets, end of year	$ -	$ 202	$ 3,452	$ 3,654

Description of amounts classified as permanently restricted and temporarily restricted net assets (endowment only):

		2014		2013
Permanently restricted net assets				
The portion of perpetual endowment funds that is required to be retained permanently either by explicit donor stipulation or by UPMIFA	**$**	**3,478**	$	3,452
Temporarily restricted net assets				
The portion of perpetual endowment funds subject to a time restriction under UPMIFA and without purpose restrictions	**$**	**466**	$	161

Funds with Deficiencies
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 UPMIFA requires the PFM to retain as a fund of perpetual duration. There were no such deficiencies as of June 30, 2014 and 2013.

Return Objectives and Risk Parameters
PFM has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment, while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that PFM must hold in perpetuity or for a donor-specified period(s), as well as board-designated funds. Under this policy, as approved by the Board of Directors, the endowment assets are invested in a manner that is intended to maximize the rate of return based upon specific allocation guidelines within the investment policy. The investment time horizon is long term and is expected that the investment portfolio will achieve moderate growth and growth of income in order to meet cash flow needs.

Strategies Employed for Achieving Objectives
To satisfy its long-term rate-of-return objectives, PFM relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). PFM targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

None of PFM's endowment earnings are donor-restricted. Any earnings are held as temporarily restricted income until appropriated for distribution by the Board. In establishing this policy, the Organization considered the long-term expected return on its endowment. This is consistent with PFM's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

19. Contingencies

The Organization maintains a self-insurance program for its employees' health care costs. Self-insurance costs are accrued based on claims reported as of the statement of financial position date as well as an estimated liability for claims incurred but not reported. The total accrued liability for self-insurance costs was $348 and $344 as of June 30, 2014 and 2013, respectively.