

**PRISON FELLOWSHIP MINISTRIES AND
AFFILIATE**

**AUDITED CONSOLIDATED FINANCIAL
STATEMENTS**

YEARS ENDED JUNE 30, 2016 AND 2015

Prison Fellowship Ministries and Affiliate

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Independent Auditor's Report

Board of Directors

Prison Fellowship Ministries and Affiliate
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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, 2016 and 2015, 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 consolidated 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 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.

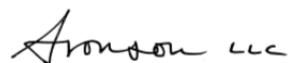
An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, 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 financial position of **Prison Fellowship Ministries and Affiliate** as of June 30, 2016 and 2015, 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.



Rockville, Maryland
October 14, 2016

Prison Fellowship Ministries and Affiliate

Consolidated Statements of Financial Position (\$ in Thousands)

<u>June 30</u>	<u>2016</u>	<u>2015</u>
Assets		
Cash and cash equivalents	\$ 958	\$ 436
Investments		
Cash and cash equivalents held for long-term use	3,787	4,390
Investments	19,081	15,569
Assets held in charitable remainder trusts	185	199
Total investments	23,053	20,158
Contributions receivable, net	740	290
Program advances and other receivables	872	1,091
Prepaid expenses and other assets	283	351
Inventory of publications and supplies	298	432
Beneficial interest in trusts	676	710
Cash surrender value of life insurance policies	86	107
Property, buildings and equipment, net	16,729	17,184
Total assets	\$ 43,695	\$ 40,759
Liabilities and Net Assets		
Liabilities		
Accounts payable and accrued expenses	\$ 2,490	\$ 1,638
Accrued salaries and benefits	857	899
Deferred revenue	80	72
Donor advances	35	-
Annuities payable	4,159	4,254
Liability under trust agreements	69	76
Total liabilities	7,690	6,939
Net assets		
Unrestricted	25,807	25,379
Temporarily restricted	6,742	4,967
Permanently restricted	3,456	3,474
Total net assets	36,005	33,820
Total liabilities and net assets	\$ 43,695	\$ 40,759

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)

<i>For the Year Ended June 30, 2016</i>	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Support and revenue				
Contributions	\$ 32,731	\$ 7,606	\$ -	\$ 40,337
Investment return	16	(6)	-	10
Loss on sale and disposal of property	(3)	-	-	(3)
Other revenue	1,349	-	-	1,349
In-kind contributions	139	-	-	139
Loss on impairment	(310)	-	-	(310)
Loss on restricted promises to give	-	(100)	-	(100)
Net assets released from restrictions	5,741	(5,741)	-	-
Total support and revenue	39,663	1,759	-	41,422
Expenses				
Program services:				
Program ministry	19,936	-	-	19,936
Public education	3,204	-	-	3,204
International prison ministry	2,735	-	-	2,735
Total program services	25,875	-	-	25,875
Supporting services:				
Management and general	4,247	-	-	4,247
Fundraising	8,824	-	-	8,824
Total supporting services	13,071	-	-	13,071
Total expenses	38,946	-	-	38,946
Change in net assets from operations	717	1,759	-	2,476
Unrealized net market gain on investments	100	39	-	139
Change in value of split-interest agreements	(389)	(23)	(18)	(430)
Change in net assets	428	1,775	(18)	2,185
Net assets, beginning of year	25,379	4,967	3,474	33,820
Net assets, end of year	\$ 25,807	\$ 6,742	\$ 3,456	\$ 36,005

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)

<i>For the Year Ended June 30, 2015</i>	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Support and revenue				
Contributions	\$ 33,457	\$ 4,473	\$ -	\$ 37,930
Investment return	524	137	-	661
Gain on sale and disposal of property	2	-	-	2
Other revenue	1,518	-	-	1,518
In-kind contributions	161	-	-	161
Net assets released from restrictions	5,181	(5,181)	-	-
Total support and revenue	40,843	(571)	-	40,272
Expenses				
Program services:				
Program ministry	18,508	-	-	18,508
Public education	3,116	-	-	3,116
International prison ministry	3,362	-	-	3,362
Total program services	24,986	-	-	24,986
Supporting services:				
Management and general	4,573	-	-	4,573
Fundraising	8,991	-	-	8,991
Total supporting services	13,564	-	-	13,564
Total expenses	38,550	-	-	38,550
Change in net assets from operations				
	2,293	(571)	-	1,722
Unrealized net market loss on investments	(262)	(94)	-	(356)
Change in value of split-interest agreements	(299)	15	(4)	(288)
Change in net assets	1,732	(650)	(4)	1,078
Net assets, beginning of year	23,647	5,617	3,478	32,742
Net assets, end of year	\$ 25,379	\$ 4,967	\$ 3,474	\$ 33,820

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)

<i>For the Year Ended June 30, 2016</i>	Program Services				Supporting Services			
	Program Ministry	Public Education	International Prison Ministry	Total	Management and General	Fundraising	Total	Total
Salaries and related expenses	\$ 11,630	\$ 1,506	\$ 18	\$ 13,154	\$ 2,311	\$ 1,238	\$ 3,549	\$ 16,703
Other expenses								
Consulting	1,092	185	-	1,277	153	107	260	1,537
Donations	1,551	3	2,715	4,269	-	-	-	4,269
Materials and supplies	1,509	51	-	1,560	96	53	149	1,709
Occupancy	300	45	-	345	138	38	176	521
Other	521	36	-	557	389	104	493	1,050
Postage	413	273	-	686	128	1,699	1,827	2,513
Printing	129	348	-	477	178	2,348	2,526	3,003
Professional fees	619	567	1	1,187	590	3,069	3,659	4,846
Repair and maintenance	125	30	1	156	65	22	87	243
Telephone	317	28	-	345	35	21	56	401
Travel	1,279	94	-	1,373	73	92	165	1,538
Total other expenses	19,485	3,166	2,735	25,386	4,156	8,791	12,947	38,333
Depreciation and amortization	451	38	-	489	91	33	124	613
Total expenses	\$ 19,936	\$ 3,204	\$ 2,735	\$ 25,875	\$ 4,247	\$ 8,824	\$ 13,071	\$ 38,946

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)

<i>For the Year Ended June 30, 2015</i>	Program Services				Supporting Services			
	Program Ministry	Public Education	International Prison Ministry	Total	Management and General	Fundraising	Total	Total
Salaries and related expenses	\$ 11,753	\$ 1,205	\$ 17	\$ 12,975	\$ 2,698	\$ 1,996	\$ 4,694	\$ 17,669
Other expenses								
Consulting	873	143	-	1,016	201	130	331	1,347
Donations	726	-	3,345	4,071	3	-	3	4,074
Materials and supplies	1,351	30	-	1,381	94	47	141	1,522
Occupancy	291	42	-	333	139	51	190	523
Other	425	23	-	448	340	111	451	899
Postage	429	309	-	738	134	1,588	1,722	2,460
Printing	126	380	-	506	183	2,229	2,412	2,918
Professional fees	364	794	-	1,158	500	2,571	3,071	4,229
Repair and maintenance	101	23	-	124	54	23	77	201
Telephone	294	26	-	320	51	38	89	409
Travel	1,350	97	-	1,447	76	156	232	1,679
Total other expenses	18,083	3,072	3,362	24,517	4,473	8,940	13,413	37,930
Depreciation and amortization	425	44	-	469	100	51	151	620
Total expenses	\$ 18,508	\$ 3,116	\$ 3,362	\$ 24,986	\$ 4,573	\$ 8,991	\$ 13,564	\$ 38,550

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)

<i>For the Years Ended June 30,</i>	2016	2015
Cash flows from operating activities		
Change in net assets	\$ 2,185	\$ 1,078
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation and amortization	613	620
Change in contributions receivable discount and allowance	(2)	(117)
Realized and unrealized loss (gains) on investments	212	(15)
Actuarial loss on annuity obligations	387	304
Loss (gain) on sale and disposal of property	3	(2)
Loss on impairment	310	-
Change in cash surrender value of life insurance policies	21	(4)
(Increase) decrease in:		
Contributions receivable	(448)	307
Program advances and other receivables	219	(76)
Prepaid expenses and other assets	68	(6)
Inventory of publications and supplies	134	10
Beneficial interest in trusts	34	7
Increase (decrease) in:		
Accounts payable and accrued expenses	(19)	(66)
Accrued salaries and benefits	(42)	(190)
Donor advances	35	-
Deferred revenue	8	(39)
Liability under trust agreements	(7)	(30)
Net cash provided by operating activities	3,711	1,781
Cash flows from investing activities		
Transfers from cash and cash equivalents held for long-term use	603	(1,604)
Acquisitions of property and equipment	(471)	(264)
Proceeds from sale of investments	11,747	9,519
Purchase of investments	(14,586)	(9,429)
Net cash used in investing activities	(2,707)	(1,778)
Cash flows from financing activities		
Proceeds from annuity agreements	142	89
Payment of annuity obligations	(624)	(622)
Repayment of line of credit	-	(150)
Net cash used in financing activities	(482)	(683)

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 (continued)
(\$ in Thousands)

<i>For the Years Ended June 30,</i>	2016	2015
Net change in cash and cash equivalents	522	(680)
Cash and cash equivalents, beginning of year	436	1,116
Cash and cash equivalents, end of year	\$ 958	\$ 436
Supplemental disclosures		
Cash paid for interest	\$ -	\$ 18
Noncash investing transactions		
Unsettled purchases of investment securities	\$ 871	\$ -

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

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

1. Organization and significant accounting policies

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

PFM is a national outreach to prisoners, former prisoners, and their families, and a leading advocate for criminal justice reform. PFM brings restoration to those affected by crime and incarceration in by facilitating prisoners’ transformation, supporting prisoners’ families and returning citizens, and advocating for a criminal justice system that reflects the God-given dignity and potential of each life. Through an awakening to new hope and life purpose, those who once broke the law are transformed and mobilized to serve their community, replacing the cycle of crime with a cycle of renewal.

PFM 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 (“P FMF”), which manages and administers planned giving programs to support Prison Fellowship Ministries. In addition, P FMF owns property in Lansdowne, Virginia used by Prison Fellowship Ministries as office space.

Prison Fellowship Ministries has control over the P FMF board and provides administrative and monetary support.

The consolidated financial statements presented here include the accounts of Prison Fellowship Ministries and P FMF (together, the “Organization,” the “Ministry,” and/or “PFM”). All significant intercompany transactions have been eliminated in consolidation.

Funding for PFM is obtained primarily from private contributors.

Effective January, 1, 2016, The Chuck Colson Center for Christian Worldview (“Colson Center”) became a separate unconsolidated entity. The Colson Center was formerly a program of PFM.

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

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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 Statements 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 Consolidated 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, 2016 and 2015, unrestricted net assets included \$70 of donor advised funds. These funds are unrestricted by the donor, but have been earmarked by the PFMF 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. Purchases and sales of investments are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Realized and unrealized gains (losses) include PFM's gains and losses on investments bought and sold as well as held during the year.

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 and liabilities 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;

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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. There have been no changes in the fair value methodologies used at June 30, 2016 and 2015.

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, 2016 and 2015, all contributions receivable are deemed fully collectable.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

Program advances and other receivables: 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%, 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.

Impairment of long-lived assets: The Organization periodically evaluates the carrying value of long-lived assets where events and circumstances warrant such a review. If the carry value exceeds the fair value an impairment loss is recorded.

During the year ending June 30, 2016, the Organization evaluated the balance of construction in progress and determined that internal use software costs previously incurred and capitalized were in excess of the estimated fair value due to additional costs being required to place the asset in service. An impairment loss of \$310 was recorded during the year ended June 30, 2016. No impairment loss was recorded for the year ended June 30, 2015.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

Internal-use software costs: The Organization capitalizes costs to develop software for internal use incurred during the application development stage. Costs related to preliminary project activities and post implementation activities are expensed as incurred. Once an application has reached the development stage, management has authorized and committed to the funding of the software project, it is probable the project will be completed and the software will be used to perform the function intended, internal and external costs, if direct and incremental, are capitalized until the application is substantially complete and ready for its intended use.

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 Statements of Activities and Changes in Net Assets for the change in the value and is included in the change in value of split-interest agreements.

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.

Donated securities: PFM classifies cash receipts from the sale of donated securities that upon receipt were converted nearly immediately into cash and contained no donor-imposed restrictions as cash flows from operations on the Consolidated Statements of Cash Flows, while cash receipts from the sale of donated securities with donor-imposed long-term restrictions are classified as financing activities. Otherwise, receipts from the sale of donated securities are classified as cash flows from investing activities.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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 fundraising projects – will have an effect on the overall allocation of costs between program services and supporting services. While it is the Ministry’s intention to minimize the funds expended toward supporting 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 - PFM staff and volunteers are in correctional facilities each day sharing the Gospel, spreading hope, and teaching life-changing classes. Through evangelism events, PFM introduces incarcerated men and women to a new future in Christ and nurtures their spiritual growth with Bible studies and intensive discipleship courses. PFM also offers a holistic set of life-skills classes, mentorship opportunities, and reentry programs to prepare prisoners to be leaders in their communities—whether inside or outside of prison. In the community, PFM recruits, trains, and equips churches and other organizations that participate in the Angel Tree program, which provides a pathway for incarcerated parents to restore and strengthen their relationships with their children and families. To help returning citizens, PFM connects those who have participated in in-prison programs with local churches and other community resources that assist with community re-integration.

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).

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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 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, 2016 and 2015, advertising costs approximated \$39 and \$24, 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 Prison Fellowship Ministries 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, Prison Fellowship Ministries and PFMF have made no provision for income taxes. Both Prison Fellowship Ministries and PFMF are classified as public charities.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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, 2016 and 2015, 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 2013 through the current year remain open for examination by tax authorities.

Subsequent events: Management has evaluated subsequent events for disclosure in these consolidated financial statements through October 14, 2016 which was the date the consolidated financial statements were available to be issued.

2. Investments

Investments (including assets held in charitable remainder trusts) as of June 30, 2016 and 2015, are as follows:

	2016	2015
Cash and equivalents held for long-term use	\$ 3,787	\$ 4,390
Money market funds	2	7
Equities	10,984	9,739
Mutual funds:		
Equity funds	361	381
Fixed income funds	240	289
Fixed income securities:		
Federal government bonds and notes	3,769	2,574
Mortgage backed securities	662	291
Corporate bonds	2,897	2,123
International bonds	349	359
Alternative investments:		
REIT	-	3
Land trusts	2	2
Total investments	\$ 23,053	\$ 20,158

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

	2016	2015
Investment income:		
Interest and dividends	\$ 361	\$ 290
Net realized and unrealized (loss) gain	(212)	15
Total investment income	\$ 149	\$ 305

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

3. Fair value

Certain investments and liabilities were recorded at fair value on a recurring basis as of June 30, 2016 based on the following level of hierarchy:

June 30, 2016	Fair Value Measurements			
	Total	Level 1	Level 2	Level 3
Beneficial interest in trusts	\$ 676	\$ -	\$ -	\$ 676
Charitable gift annuity liability	\$ (4,159)	\$ -	\$ -	\$ (4,159)
Investments:				
Money market funds	\$ 2	\$ 2	\$ -	\$ -
Equities	10,984	10,984	-	-
Mutual funds:				
Equity funds	361	361	-	-
Fixed income funds	240	240	-	-
Fixed income securities:				
Federal government bonds and notes	3,769	-	3,769	-
Mortgage backed securities	662	-	662	-
Corporate bonds	2,897	-	2,897	-
International bonds	349	-	349	-
Land trusts	2	-	-	2
Total investments	\$ 19,266	\$ 11,587	\$ 7,677	\$ 2

The following is a reconciliation of the beginning and ending balances for assets and liabilities measured at fair value using significant unobservable inputs (Level 3) during the period ended June 30, 2016:

	Land trusts	REIT	Beneficial interest in trusts	Charitable gift annuity liability
Beginning balance	\$ 2	\$ 3	\$ 710	\$ (4,254)
Change in value	-	-	(34)	-
Actuarial change	-	-	-	(387)
Sales	-	(3)	-	-
Additions	-	-	-	(142)
Payments	-	-	-	624
Ending balance	\$ 2	\$ -	\$ 676	\$ (4,159)

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

Certain investments and liabilities were recorded at fair value on a recurring basis as of June 30, 2015 based on the following level of hierarchy:

June 30, 2015	Total	Level 1	Level 2	Level 3
Beneficial interest in trusts	\$ 710	\$ -	\$ -	\$ 710
Charitable gift annuity liability	\$ (4,254)	\$ -	\$ -	\$ (4,254)
Investments:				
Money market funds	\$ 7	\$ 7	\$ -	\$ -
Equities	9,739	9,739	-	-
Mutual funds:				
Equity funds	381	381	-	-
Fixed income funds	289	289	-	-
Fixed income securities:				
Federal government bonds and notes	2,574	-	2,574	-
Mortgage backed securities	291	-	291	-
Corporate bonds	2,123	-	2,123	-
International bonds	359	-	359	-
Other investments:				
REIT	3	-	-	3
Land trusts	2	-	-	2
Total	\$ 15,768	\$ 10,416	\$ 5,347	\$ 5

The following is a reconciliation of the beginning and ending balances for assets and liabilities measured at fair value using significant unobservable inputs (Level 3) during the period ended June 30, 2015:

	Land trusts	REIT	Beneficial interest in trusts	Charitable gift annuity liability
Beginning balance	\$ 2	\$ 3	\$ 717	\$ (4,483)
Change in value	-	-	(7)	-
Actuarial change	-	-	-	(304)
Additions	-	-	-	(89)
Payments	-	-	-	622
Ending balance	\$ 2	\$ 3	\$ 710	\$ (4,254)

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

Level 2 values of federal, corporate and international bonds and mortgage backed securities are estimated using various techniques, which may consider recently executed transactions in securities of the issuer or comparable issuers, market price quotations (where observable), bond spreads, and fundamental data relating to the issuer.

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.

Level 3 charitable gift annuity liability is valued using the income approach, in the form of present value using an interest rate of 5% and the 2000 Individual Annuity Mortality Table ("IAMT").

The following table summarizes the valuation techniques and significant unobservable inputs used for PFM's significant assets and liabilities categorized within Level 3 of the fair value hierarchy at June 30, 2016 and 2015.

	Fair Value at 6/30/2016	Fair Value at 6/30/2015	Valuation techniques	Unobservable input	Range of significant input values
Beneficial interest in remainder trusts	\$ 458	\$ 473	Income approach Present value of future cash flows	Discount rate Life expectancy	6%, 4.9 – 7.6 years
Beneficial interest in perpetual trust	\$ 218	\$ 237	Income approach Present value of future cash flows	Fair value of assets contributed to the trust	N/A
Charitable gift annuity liability	\$ (4,159)	\$ (4,254)	Income approach Present value of future cash flows	Discount rates Life expectancy	5% - 6.5%, IRS 1983 table a / 2000 annuity tables

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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- 4. Contributions receivable** The following comprised contributions receivable as of June 30:

	2016	2015
Due in 1 year or less	\$ 740	\$ 242
Due in 1 to 5 years	-	50
Total gross contributions receivable	740	292
Less:		
Discounts on pledges due in 2 to 5 years	-	(2)
Contributions receivable, net	\$ 740	\$ 290

Contributions receivable are discounted to their present value using a rate of 1.83%.

As of June 30, 2016, three donors had contribution receivable balances outstanding which represented 85% of total gross contributions receivable.

As of June 30, 2015, one donor had a contribution receivable balance outstanding which represented 34% of total gross contributions receivable.

- 5. Conditional promises to give** For the years ended June 30, 2016 and 2015, PFM received conditional promises to give, totaling \$35 and \$124, respectively, designed to provide funds through matching contributions.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

6. Property, buildings and equipment

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

	2016	2015
Land	\$ 3,306	\$ 3,306
Building and improvements	19,080	19,575
Furniture and equipment	2,588	2,589
Vehicles	44	44
Computer hardware	809	731
Computer software	5,449	5,449
Total	31,276	31,694
Less: Accumulated depreciation and amortization	(15,124)	(15,103)
Total	16,152	16,591
Construction in progress	577	593
Property, buildings and equipment, net	\$ 16,729	\$ 17,184

Depreciation and amortization expense totaled \$613 and \$620, for the years ended June 30, 2016 and 2015, respectively.

Construction in progress consists of internal use software developed to be used with program and supporting services. Depreciation will begin once the software is completed and placed in service.

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 June 30, 2016 and 2015, based on an independent actuarial valuation, is \$4,159 and \$4,254, 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.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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. Total assets separately maintained as cash, cash equivalents and investments held by affiliate relating to charitable gift annuities totaled \$5,539 and \$6,442 as of June 30, 2016 and 2015, respectively. Asset balances at June 30, 2016 and 2015 exceeded the reserve requirements of the relevant regulatory bodies in all states that require a reserve fund and in which PFMF issues gift annuities.

Charitable trusts: As of June 30, 2016 and 2015, PFM maintained assets totaling \$185 and \$199, 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, 2016 and 2015 was \$69 and \$76, 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 \$458 and \$473, as of June 30, 2016 and 2015, 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 assets. 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 \$218 and \$237, as of June 30, 2016 and 2015, 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 assets. Distributions received from the trusts are recognized as unrestricted net assets unless purpose restricted by the donor.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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- 8. Line of credit** PFM has a line of credit that was renewed on March 22, 2016, totaling \$5,850, and is secured by a covenant not to encumber or convey PFMF's Lansdowne, Virginia real property. This agreement will expire on March 25, 2017. At June 30, 2016 and 2015, there was no outstanding balance on the line of credit. 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, 2016 and 2015. Under the terms of the line of credit agreement, PFM must maintain a minimum tangible net worth of \$25,000. PFM is in compliance with all debt covenants as of June 30, 2016 and 2015.
- 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. Cash held by financial institutions is insured by the Federal Deposit Insurance Corporation up to \$250. Investments held by financial institutions are insured by the Securities Investor Protection Corporation up to \$500, which includes up to \$250 protection for cash held in brokerage accounts. At June 30, 2016 and 2015, substantially all of PFM's cash, cash equivalents and investment balances were uninsured. For the composition of investment balances at June 30, 2016 and 2015, 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, 2016 and 2015. 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 \$364 and \$390 for the years ended June 30, 2016 and 2015, respectively.
- 11. Obligations under operating leases** PFM has entered into various operating lease agreements, primarily for office space and office equipment. Operating lease expenses incurred under these operating leases were \$74 and \$73 in 2016 and 2015, respectively.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

PFM's future minimum payments for the equipment under non-cancelable operating leases as of June 30, 2016, are as follows:

Year Ending June 30	Total
2017	\$ 30
2018	9
2019	1
Total	\$ 40

- 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 \$1,234 and \$1,141 in 2016 and 2015, respectively, and is included in other revenue on the Consolidated Statements of Activities and Changes in Net Assets.

PFM's future sublease receipts for the use of the facilities as of June 30, 2016, are as follows:

Year Ending June 30	Total
2017	\$ 1,200
2018	1,193
2019	966
2020	104
Total	\$ 3,463

- 13. Allocation of joint costs** During 2016 and 2015, PFM incurred joint costs of \$7,210 and \$7,003, 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:

	2016	2015
Program services	\$ 798	\$ 908
Supporting services:		
Fundraising	5,996	5,501
Management and general	416	594
Total	\$ 7,210	\$ 7,003

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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 as the criteria for control (determining consolidation) have not been met. 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.

The total amount of monetary support provided to PFI was \$2,715 and \$3,345 in 2016 and 2015, respectively. As of June 30, 2016 and 2015, PFM had a contribution payable due in less than one year to PFI of approximately \$94 and \$0, respectively, which is included in accounts payable in the accompanying Consolidated Statements of Financial Position. As of June 30, 2016 and 2015, PFI owed PFM, \$4 and \$30, 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 Statements of Financial Position.

16. Temporarily restricted net assets

Temporarily restricted net assets at June 30, 2016 and 2015, are as follows:

	2016	2015
Program assistance	\$ 4,769	\$ 3,483
Time restricted for periods after June 30	1,451	984
Cumulative unappropriated endowment income – time restricted	522	500
Total	\$ 6,742	\$ 4,967

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

For the years ended June 30, 2016 and 2015, net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by the passage of time releasing time restrictions:

	2016	2015
Program assistance	\$ 5,622	\$ 4,797
Time restrictions expired	119	384
Total	\$ 5,741	\$ 5,181

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, 2016 and 2015, totaled \$3,456 and \$3,474, respectively.

18. Endowment funds

The Organization had donor-restricted endowment funds totaling \$3,456 and \$3,474 at June 30, 2016 and 2015. 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:

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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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.

Endowment net assets composition by type of fund as of June 30, 2016:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ -	\$ 3,456	\$ 3,456
Endowment income reserved by Board for endowment	- -	522	-	522
Total funds	\$ -	\$ 522	\$ 3,456	\$ 3,978

Changes in endowment net assets for the fiscal year ended June 30, 2016:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ -	\$ 500	\$ 3,474	\$ 3,974
Investment return:				
Investment income	- -	64	-	64
Net depreciation (realized and unrealized)	- -	(42)	-	(42)
Total investment return	- -	22	-	22
Change in value of perpetual trusts	- -	-	(18)	(18)
Endowment net assets, end of year	\$ -	\$ 522	\$ 3,456	\$ 3,978

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

Endowment net assets composition by type of fund as of June 30, 2015:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ -	\$ 3,474	\$ 3,474
Endowment income reserved by Board for endowment	-	500	-	500
Total funds	\$ -	\$ 500	\$ 3,474	\$ 3,974

Changes in endowment net assets for the fiscal year ended June 30, 2015:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ -	\$ 507	\$ 3,478	\$ 3,985
Investment return:				
Investment income	-	51	-	51
Net depreciation (realized and unrealized)	-	(17)	-	(17)
Total investment return	-	34	-	34
Appropriations of endowment assets for expenditure	-	(41)	-	(41)
Change in value of perpetual trusts	-	-	(4)	(4)
Endowment net assets, end of year	\$ -	\$ 500	\$ 3,474	\$ 3,974

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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

	2016	2015
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	\$ 3,456	\$ 3,474
Temporarily restricted net assets		
The portion of perpetual endowment funds subject to a time restriction under UPMIFA and without purpose restrictions	\$ 522	\$ 500

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, 2016 and 2015.

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.

Prison Fellowship Ministries and Affiliate

Notes to Consolidated Financial Statements (\$ in Thousands)

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 \$283 and \$294 as of June 30, 2016 and 2015, respectively.