

The Heritage Society

Financial Statements
and Independent Accountants' Review Report
for the year ended May 31, 2017

The Heritage Society

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Independent Accountants' Review Report

To the Board of Directors of
The Heritage Society:

We have reviewed the accompanying financial statements of The Heritage Society, which comprise the statement of financial position as of May 31, 2017 and the related statements of activities, of functional expenses, and of cash flows for the year then ended, and the related notes to the financial statements. A review includes primarily applying analytical procedures to management's financial data and making inquiries of management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the financial statements as a whole. Accordingly, we do not express such an opinion.

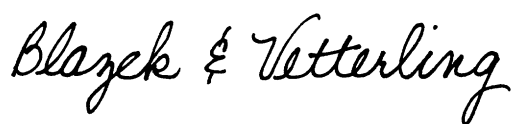
Management's Responsibility for the Financial Statements – Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance 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.

Accountants' Responsibility – Our responsibility is to conduct the review engagement in accordance with Statements on Standards for Accounting and Review Services promulgated by the Accounting and Review Services Committee of the American Institute of Certified Public Accountants. Those standards require us to perform procedures to obtain limited assurance as a basis for reporting whether we are aware of any material modifications that should be made to the financial statements for them to be in accordance with accounting principles generally accepted in the United States of America. We believe that the results of our procedures provide a reasonable basis for our conclusion.

Accountants' Conclusion – Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter – The accompanying financial statements have been prepared assuming that The Heritage Society will continue as a going concern. As discussed in Note 13 to the financial statements, The Heritage Society has experienced recurring deficits that have required borrowing on their line of credit and of certain restricted funds. The deficit in unrestricted net assets raises an uncertainty about its ability to continue as a going concern. Management's plans regarding this matter are described in Note 13. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our conclusion is not modified with respect to this matter.

Financial Statements for the Year Ended May 31, 2016 – The financial statements for the year ended May 31, 2016 were audited by us, and we expressed an unqualified opinion on them in our report dated August 25, 2016, but we have not performed any auditing procedures since that date.



September 19, 2017

The Heritage Society

Statements of Financial Position as of May 31, 2017 and 2016

	REVIEWED <u>2017</u>	AUDITED <u>2016</u>
ASSETS		
Cash	\$ 542,826	\$ 589,819
Pledges receivable	131,068	67,330
Inventory	110,001	11,485
Prepaid and other assets	3,653	1,740
Property and equipment, net (<i>Note 4</i>)	74,970	24,529
Investments (<i>Note 5</i>)	821,043	912,459
Collections (<i>Note 6</i>)	<u>0</u>	<u>0</u>
TOTAL ASSETS	<u>\$ 1,683,561</u>	<u>\$ 1,607,362</u>
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable and accrued expenses	\$ 118,756	\$ 89,870
Deferred revenue	7,805	23,575
Line of credit (<i>Note 7</i>)	<u>199,500</u>	<u>197,500</u>
Total liabilities	<u>326,061</u>	<u>310,945</u>
Commitments (<i>Note 11</i>)		
Net assets (<i>Note 9</i>):		
Unrestricted (<i>Note 13</i>)	(432,651)	(464,439)
Temporarily restricted (<i>Note 8</i>)	697,707	668,412
Permanently restricted	<u>1,092,444</u>	<u>1,092,444</u>
Total net assets	<u>1,357,500</u>	<u>1,296,417</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 1,683,561</u>	<u>\$ 1,607,362</u>

See accompanying notes to financial statements and independent accountants' review report.

The Heritage Society

Statement of Activities for the year ended May 31, 2017 (Reviewed)

	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>PERMANENTLY RESTRICTED</u>	<u>TOTAL</u>
REVENUE:				
Contributions (<i>Note 10</i>)	\$ 487,461	\$ 260,300		\$ 747,761
Fundraising events	129,245			129,245
Direct donor benefits of fundraising events	(16,531)			(16,531)
Admissions and tours	61,823			61,823
Facility rental income	57,114			57,114
Investment return, net (<i>Note 5</i>)	42,092	46,542		88,634
Other income	<u>14,087</u>			<u>14,087</u>
Total revenue	775,291	306,842		1,082,133
Net assets released from restrictions:				
Expenditures for program purposes	<u>277,547</u>	<u>(277,547)</u>		
Total	<u>1,052,838</u>	<u>29,295</u>		<u>1,082,133</u>
EXPENSES:				
Program services	924,124			924,124
Management and general	159,811			159,811
Fundraising	<u>107,247</u>			<u>107,247</u>
Total expenses	<u>1,191,182</u>			<u>1,191,182</u>
CHANGES IN NET ASSETS BEFORE ACQUISITION	(138,344)	29,295		(109,049)
Fair value of Houston Arts & Media net assets acquired (<i>Note 2</i>)	<u>170,132</u>			<u>170,132</u>
CHANGES IN NET ASSETS	31,788	29,295		61,083
Net assets, beginning of year	<u>(464,439)</u>	<u>668,412</u>	<u>\$ 1,092,444</u>	<u>1,296,417</u>
Net assets, end of year	<u>\$ (432,651)</u>	<u>\$ 697,707</u>	<u>\$ 1,092,444</u>	<u>\$ 1,357,500</u>

See accompanying notes to financial statements and independent accountants' review report.

The Heritage Society

Statement of Activities for the year ended May 31, 2016 (Audited)

	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>PERMANENTLY RESTRICTED</u>	<u>TOTAL</u>
REVENUE:				
Contributions (<i>Note 10</i>)	\$ 458,636	\$ 330,837		\$ 789,473
Fundraising events	20,138			20,138
Admissions and tours	90,479			90,479
Facility rental income	32,713			32,713
Investment return, net (<i>Note 5</i>)	(42,092)			(42,092)
Other income	<u>7,785</u>	<u> </u>		<u>7,785</u>
Total revenue	567,659	330,837		898,496
Net assets released from restrictions:				
Expenditures for program purposes	272,318	(272,318)		
Expiration of time restrictions	<u>28,750</u>	<u>(28,750)</u>		<u> </u>
Total	<u>868,727</u>	<u>29,769</u>		<u>898,496</u>
EXPENSES:				
Program services	1,055,664			1,055,664
Management and general	137,804			137,804
Fundraising	<u>56,072</u>			<u>56,072</u>
Total expenses	<u>1,249,540</u>			<u>1,249,540</u>
CHANGES IN NET ASSETS	(380,813)	29,769		(351,044)
Net assets, beginning of year	<u>(83,626)</u>	<u>638,643</u>	<u>\$ 1,092,444</u>	<u>1,647,461</u>
Net assets, end of year	<u>\$ (464,439)</u>	<u>\$ 668,412</u>	<u>\$ 1,092,444</u>	<u>\$ 1,296,417</u>

See accompanying notes to financial statements and independent accountants' review report.

The Heritage Society

Statement of Functional Expenses for the year ended May 31, 2017 (Reviewed)

	PROGRAM SERVICES	MANAGEMENT AND GENERAL	FUNDRAISING	TOTAL
Salaries and related taxes and benefits	\$ 546,456	\$ 79,625	\$ 65,246	\$ 691,327
Professional fees and contract services	58,122	46,588	4,190	108,900
Historic home restoration and repair	106,913			106,913
Occupancy	53,208	3,563	3,563	60,334
Materials and supplies	37,873	1,875	10,053	49,801
Equipment rental and maintenance	27,326	660	5,250	33,236
Insurance	19,178	5,948		25,126
Event catering	13,620	233	8,980	22,833
Telephone and technology	19,857	1,330	1,038	22,225
Interest, bank and credit card fees	110	17,579		17,689
Depreciation	13,261	1,079	876	15,216
Printing and publications	6,259		4,885	11,144
Advertising and promotion	10,242		300	10,542
Postage and handling	2,715	125	2,522	5,362
Other	8,984	1,206	344	10,534
Total expenses	<u>\$ 924,124</u>	<u>\$ 159,811</u>	<u>\$ 107,247</u>	1,191,182
Custodial and investment advisory fees				<u>11,322</u>
Total				<u>\$ 1,202,504</u>

See accompanying notes to financial statements and independent accountants' review report.

The Heritage Society

Statement of Functional Expenses for the year ended May 31, 2016 (Audited)

	PROGRAM SERVICES	MANAGEMENT AND GENERAL	FUNDRAISING	TOTAL
Salaries and related taxes and benefits	\$ 540,782	\$ 84,058	\$ 37,769	\$ 662,609
Professional fees and contract services	26,103	23,609	1,620	51,332
Historic home restoration and repair	212,804			212,804
Occupancy	57,887	4,629	4,548	67,064
Materials and supplies	20,054	954	1,567	22,575
Equipment rental and maintenance	121,249	602	602	122,453
Insurance	18,799	6,176		24,975
Event catering	13,953	716	122	14,791
Telephone and technology	19,762	1,080	1,650	22,492
Interest, bank and credit card fees		13,209		13,209
Depreciation	8,514	1,139	935	10,588
Printing and publications	4,142		3,500	7,642
Advertising and promotion	5,508			5,508
Postage and handling	2,446	95	2,636	5,177
Other	<u>3,661</u>	<u>1,537</u>	<u>1,123</u>	<u>6,321</u>
Total expenses	<u>\$ 1,055,664</u>	<u>\$ 137,804</u>	<u>\$ 56,072</u>	1,249,540
Custodial and investment advisory fees				<u>10,708</u>
Total				<u>\$ 1,260,248</u>

See accompanying notes to financial statements and independent accountants' review report.

The Heritage Society

Statements of Cash Flows for the years ended May 31, 2017 and 2016

	REVIEWED <u>2017</u>	AUDITED <u>2016</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	\$ 61,083	\$ (351,044)
Adjustments to reconcile changes in net assets to net cash used by operating activities:		
Net noncash assets acquired at fair value	(123,020)	
Net realized and unrealized (gain) loss on investments	(81,589)	56,947
Depreciation	15,217	10,588
Changes in operating assets and liabilities:		
Pledges receivable	(63,738)	228,322
Inventory	4,084	(1,643)
Prepaid and other assets	(1,913)	174
Accounts payable and accrued expenses	28,886	(1,544)
Deferred revenue	<u>(15,770)</u>	<u>15,750</u>
Net cash used by operating activities	<u>(176,760)</u>	<u>(42,450)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments	(8,192)	(618,599)
Proceeds from sales and maturities of investments	172,602	765,460
Net sale of money market mutual funds	8,595	21,913
Purchases of property and equipment	<u>(45,238)</u>	<u>(2,120)</u>
Net cash provided by investing activities	<u>127,767</u>	<u>166,654</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Advances on line of credit	57,000	137,000
Payments on line of credit	<u>(55,000)</u>	<u>(37,500)</u>
Net cash provided by financing activities	<u>2,000</u>	<u>99,500</u>
NET CHANGE IN CASH	(46,993)	223,704
Cash, beginning of year	<u>589,819</u>	<u>366,115</u>
Cash, end of year	<u>\$ 542,826</u>	<u>\$ 589,819</u>

See accompanying notes to financial statements and independent accountants' review report.

The Heritage Society

Notes to Financial Statements for the years ended May 31, 2017 (Reviewed) and 2016 (Audited)

NOTE 1 – ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES

Organization – The Heritage Society (THS), a museum complex at Sam Houston Park, was incorporated in 1954 as a nonprofit corporation. THS collects, preserves, exhibits, and celebrates the diverse history of the Houston region. THS maintains ten historic buildings located in Sam Houston Park that are owned by the City of Houston. THS' collection on display in the historic homes and a museum gallery consists of furniture, household articles and textiles, art, archives and photographs that provide unique insight into the history of Houstonians. THS is supported by voluntary contributions of time and money from members and the community in connection with fundraising campaigns and events and by gifts of historical items.

Federal income tax status – THS is exempt from federal income tax under §501(c)(3) of the Internal Revenue Code and is classified as a public charity under §509(a)(2).

Cash concentration – Bank deposits exceed the federally insured limit per depositor per institution.

Pledges receivable that are expected to be collected within one year are reported at net realizable value. Amounts expected to be collected in more than one year are discounted, if material, to estimate the present value of future cash flows. At May 31, 2017, all pledges receivable are expected to be collected within one year.

Inventory consists primarily of videos and other items available for sale in the gift shop. Inventory is valued at the lower of cost or net realizable value.

Property and equipment is reported at cost if purchased and at estimated fair value at the date of contribution if donated. Depreciation is computed using the straight-line method over estimated useful lives of 3 to 25 years. Restoration and repairs of historic homes belonging to the City of Houston are expensed as incurred.

Investments are reported at fair value. Investment return is reported in the statement of activities as an increase in unrestricted net assets unless the use of the income is limited by donor-imposed restrictions. Investment return whose use is restricted by the donor is reported as an increase in temporarily restricted net assets until expended in accordance with donor-imposed restrictions.

Collections – Collections, which were acquired through purchases and contributions, are not recognized as assets in the statement of financial position. Purchases of collection items are recognized as decreases in unrestricted net assets in the year in which the items are acquired or as decreases in temporarily restricted net assets if the assets used to purchase the items are restricted by donors. Contributed collection items are not reflected in the financial statements. Proceeds from deaccessions or insurance recoveries are reflected as increases in the appropriate net asset classes.

Net asset classification – Contributions, investment return, and the related net assets are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Unrestricted net assets* include those net assets whose use is not restricted by donor-imposed stipulations even though their use may be limited in other respects such as by contract or board designation.

- *Temporarily restricted net assets* include contributions and investment return restricted by the donor for specific purposes or time periods. When a purpose restriction is accomplished or a time restriction ends, temporarily restricted net assets are released to unrestricted net assets.
- *Permanently restricted net assets* include contributions that donors have restricted in perpetuity. Investment return from these funds is donor-restricted to support the maintenance of historical structures, grounds, and collections.

Contributions are recognized as revenue at estimated fair value when an unconditional commitment is received from the donor. Contributions received with donor stipulations that limit the use of the donated assets are classified as restricted support. Conditional contributions are recognized in the same manner when the conditions are substantially met.

Non-cash contributions – Donated materials and use of facilities are recognized at fair value as contributions when an unconditional commitment is received from a donor. The related expense is recognized as the item is used. Contributions of services are recognized when services received (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation.

Admission and tour fees are recognized when services are provided.

Facility rental income is recognized when services are provided. Amounts received in advance are reflected as deferred revenue in the statement of financial position.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts of reported revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

NOTE 2 – ACQUISITION OF HOUSTON ARTS & MEDIA

Effective October 1, 2016, the Board of Directors of Houston Arts & Media amended and restated its bylaws giving THS Board of Directors the exclusive right and power to elect, appoint, remove and replace the directors and officers of Houston Arts & Media and to amend its bylaws. The partnership between THS, which collects, preserves, exhibits, and celebrates the diverse history of the Houston region and Houston Arts & Media, which produces film, video, books, web content and other media projects that address themes in Texas and Houston, will fulfill their common missions of preserving the stories of the Houston region.

No consideration was transferred as part of the acquisition, no liabilities were assumed, and no significant acquisition costs were incurred by THS. Houston Arts & Media had no conditional promises to give outstanding as of the date of acquisition. The fair value of assets acquired at October 1, 2016 consist of the following:

Fair value of assets acquired:

Cash	\$ 47,112
Property and equipment	20,420
Inventory	<u>102,600</u>

Fair value of net assets acquired	<u>\$ 170,132</u>
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NOTE 3 – AGREEMENT WITH THE CITY OF HOUSTON

THS operates the museum and ten historical structures located in Sam Houston Park (the Park) under an agreement with the City of Houston (the City). The agreement is subject to certain restrictions set by the City, and THS does not have exclusive use of the land. The current agreement terminates in June 2039. Titles to all buildings located in the Park are vested in the City. Titles to newly acquired buildings are transferred to the City within 15 days of completed installation.

NOTE 4 – PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	<u>2017</u>	<u>2016</u>
Gallery and exhibition fixtures	\$ 162,253	\$ 162,253
Furniture and equipment	<u>243,006</u>	<u>217,156</u>
Total property and equipment, at cost	405,259	379,409
Accumulated depreciation	<u>(330,289)</u>	<u>(354,880)</u>
Property and equipment, net	<u>\$ 74,970</u>	<u>\$ 24,529</u>

NOTE 5 – INVESTMENTS AND FAIR VALUE MEASUREMENTS

Generally accepted accounting principles require that certain assets and liabilities be reported at fair value and establish a hierarchy that prioritizes inputs used to measure fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The three levels of the fair value hierarchy are as follows:

- *Level 1* – Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date.
- *Level 2* – Inputs are other than quoted prices included in Level 1, which are either directly observable or can be derived from or corroborated by observable market data at the reporting date.
- *Level 3* – Inputs are not observable and are based on the reporting entity's assumptions about the inputs market participants would use in pricing the asset or liability.

Assets measured at fair value at May 31, 2017 are as follows:

	<u>LEVEL 1</u>	<u>LEVEL 2</u>	<u>LEVEL 3</u>	<u>TOTAL</u>
Investments:				
Equity securities:				
Large-cap exchange-traded funds	\$ 239,900			\$ 239,900
International developed:				
Mutual funds	126,984			126,984
Exchange-traded funds	54,169			54,169
Small-cap mutual funds	90,834			90,834
Mid-cap exchange-traded funds	52,912			52,912
Fixed-income securities:				
Corporate and other bonds		\$ 181,049		181,049
Global real estate index mutual fund	52,255			52,255
Money market mutual funds	<u>22,940</u>	<u> </u>	<u> </u>	<u>22,940</u>
Total assets measured at fair value	<u>\$ 639,994</u>	<u>\$ 181,049</u>	<u>\$ 0</u>	<u>\$ 821,043</u>

Assets measured at fair value at May 31, 2016 are as follows:

	<u>LEVEL 1</u>	<u>LEVEL 2</u>	<u>LEVEL 3</u>	<u>TOTAL</u>
Investments:				
Equity securities:				
Large-cap exchange-traded funds	\$ 261,075			\$ 261,075
International developed:				
Mutual funds	144,963			144,963
Exchange-traded funds	47,872			47,872
Small-cap mutual funds	85,603			85,603
Mid-cap exchange-traded funds	51,027			51,027
Fixed-income securities:				
Corporate and other bonds		\$ 238,187		238,187
Global real estate index mutual fund	52,197			52,197
Money market mutual funds	<u>31,535</u>			<u>31,535</u>
Total assets measured at fair value	<u>\$ 674,272</u>	<u>\$ 238,187</u>	<u>\$ 0</u>	<u>\$ 912,459</u>

Valuation methods used for assets measured at fair value are as follows:

- *Exchange-traded funds* are valued at the closing price reported on the active market on which the individual securities are traded.
- *Mutual funds* are valued at the reported net asset value.
- *Fixed-income securities* are valued using prices obtained from independent quotation bureaus that use computerized valuation formulas to calculate fair values.

These valuation methods may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while THS believes its valuation methods are appropriate, the use of different methods or assumptions could result in a different fair value measurement at the reporting date.

Investments are exposed to various risks such as interest rate, market, and credit risks. Because of these risks, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position and statement of activities.

Investment return consists of the following:

	<u>2017</u>	<u>2016</u>
Interest and dividends	\$ 18,367	\$ 25,563
Net realized and unrealized gain (loss) on investments	81,589	(56,947)
Custodial and investment advisory fees	<u>(11,322)</u>	<u>(10,708)</u>
Investment return, net	<u>\$ 88,634</u>	<u>\$ (42,092)</u>

NOTE 6 – COLLECTIONS

THS' collections are made up of historical artifacts that are held for educational, research, and curatorial purposes. Each of the items is catalogued, preserved, and cared for, and activities verifying existence and assessing the condition are performed periodically. The collections are subject to a policy that requires proceeds from the sale or other disposition of collection items to be used to acquire other items for the collections. Proceeds from sales of collection items that were contributed with restrictions are

reflected as an increase in temporarily restricted net assets in the statement of activities. During 2017 and 2016, various collection items including paper archival materials, furniture, housewares, and other accessories were deaccessioned from the permanent collection.

NOTE 7 – LINE OF CREDIT

THS has a \$200,000 unsecured line of credit with a bank, which matures on November 30, 2017. Amounts outstanding under the line bear interest at prime rate plus 2.0% (5.5% at May 31, 2017). Interest expense recognized and paid was approximately \$11,200 in 2017 and \$7,200 in 2016.

NOTE 8 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes:

	<u>2017</u>	<u>2016</u>
Maintenance of historical structures	\$ 542,139	\$ 534,813
Museum collections	110,886	110,886
Time-restricted for future operations	5,000	5,000
Other	<u>39,682</u>	<u>17,713</u>
Total temporarily restricted net assets	<u>\$ 697,707</u>	<u>\$ 668,412</u>

NOTE 9 – ENDOWMENT FUNDS

THS maintains an endowment fund comprised of donor-restricted endowment funds, which are maintained in accordance with explicit donor stipulations. The endowment funds are invested to support maintenance of historical structures, grounds and collections.

The Board of Directors (the Board) has interpreted the Texas Uniform Prudent Management of Institutional Funds Act (TUPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, THS classifies the amount specified by explicit donor stipulation as endowments as permanently restricted net assets. This amount is not reduced by losses on investments in the endowment funds or by approved appropriations for expenditure from the funds. The portion of the donor-restricted endowment funds not classified as permanently restricted net assets is classified as temporarily restricted net assets until appropriated for expenditure. Temporarily restricted net assets are reclassified to unrestricted net assets for the amount appropriated when the purpose restriction has been met. In accordance with TUPMIFA, THS considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the funds
- The purposes of THS and the donor-restricted endowment funds
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of THS
- The investment policies of THS

Endowment funds are maintained in a separate investment account, which is managed by an independent financial firm that follows guidance provided in an investment policy approved by the Board. The Board approves appropriations for expenditures of endowment funds as part of the annual budget, or as needed.

THS' investment policy attempts to provide a predictable stream of funding for maintenance while seeking to maintain the purchasing power of the endowment assets. To satisfy its long-term rate-of-return objectives, THS 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). THS targets a diversified asset allocation that places a greater emphasis on a blend of equity-based investments and fixed-income investments to achieve its long-term return objectives within prudent risk constraints.

The fair value of investments associated with individual donor-restricted endowment funds, at times, may fall below donor-stipulated or TUPMIFA-required levels. Such deficiencies result from unfavorable market fluctuations and/or continued appropriations deemed prudent by the Board. There were no such deficiencies at May 31, 2017. At May 31, 2016, such deficiencies were \$42,092 and are reflected as a reduction of unrestricted net assets.

Endowment net asset composition at May 31, 2017:

	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>PERMANENTLY RESTRICTED</u>	<u>TOTAL</u>
Donor-restricted endowment funds	\$ <u>0</u>	\$ <u>46,542</u>	\$ <u>1,092,444</u>	\$ <u>1,138,986</u>

Endowment net asset composition at May 31, 2016:

	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>PERMANENTLY RESTRICTED</u>	<u>TOTAL</u>
Donor-restricted endowment funds	\$ <u>(42,092)</u>	\$ <u>0</u>	\$ <u>1,092,444</u>	\$ <u>1,050,352</u>

Changes in net assets of the endowment funds are as follows:

	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>PERMANENTLY RESTRICTED</u>	<u>TOTAL</u>
Endowment net assets, May 31, 2015	\$ <u>0</u>	\$ <u>0</u>	\$ <u>1,092,444</u>	\$ <u>1,092,444</u>
Investment return:				
Interest and dividends	25,563			25,563
Net realized and unrealized loss	(56,947)			(56,947)
Investment management fees	<u>(10,708)</u>			<u>(10,708)</u>
Net investment return	<u>(42,092)</u>			<u>(42,092)</u>
Endowment net assets, May 31, 2016	<u>(42,092)</u>	<u>0</u>	<u>1,092,444</u>	<u>1,050,352</u>
Investment return:				
Interest and dividends	8,722	9,645		18,367
Net realized and unrealized gain	38,746	42,843		81,589
Investment management fees	<u>(5,376)</u>	<u>(5,946)</u>		<u>(11,322)</u>
Net investment return	<u>42,092</u>	<u>46,542</u>		<u>88,634</u>
Endowment net assets, May 31, 2017	\$ <u>0</u>	\$ <u>46,542</u>	\$ <u>1,092,444</u>	\$ <u>1,138,986</u>

NOTE 10 – IN-KIND CONTRIBUTIONS

During 2017 and 2016, THS recognized approximately \$65,000 and \$161,000, respectively, of contributed printing, advertising, educational services, and historic house utilities and maintenance. These amounts are recognized as contributions and primarily as program expenses in the accompanying statement of activities.

NOTE 11 – COMMITMENTS

During 2015, THS entered into a restoration contract for the Kellum-Noble property. At May 31, 2017, approximately \$34,300 of the contracted restoration work had not yet been completed.

NOTE 12 – RETIREMENT PLAN

THS maintains a §401(k) retirement savings plan for its employees. The plan allows eligible employees to contribute a portion of their earnings each plan year subject to certain Internal Revenue Service limitations and defer federal income taxes on the contributions. THS makes contributions to the plan for each employee equal to 3% of their salary. During 2017 and 2016, THS contributed \$13,700 and \$13,697, respectively, to the plan.

NOTE 13 – UNRESTRICTED NET ASSETS AND MANAGEMENT'S PLANS

Unrestricted net assets are as follows:

	<u>2017</u>	<u>2016</u>
Cumulative unrestricted deficits	\$ (432,651)	\$ (422,347)
Aggregate deficiency of endowment investments	<u> </u>	<u>(42,092)</u>
Unrestricted net asset deficit	<u>\$ (432,651)</u>	<u>\$ (464,439)</u>

During 2017, the aggregate deficiency of endowment investments was restored from positive net investment return.

In recent years, THS has experienced cumulative unrestricted deficits that have been financed through a line of credit with a bank with a balance of \$199,500 at May 31, 2017 and by Board-approved internal borrowing of THS's temporarily restricted museum collection funds and donor-restricted endowment funds, which totaled approximately \$433,000 at May 31, 2017. The primary cause of this deficit is THS's funding of the regular maintenance of and major repairs to the City of Houston-owned historic buildings THS operates in Sam Houston Park. The City provides no funding for expenditures such as roofs, HVAC systems, paint, carpentry, alarm monitoring, insurance, pest control, preservation planning, etc. For the five years ending May 31, 2017, these costs exceeded \$557,000.

While management and the Board have implemented strategies to increase revenue, reduce expenses, and manage cash flows over the past few years, the primary focus over the past twelve months has been on securing funding from the City to support maintenance and repair of the city-owned buildings. An amendment to the City's fiscal year end 2018 budget recently passed to explore the possibility of funding through third party events held in Sam Houston Park. Additionally, conversations are ongoing with City

Council members, the Mayor, and Houston First Corporation regarding funding for the city-owned assets operated by THS. THS is currently engaged in a Houston First Corporation-funded strategic planning project to support these efforts.

NOTE 14 – SUBSEQUENT EVENTS

Management has evaluated subsequent events through September 19, 2017, which is the date that the financial statements were available for issuance. In August 2017, THS sustained damages from Hurricane Harvey. Evaluation of the extent of damage has not been completed and an estimate of the amount of loss is not possible at this time. No other events were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.
