

**ZUMIX, INC. AND AFFILIATE**

Consolidated Financial Statements  
and Supplementary Information

March 31, 2017 and 2016

(With Independent Auditors' Report Thereon)



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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
ZUMIX, Inc.:

### **Report on the Consolidated Financial Statements**

We have audited the accompanying consolidated financial statements of ZUMIX, Inc. and its affiliate (together the "Organization"). These comprise the consolidated statements of financial position as of March 31, 2017 and 2016, the related consolidated statements of cash flows for the years then ended, the related consolidated statements of activities and changes in net assets and functional expenses for the year ended March 31, 2017, 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.

### ***Auditors' 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.

### ***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Organization as of March 31, 2017 and 2016, and the change in its net assets and its cash flows for the year ended March 31, 2017 in accordance with accounting principles generally accepted in the United States of America.

### ***Other Matter***

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary consolidating statement of financial position as of March 31, 2017, the supplementary consolidating statement of activities and changes in net assets for the year then ended and the supplementary consolidating statement of cash flows for the year then ended are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

### **Report on Summarized Comparative Information**

We have previously audited the Organization's March 31, 2016 consolidated financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated November 15, 2016. In our opinion, the summarized comparative information presented herein as of and for the year ended March 31, 2016 is consistent, in all material respects, with the audited financial statements from which it has been derived.

*Nardella + Taylor, LLP*

November 10, 2017

# ZUMIX, INC. AND AFFILIATE

## Consolidated Statements of Financial Position

March 31, 2017 and 2016

	<u>2017</u>	<u>2016</u>
<i>Assets</i>		
Current assets:		
Cash and cash equivalents	\$ 666,816	\$ 553,440
Amounts held for others	32,242	6,841
Amounts held in escrow, current	-	130,000
Contributions receivable, net	137,762	195,807
Prepaid expenses and other current assets	28,991	30,219
	<u>865,811</u>	<u>916,307</u>
Total current assets	<u>865,811</u>	<u>916,307</u>
Property and equipment, net	2,912,417	3,038,491
Deferred debt issuance costs, net	-	44,064
	<u>-</u>	<u>44,064</u>
Total assets	<u>\$ 3,778,228</u>	<u>\$ 3,998,862</u>
<i>Liabilities and Net Assets</i>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 48,393	\$ 32,629
Amounts held for others	32,242	6,841
	<u>80,635</u>	<u>39,470</u>
Total current liabilities	<u>80,635</u>	<u>39,470</u>
Deferred income	-	588,677
Mortgage notes payable, net	-	331,323
	<u>-</u>	<u>331,323</u>
Total liabilities	<u>80,635</u>	<u>959,470</u>
Net assets:		
Unrestricted	3,577,191	2,797,186
Temporarily restricted	120,402	242,206
	<u>3,697,593</u>	<u>3,039,392</u>
Total net assets	<u>3,697,593</u>	<u>3,039,392</u>
Total liabilities and net assets	<u>\$ 3,778,228</u>	<u>\$ 3,998,862</u>

*The accompanying notes are an integral part of these financial statements.*

## ZUMIX, INC. AND AFFILIATE

### Consolidated Statement of Activities and Changes in Net Assets

For the Year Ended March 31, 2017 (With Comparative Totals for 2016)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Totals 2017</u>	<u>2016</u>
Support and revenue:				
Individual donations	\$ 106,148	\$ -	\$ 106,148	\$ 84,261
In-kind donations	64,861	-	64,861	59,873
Corporate donations	55,892	-	55,892	35,927
Foundation donations	507,918	120,167	628,085	768,555
Events	44,323	-	44,323	43,473
Government grants	82,993	-	82,993	74,559
Program fees	152,664	-	152,664	146,587
Interest income	4,837	-	4,837	39,754
Amortization of deferred income				
from below-market interest rate loans	16,663	-	16,663	96,820
Rental income	37,557	-	37,557	24,905
Sale of product	4,493	-	4,493	9,273
Net gain on extinguishment of debt	876,894	-	876,894	817,618
Other income	-	-	-	1,485
Net assets released from restriction	241,971	(241,971)	-	-
	<u>2,197,214</u>	<u>(121,804)</u>	<u>2,075,410</u>	<u>2,203,090</u>
Total support and revenue				
Expenses:				
Youth programs	1,080,764	-	1,080,764	1,118,750
Community arts program	132,685	-	132,685	132,654
Total program expenses	<u>1,213,449</u>	<u>-</u>	<u>1,213,449</u>	<u>1,251,404</u>
Management and general	118,004	-	118,004	102,802
Fundraising	85,756	-	85,756	91,500
	<u>1,417,209</u>	<u>-</u>	<u>1,417,209</u>	<u>1,445,706</u>
Total expenses				
Increase (decrease) in net assets	780,005	(121,804)	658,201	757,384
Net assets, beginning of year	<u>2,797,186</u>	<u>242,206</u>	<u>3,039,392</u>	<u>2,282,008</u>
Net assets, end of year	<u>\$ 3,577,191</u>	<u>\$ 120,402</u>	<u>\$ 3,697,593</u>	<u>\$ 3,039,392</u>

*The accompanying notes are an integral part of these financial statements.*

## ZUMIX, INC. AND AFFILIATE

### Consolidated Statement of Functional Expenses

For the Year Ended March 31, 2017 (With Comparative Totals for 2016)

	Youth Programs	Community Arts	Total Program Services	Management and General	Fundraising	2017 Totals	2016 Totals
Salaries	\$ 403,705	\$ 63,652	\$ 467,357	\$ 36,338	\$ 52,307	\$ 556,002	\$ 516,117
Youth stipends	9,148	6,170	15,318	-	110	15,428	22,535
Employee benefits	31,775	5,065	36,840	19,368	1,428	57,636	50,849
Payroll taxes	33,132	4,982	38,114	2,943	4,418	45,475	43,922
<b>Total salaries and related expenses</b>	<b>477,760</b>	<b>79,869</b>	<b>557,629</b>	<b>58,649</b>	<b>58,263</b>	<b>674,541</b>	<b>633,423</b>
Consulting	271,033	25,838	296,871	29,577	6,634	333,082	309,138
Professional development	9,288	543	9,831	3,391	2,089	15,311	11,014
Bank fees and payroll fees	532	314	846	7,055	520	8,421	5,398
Advertising	462	1,821	2,283	63	400	2,746	4,043
Marketing and printing	6,809	3,789	10,598	614	876	12,088	17,978
Bad debt expense	-	-	-	-	-	-	1,050
Supplies	4,622	813	5,435	367	290	6,092	7,869
Telephone and network	14,090	1,176	15,266	1,762	1,419	18,447	18,220
Postage and shipping	867	164	1,031	216	201	1,448	2,787
Rent	6,000	4,800	10,800	600	600	12,000	300
Equipment rental, maintenance and purchases	45,910	2,489	48,399	192	723	49,314	12,941
Facilities maintenance and repair	33,419	4,176	37,595	-	2,136	39,731	50,817
	2,728	895	3,623	10	-	3,633	5,454
Meetings	8,306	2,993	11,299	2,266	803	14,368	11,148
Insurance	10,904	806	11,710	1,352	1,352	14,414	15,117
Utilities	18,694	2,199	20,893	1,161	1,161	23,215	22,276
Depreciation	153,481	-	153,481	9,848	5,411	168,740	170,927
Vehicle expense	-	-	-	-	-	-	88
Interest expense	15,859	-	15,859	881	881	17,621	145,718
Other expenses	-	-	-	-	1,997	1,997	-
	<b>\$ 1,080,764</b>	<b>\$ 132,685</b>	<b>\$ 1,213,449</b>	<b>\$ 118,004</b>	<b>\$ 85,756</b>	<b>\$ 1,417,209</b>	<b>\$ 1,445,706</b>

*The accompanying notes are an integral part of these financial statements.*

## ZUMIX, INC. AND AFFILIATE

### Consolidated Statements of Cash Flows

For the Years Ended March 31, 2017 and 2016

	<b>2017</b>	<b>2016</b>
Cash flows from operating activities:		
Increase in net assets	\$ 658,201	\$ 757,384
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Amortization of deferred financing and debt issuance costs	958	43,723
Amortization of discount on notes receivable	-	(35,689)
Amortization of deferred income	(16,663)	(96,820)
Amortization of discount on mortgage notes payable	16,663	96,820
Depreciation	168,740	170,927
Contributed property and equipment	-	(1,200)
Net gain on extinguishment of debt	(876,894)	(817,618)
Receipt of contributions restricted for purchase of long-lived assets	-	(45,705)
Changes in operating assets and liabilities:		
Decrease (increase) in contributions receivable	58,045	(30,300)
Decrease (increase) in prepaid expenses	1,228	(4,064)
Increase (decrease) in accounts payable and accrued expenses	15,764	(39,008)
Net cash provided by (used in) operating activities	26,042	(1,550)
Cash flows from investing activities:		
Decrease in amounts held for escrow	130,000	-
Purchases of property and equipment	(42,666)	(20,174)
Net cash provided by (used in) investing activities	87,334	(20,174)
Receipt of contributions restricted for the purchase of long-lived assets	-	45,705
Net cash provided by financing activities	-	45,705
Net increase in cash and cash equivalents	113,376	23,981
Cash and cash equivalents, beginning of year	553,440	529,459
Cash and cash equivalents, end of year	\$ 666,816	\$ 553,440
Supplemental Information:		
Cash paid for interest	\$ -	\$ 5,175
Non-cash activity:		
Workers paid directly by a third party	\$ 58,813	\$ 58,673
Contributed professional services	630	-
Contributions of of property and equipment	-	1,200
Contributions of supplies and items for sale	5,418	-
Total non-cash activity	\$ 64,861	\$ 59,873

*The accompanying notes are an integral part of these financial statements.*

# ZUMIX, INC. AND AFFILIATE

## Notes to Consolidated Financial Statements

March 31, 2017

### 1. Nature of Operations

ZUMIX, Inc. (“ZUMIX”) is a nationally recognized, non-profit cultural organization located in East Boston, MA. ZUMIX’s mission is empowered youth who use music to make strong positive change in their lives, their communities, and the world.

The consolidated financial statements of ZUMIX include the accounts of its affiliate, ZUMIX Firehouse, Inc. (“ZFI”), (together, the “Organization”).

ZFI is a non-profit organization formed in 2008 for the purpose of purchasing and renovating the Engine Company 40 Firehouse, at 260 Sumner Street in East Boston, MA (the “Firehouse Property”) in order to turn the building into a vibrant youth arts center.

#### *Background and History*

East Boston has long been an immigrant, working-class neighborhood, with a strong history of community activism. Geographically separated from the rest of the City by the Boston Harbor, it is home to Logan International Airport, which makes up two-thirds of its landmass.

1990 marked the worst year of violence in Boston’s history. 152 homicides were recorded; many of the victims and perpetrators were youth. ZUMIX was incorporated on April 1, 1991, with \$200, and the belief that giving young people an opportunity to express themselves through music, would dramatically improve their lives, and might elevate a neglected and economically depressed community.

For 26 years, ZUMIX has provided free and subsidized programs for low-income youth. Initially designed to address the pressing issue of gang violence, ZUMIX has grown and evolved with the changing needs of the community. With the recent development of luxury housing on its waterfront, along with skyrocketing rents, East Boston is currently facing new challenges. Families are facing unprecedented levels of displacement and housing insecurity. There has also been an upsurge in opioid abuse, and two street gangs have been battling each other and actively recruiting area youth. In 2016, East Boston gang-related incidents included six homicides, five non-fatal shootings, four stabbings, and three assaults.

ZUMIX has a long track record of positive youth outcomes. In 2011, ZUMIX received the National Arts and Humanities Youth Programs Award from First Lady Michelle Obama at the White House.

#### *Recent Accomplishments*

Highlights during the year ended March 31, 2017 include the following:

- ZUMIX continued to serve over 1,000 youth through after-school programming and in-school partnerships.
- 100% of ZUMIX seniors graduated from high school, and 88% were accepted to college. Two students received full scholarships to Berklee College of Music and Columbia University respectively.



## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

- About 50 youth (ages 14-19) were employed either at ZUMIX, or through ZUMIX, collectively earning over \$35,000 as musicians, sound engineers, program assistants, and journalists, using 21st century skills learned at ZUMIX.
- In December 2014, ZUMIX Radio was awarded a Low Power FM license from the Federal Communications Commission. In September 2016, ZUMIX transitioned from an online-only station to a terrestrial station, broadcasting at 94.9FM, providing youth and community members a platform to share their voices.
- Seven ZUMIX Alumni were employed at ZUMIX giving back to the community they grew up in.

## 2. Summary of Significant Accounting Policies

### *Basis of Accounting*

The financial statements were prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (“GAAP”).

### *Basis of Presentation*

The Organization is required to report information regarding financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. Unrestricted net assets represent amounts without donor-imposed time or purpose restrictions as of the reporting date. Temporarily restricted net assets represent amounts received with donor-imposed time restrictions that have not yet expired or donor-imposed purpose restrictions which have not yet been satisfied by the Organization. Permanently restricted net assets represent amounts with donor-imposed restrictions requiring those amounts to be held in perpetuity. None of the Organization’s net assets are classified as permanently restricted as of March 31, 2017 and 2016.

### *Use of Estimates*

Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from those estimates.

### *Comparative Financial Information*

The financial statements include certain prior-year summarized comparative financial information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with GAAP. Accordingly, such information should be read in conjunction with the Organization’s financial statements for the year ended March 31, 2016, from which the summarized information was derived.

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

#### *Principles of Consolidation*

ZUMIX has the power to appoint a voting majority of board members of ZFI and has made an equity contribution in the amount of \$166,000 to ZFI (described in further detail below). Management has deemed that these factors together constitute both an “economic interest” and “control,” requiring consolidation under GAAP. The accounts of ZFI are included as of December 31, 2016 and 2015. All significant intercompany transactions and balances have been eliminated in consolidation.

The Firehouse Property project had a total capital budget (including all New Markets Tax Credit transaction costs) of \$4,172,904 aggregated by the MHIC New Markets Fund II, LLC, (“MHIC New Markets Fund II”) an investment fund managed by the Massachusetts Housing Investment Corporation (“MHIC”). It was composed of the following sources:

Equity investments in New Markets Tax Credits by multiple investors	\$ 1,273,242
Loan from East Boston Community Development Corporation	920,000
Two sponsor loans from the Organization	<u>1,979,662</u>
	<u>\$ 4,172,904</u>

This pool was in turn invested in two Community Development Entities (“CDEs”) and used to cover MHIC New Markets Fund II’s transaction costs as follows:

Investment in MHIC New Markets CDE II Series 5, LLC	\$ 3,589,954
Investment in Nuestra Commercial Markets Fund 2008, LLC	<u>565,000</u>
	4,154,954
Fund transaction costs	<u>17,950</u>
	<u>\$ 4,172,904</u>

The \$4,154,954 invested in the CDEs was expended in the following manner:

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

Fees, third party costs and reserves:	
Fees and third party costs - MHIC New Markets CDE II Series 5, LLC	\$ 179,498
Fees and third party costs - Nuestra Commercial Markets Fund 2008, LLC	39,550
Reserves withheld by MHIC	<u>78,014</u>
Total fees, third party costs and reserves	<u>297,062</u>
Loans to ZFI:	
MHIC New Markets CDE II Series 5, LLC	3,332,442
Nuestra Commercial Markets Fund 2008, LLC	<u>525,450</u>
Total loans to ZFI	<u>3,857,892</u>
	<u><u>\$ 4,154,954</u></u>

Additionally, as noted above, ZUMIX made an equity investment in ZFI of \$166,000. This equity investment plus the \$3,857,892 loaned to ZFI comprise the \$4,023,892 budgeted for the purchase, construction and renovation of the Firehouse Property.

On December 17, 2008, ZFI purchased the Firehouse Property from the previous owner. Events occurring at that date are described as having occurred "at closing."

In connection with the Firehouse Property project, ZFI committed to paying \$800,000 in developer fees as follows:

Fee paid at closing to East Boston Community Development Corporation	\$ 320,000
Fee paid at closing to the Organization	350,000
Fee paid at completion to the Organization	<u>130,000</u>
	<u><u>\$ 800,000</u></u>

The \$320,000 paid at closing to East Boston Community Development Corporation ("East Boston CDC") represents a payment to this entity for managing the construction of the building.

The \$350,000 paid at closing to ZUMIX represents a payment for management of the predevelopment process.

The \$130,000 was due at completion (April 1, 2010) to ZUMIX and was for the purpose of establishing an operating reserve of \$50,000 and a debt service escrow of \$80,000. This amount was due to ZUMIX from ZFI as of December 31, 2010 and March 31, 2011 and remained due to ZUMIX from ZFI as of December 31, 2016 and March 31, 2017.

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

On December 31, 2015, the two sponsor loans payable to ZUMIX were forgiven. In exchange for the forgiveness of this debt, the right to receive payment from ZFI on two notes payable was assigned to ZUMIX by the noteholders. In addition, two loans to ZFI were forgiven in their entirety. The net effect of these transactions during the year ended March 31, 2016 was a gain of \$817,618 which is included in net gain on extinguishment of debt in the Organization's consolidated statement of activities and changes in net assets for the year ended March 31, 2016. Additional detail regarding these transactions is included in Notes 5, 7, 8 and 9.

On July 19, 2016 the terms of ZFI's remaining note payable to a third party were amended in such a way that there is no principal or interest payable unless certain events or acts occur in a specified time period. Because the Organization's management believes that, based on all available facts and evidence, that it is more likely than not that such actions and events will not occur during the specified time period, the amendment has been accounted for as an in-substance forgiveness of debt which created an associated contingency. In connection with this amendment the Organization recognized a net gain of \$876,894 which is included in net gain on extinguishment of debt in the Organization's consolidated statement of activities and changes in net assets for the year ended March 31, 2017. Additional detail regarding this transaction is included in Notes 8 and 9.

#### *Contributions*

Contributions that are restricted by the donor are reported as increases in unrestricted net assets if the restrictions expire (that is, when a stipulated time restriction ends or purpose restriction is accomplished) in the reporting period in which the revenue is recognized. All other donor-restricted contributions are reported as increases in temporarily restricted or permanently restricted net assets, depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions.

Contributions of long-lived assets (including enhancements to property and equipment) and amounts restricted for the purchase of long-lived assets, for which the donor does not specify a particular period of use, are treated as increases in temporarily restricted net assets when received and reclassified as unrestricted net assets at the time the asset is placed in service.

The Organization's contributions come primarily from the general public, private foundations, corporations and certain governmental agencies.

#### *Cash and Cash Equivalents*

The Organization considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. Certain grants require the Organization to hold cash in separate bank accounts. The total amount of cash held in separate accounts was \$5,604 and \$5,597 as of March 31, 2017 and 2016, respectively.

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

#### *Property and Equipment*

Property and equipment are recorded at cost if purchased and estimated fair market value at the time of donation if donated to the Organization. Contributed services that create or enhance long-lived assets are capitalized and recognized at the estimated fair market value at the time of donation. It is the Organization's policy to capitalize all purchases or contributions of assets with an expected useful life greater than one year that have an initial purchase price or donated value equal to or in excess of \$1,000. Expenditures for repairs and maintenance are charged to expense as incurred. When assets are retired or disposed of, the assets and related accumulated depreciation are eliminated from the accounts and any resulting gain or loss is reflected in income. Depreciation is provided using the straight-line method over the estimated useful life of the assets as follows:

Furniture, fixtures and equipment	5 - 10 years
Website	3 years
Vehicle	5 years
Building	40 years
Building improvements	30 years

#### *Deferred Financing Costs*

Deferred financing costs associated with the issuance of notes receivable at below-market rates are capitalized and amortized over the lives of the respective notes using the effective interest method. Amortization of deferred financing costs is included in interest expense in the accompanying consolidated statement of functional expenses.

#### *Deferred Debt Issuance Costs*

Deferred debt issuance costs include amounts paid by ZFI in connection with the issuance of long-term mortgage notes payable in December of 2008 to finance the Firehouse Property project, as well as the fair value of contributed legal services directly allocable to the issuance of these notes. Amortization of deferred debt issuance costs is calculated using the straight-line method over the 30-year term of the notes. If debt is extinguished, the deferred debt issuance costs associated with the extinguished debt are written off and included as a component of gain or loss on extinguishment of debt in the Organization's statement of activities and changes in net assets. As of March 31, 2016 debt issuance costs are presented net of accumulated amortization of \$13,411.

The Organization's policy is to recognize contributed legal services capitalized as deferred debt issuance costs as an increase in temporarily restricted net assets when received. As the contributed deferred debt issuance costs are amortized into expense the Organization simultaneously recognizes a corresponding decrease in temporarily restricted net assets and an equal increase in unrestricted net assets. Amortization of deferred debt issuance costs is included in interest expense in the accompanying consolidated statement of functional expenses.

During the year ended March 31, 2017, \$15,996 of debt issuance costs written off by the Organization in connection with the amendment of Loan E described in Note 8 represented legal fees

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

previously being amortized as deferred debt issuance costs. The legal fees written off were recorded by the Organization as having been released from restriction during the year ended March 31, 2017.

During the year ended March 31, 2016, in connection with the extinguishment of Loans A, B, C, and D described in Note 8, the Organization wrote off \$140,710 of associated deferred debt issuance costs which is included as a component of net gain on extinguishment of debt. \$64,812 of the debt issuance costs written off during the year ended March 3, 2016 represented legal fees previously being amortized as loan issuance costs. The legal fees written off were recorded by the Organization as having been released from restriction during the year ended March 31, 2016.

#### *Advertising Expenses*

The Organization expenses advertising costs as incurred. Advertising expenses amounted to \$2,764 and \$4,043 for the years ended March 31, 2017 and 2016, respectively.

#### *Income Taxes*

ZUMIX and ZFI are exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code and Massachusetts state income tax under Massachusetts General Law 180. ZUMIX and ZFI qualify for the charitable contribution deduction under Section 170(b)(1)(A) and have been classified as organizations other than a private foundation under Section 509(a)(2).

Management evaluates all significant tax positions as required by GAAP. As of March 31, 2017 and 2016, management does not believe that it has taken any tax positions that would require the recording of any additional tax liability nor does it believe that there are any unrealized tax benefits that would either increase or decrease within the next twelve months.

#### *Fair Value Measurement*

GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

Level 2: Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly;

Level 3: Prices or valuations that require inputs that are both significant to the fair value measurement and unobservable.

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

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. The carrying value of financial instruments in the financial statements approximates fair value.

#### 3. Contributions Receivable

Contributions receivable are stated at the amounts management expects to collect from outstanding balances. Based on management's assessment of the credit history with donors having outstanding balances, and current relationships with them, it has been determined that realized losses from balances outstanding at year-end are immaterial.

Contributions receivable are due to be collected according to the following schedule as of March 31:

	<u>2017</u>	<u>2016</u>
Less than one year	\$ 139,762	\$ 197,807
	139,762	197,807
Allowance for bad debts	<u>(2,000)</u>	<u>(2,000)</u>
	<u>\$ 137,762</u>	<u>\$ 195,807</u>

#### 4. Amounts Held in Escrow

Amounts held in escrow represent funds held by MHIC on behalf of ZFI as of December 31, 2015 and amounted to \$130,000 as of that date. These funds consisted of an \$80,000 debt service escrow and \$50,000 which serves as an operating reserve. Due to the forgiveness of and assignment of the long-term notes payable by ZFI to MHIC on December 31, 2015, the contractual requirement for these funds to be held in escrow ceased to apply and the funds were transferred to a bank account held by ZFI during January of 2016.

#### 5. Notes Receivable

ZUMIX made two sponsor loans, totaling \$1,979,562 to MHIC New Markets Fund II in exchange for notes receivable. The proceeds of these loans were used by MHIC New Markets Fund II for the purpose of making Qualified Equity Investments of \$1,587,757 and \$391,805, in MHIC New Markets CDE II Series 5, LLC and Nuestra Commercial Markets Fund 2008, LLC, respectively. These respective entities subsequently used these funds for making 0% stated interest rate loans to ZFI of \$1,587,757 and \$391,805. The financing was structured in this manner in order to increase the amount of Qualified Equity Investment in MHIC New Markets Fund II to \$4,172,904, thereby increasing the dollar amount of New Markets Tax Credits allocable to equity investors to a total of approximately \$1.6 million.

During the year ended March 31, 2016, ZUMIX agreed to forgive the Tranche A and Tranche B Loans in exchange for the assignment to ZUMIX of the right to receive payment under certain notes

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

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payable from ZFI. This forgiveness and assignment was completed on December 31, 2015. As indicated in Note 8, Loans A and B are eliminated in consolidation at March 31, 2017 and 2016. The total carrying value of Tranche A and Tranche B loans, not including deferred financing costs at the time of forgiveness was \$930,253, these amounts are included as a component of the net gain on extinguishment of debt in the consolidated statement of activities and changes in net assets for the year ended March 31, 2016. The value of the assigned loans, which eliminate in consolidation, and represent the consideration received for forgiveness of the sponsor loan, was deemed to be \$1,979,562, which is the face value of the notes. These amounts are included as a component of the net gain on extinguishment of debt in the consolidated statement of activities and changes in net assets for the year ended March 31, 2016.

Interest income for the years ended March 31, 2017 and 2016 includes \$0 and \$35,689, respectively, which represent the amortization of the original issue discounts on notes receivable.

#### 6. Property and Equipment

Property and equipment consists of the following as of March 31:

	<u>2017</u>	<u>2016</u>
Furniture and fixtures	\$ 32,026	\$ 32,026
Motor vehicle	22,423	22,423
Computer equipment	342,784	319,490
Website	16,000	16,000
Land	227,998	227,998
Building and improvements	<u>3,444,682</u>	<u>3,444,682</u>
	4,085,913	4,062,619
Less accumulated depreciation and amortization	<u>(1,173,496)</u>	<u>(1,024,128)</u>
Property and equipment, net	<u>\$ 2,912,417</u>	<u>\$ 3,038,491</u>

As of March 31, 2017 and 2016, building and improvements include \$65,777 and \$68,607 net of accumulated amortization of \$19,097 and \$16,267, respectively, of capitalized interest costs incurred during the period of construction.

#### 7. Deferred Financing Costs

In connection with the cancellation of the Tranche A and Tranche B notes receivable on December 31, 2015 the associated unamortized deferred financing costs of \$1,049,139 were written off in their entirety. This write down is included as a component of the net gain on extinguishment of debt in the consolidated statement of activities and changes in net assets for the year ended March 31, 2016.



**ZUMIX, INC. AND AFFILIATE**

Notes to Consolidated Financial Statements

March 31, 2017

**8. Mortgage Notes Payable**

Mortgage notes payable by the Organization consist of the following as of March 31:

	<b>2017</b>	<b>2016</b>
0% note payable to East Boston CDC at December 31, 2015 ("Loan E"). Secured by a third mortgage and security in land and building, carrying value of \$2,905,363.	\$ -	\$ 920,000
	-	920,000
Discount for imputed interest on below-market interest rate loans	-	(588,677)
Mortgage notes payable, net	\$ -	\$ 331,323

As of March 31, 2016 the discount on the below-market interest rate loan is imputed using an interest rate of 8.38%. For the years ended March 31, 2017 and 2016, interest expense included \$16,663 and \$96,820, respectively, representing the amortization of discounts on mortgage notes payable.

The following table summarizes ZFI's long-term notes payable as of March 31, 2015:

	<b>2015</b>
0% note payable to MHIC New Markets CDE II Series 5, LLC ("Loan A"). Secured by a shared first mortgage and security interest in land and building.	\$ 1,587,757
0% note payable to Nuestra Commercial Markets Fund 2008, LLC ("Loan B"). Secured by a shared first mortgage and security interest in land and building.	391,805
0.50% note payable to MHIC New Markets CDE II Series 5, LLC ("Loan C"). Secured by a shared second mortgage and security interest in land and building.	824,685
1.50% note payable to Nuestra Commercial Markets Fund 2008, LLC ("Loan D"). Secured by a shared second mortgage and security interest in land and building.	133,645
0% note payable to MHIC New Markets CDE II Series 5, LLC ("Loan E"). Secured by a third mortgage and security in land and building.	920,000
	3,857,892
Discount for imputed interest on below-market interest rate loans	(2,222,392)
Mortgage notes payable, net	\$ 1,635,500

On December 31, 2015 the right to receive payment from ZFI on Loan A and Loan B was assigned by the noteholders to ZUMIX. This intercompany debt is eliminated in the preparation of the consolidated financial statements as of and for the years ended March 31, 2017 and 2016.

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

On December 31, 2015 Loan C and Loan D were forgiven by the note holders. The associated gain of \$447,517, representing the carrying value of the loans at the time they were forgiven (exclusive of associated deferred income described in Note 9), is included as a component of the net gain on extinguishment of debt in the consolidated statement of activities and changes in net assets for the year ended March 31, 2016.

On December 31, 2015 the right to receive payment on Loan E was assigned to East Boston CDC. On July 19, 2016 ZFI and East Boston CDC agreed to reduce the principal amount payable on Loan E to \$600,000. Under the July 19, 2016 amendment no payment of principal or is due on the loan unless an incident of default as defined by amendment occurs (see below). If no event of default occurs by June 20, 2046 (“the Maturity Date”) the principal sum of Loan E will be forgiven by East Boston CDC. In the event of default, payments on the principal sum, together with default interest of 4% per annum, must be paid in equal installments by the first day of each month, such payments are amortized by the date of default to the Maturity Date.

Actions or events that would constitute default under the amended loan agreement between ZFI and East Boston CDC are as follows:

- a) The failure by ZFI at any time, in the reasonable judgment of East Boston CDC and beyond any applicable notice and cure period, substantially to adhere to the general purposes of any of the covenants, conditions and restrictions set forth in the deed to the Firehouse Property from the City of Boston to ZFI dated December 19, 2008 and recorded in the Suffolk County Registry of Deeds at Book 44360, Page 324, notwithstanding that the deed provides for an expiration of the covenants, conditions and restrictions.
- b) The violation by ZFI, beyond any applicable notice and cure period of any of the material provisions of the mortgage, security agreement, and assignment of leases and rents on the Firehouse Property.
- c) The permanent discontinuation by ZFI of its current use of the Firehouse Property or any substantially similar use.
- d) The cessation of business or operations by ZFI, dissolution of ZFI, the filing of a bankruptcy petition (voluntary or involuntary) that is not dismissed within ninety days, assignment for the benefit of creditors or other insolvency petition brought by or against ZFI that is not dismissed within ninety days.

The amendment also states for the purposes of item “c” above that a period of one hundred consecutive days constitutes a rebuttable presumption that ZFI has permanently discontinued its use of the Firehouse Property.

As of the date the financial statements were available to be issued, the Organization does not deem it to be probable that an incident of default will occur and therefore does not expect that any payments will be required under the amended loan. As a result of this determination the Organization recognized a net gain of \$876,894 due to the amendment of Loan E which is included in net gain on

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

extinguishment of debt in the Organization's consolidated statement of activities and changes in net assets for the year ended March 31, 2017. The gain net consists of the following components:

- A write-off of the carrying value of the Loan E of July 19, 2016 of \$347,986 (gain)
- The recognition of previously deferred income associated with Loan E of \$572,014 (gain)
- A write-off of previously unamortized deferred debt issuance costs associated with the Loan E of \$43,106 (loss)

#### **9. Deferred Income**

In connection with the purchase and renovation of the Firehouse Property, ZFI entered into several long-term financing agreements by issuing mortgage notes payable with face amounts totaling \$3,857,892 as described in Note 8. The Organization's policy is to report long-term notes payable at the net present value at the time of issuance, net of any amortized discount or premium. In accordance with this policy, the Organization recorded discounts on these notes payable amounting to \$2,656,213 at the time of their issuance, as the Organization deemed the stated interest rates on these notes to be below market rates at that time. In connection with the receipt of this below-market financing ZFI also recognized deferred income in the amount of \$2,656,213 which ZFI has amortized as income over the lives of the notes using the effective interest rate method. In connection with the forgiveness and assignment of Loans A, B, C and D above on December 31, 2015, ZFI recognized income of \$487,756 which was previously deferred. This amount is included as a component of the net gain on extinguishment of debt in the consolidated statement of activities and changes in net assets for the year ended March 31, 2016.

In connection with the in-substance forgiveness of Loan E on July 19, 2016, ZFI recognized income of \$572,014 which was previously deferred. This amount is included as a component of the net gain on extinguishment of debt in the consolidated statement of activities and changes in net assets for the year ended March 31, 2017.

Unamortized deferred income amounted to \$0 and \$588,677 as of March 31, 2017 and 2016, respectively.

#### **10. Temporarily Restricted Net Assets**

The Organization's temporarily restricted net assets consist of the following as of March 31:

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

	<b>2017</b>	<b>2016</b>
Amounts restricted for use in future periods	\$ 103,500	\$ 180,300
Strategic planning activities	16,667	-
Amounts restricted for acquisition of program equipment and other capital expenditures	235	45,940
Contributed debt issuance costs to be amortized in future periods	-	15,966
	<b>\$ 120,402</b>	<b>\$ 242,206</b>

Net assets were released from donor restrictions by incurring expenses or otherwise satisfying the purpose restrictions specified by donors as follows during the years ended March 31:

	<b>2017</b>	<b>2016</b>
Expiration of donor-imposed time restrictions:	\$ 52,300	\$ 75,000
Purpose restrictions accomplished:		
Acquisition of program equipment and other capital expenditures	45,705	12,997
Program expenses	128,000	85,000
Amortization and impairment of contributed debt issuance costs	15,966	68,512
	189,671	166,509
Net assets released from restrictions	<b>\$ 241,971</b>	<b>\$ 241,509</b>

### 11. Operating Reserve and Capitalization

Historically, ZUMIX has maintained a stable financial position by achieving reasonable, modest end-of-year surpluses. With increased growth, ZUMIX has increased its commitment to financial stability by: 1) budgeting for depreciation, 2) designating capital asset replacement reserve, and 3) striving to maintain up to three months of unrestricted operating funds.

Months of unrestricted operating funds held by ZUMIX were calculated as follows as of March 31:

	<b>2017</b>	<b>2016</b>
Cash balance	\$ 493,012	\$ 515,712
Temporarily restricted net assets representing cash with purpose restrictions	(235)	(45,940)
Management designated capital asset replacement reserve	(363,795)	(332,943)
Cash balance less restricted and designated funds	<b>\$ 128,982</b>	<b>\$ 136,829</b>
Average monthly operating expenses	\$ 110,538	\$ 100,863
Months of unrestricted operating funds	1.17	1.36

## ZUMIX, INC. AND AFFILIATE

### Notes to Consolidated Financial Statements

March 31, 2017

#### 12. Credit Card Line of Credit

The Organization has a business line of credit available from a credit card company allowing for purchases or cash borrowings. As of March 31, 2017, the Organization had no outstanding cash borrowings and had an outstanding balance from purchases of \$1,997 which is included in accounts payable and accrued expenses. As of March 31, 2017, the Organization had remaining credit available for purchases of \$30,703 and \$11,200 for cash advances. Minimum monthly payments, which vary according to the outstanding balances, are due under the agreement including interest at 14.99% for purchases and 21.99% for cash advances, as of March 31, 2017.

As of March 31, 2016, the Organization had no outstanding cash borrowings and had an outstanding balance from purchases of \$1,140 which is included in accounts payable and accrued expenses. As of March 31, 2016, the Organization has remaining credit available for purchases of \$31,560 and \$11,200 for cash advances.

#### 13. Interest

For the year ended March 31, 2017 and 2016, total interest expense amounted to \$17,621 and \$145,718, respectively. No interest was capitalized during the years ended March 31, 2017 or 2016. Amortization of deferred financing and debt issuance costs included in interest expense for the years ended March 31, 2017 and 2016 amounted to \$958 and \$43,723, respectively.

#### 14. Concentrations of Credit Risk

Financial instruments which subject the Organization to credit risk consist principally of temporary cash investments. The Federal Deposit Insurance Corporation ("FDIC") provides insurance of up to \$250,000 per depositor, per insured bank. The Organization places its temporary cash investments with a Massachusetts chartered savings bank which is a member of the Depositors Insurance Fund ("DIF"). DIF insures all amounts in excess of FDIC insured limits deposited with member banks.

#### 15. Retirement Plan

ZUMIX sponsors a defined contribution retirement plan for eligible employees. Annual contributions are at the discretion of ZUMIX. During the years ended March 31, 2017 and 2016, the Organization recognized expenses for its contributions to the plan amounting to \$5,346 and \$5,125, respectively which represents 1% of the gross salary of eligible ZUMIX employees for each of the fiscal years then-ended.

#### 16. Reclassifications

Certain amounts included in the consolidated financial statements for the year ended March 31, 2016 have been reclassified to conform to the current year presentation. These reclassifications had no impact on previously reported consolidated net assets or changes in consolidated net assets.

## **ZUMIX, INC. AND AFFILIATE**

Notes to Consolidated Financial Statements

March 31, 2017

### **17. Subsequent Events**

The Organization has evaluated subsequent events through November 10, 2017 the date the financial statements were available to be issued.

## ZUMIX, INC. AND AFFILIATE

### Consolidating Statement of Financial Position

(Supplementary Information)

March 31, 2017

<i>Assets</i>	<b>ZUMIX, Inc.</b>	<b>ZUMIX Firehouse, Inc.</b>	<b>Elimination</b>	<b>Consolidated</b>
Current assets:				
Cash and cash equivalents	\$ 493,012	\$ 173,804	\$ -	\$ 666,816
Amounts held for others	32,242	-	-	32,242
Contributions receivable, net	137,759	3	-	137,762
Prepaid expenses and other current assets	28,991	-	-	28,991
Total current assets	692,004	173,807	-	865,811
Due from affiliate	2,109,562	23,100	(2,132,662)	-
Property and equipment, net	115,267	3,173,800	(376,650)	2,912,417
Interest in the net assets of ZUMIX Firehouse, Inc.	166,000	-	(166,000)	-
Total assets	\$ 3,082,833	\$ 3,370,707	\$ (2,675,312)	\$ 3,778,228
<b><i>Liabilities and Net Assets</i></b>				
Current liabilities:				
Accounts payable and accrued expenses	\$ 48,393	\$ -	\$ -	\$ 48,393
Amounts held for others	32,242	-	-	32,242
Total current liabilities	80,635	-	-	80,635
Due to affiliate	23,100	2,109,562	(2,132,662)	-
Total liabilities	103,735	2,109,562	(2,132,662)	80,635
Net assets:				
Unrestricted	2,858,696	1,261,145	(542,650)	3,577,191
Temporarily restricted	120,402	-	-	120,402
Total net assets	2,979,098	1,261,145	(542,650)	3,697,593
Total liabilities and net assets	\$ 3,082,833	\$ 3,370,707	\$ (2,675,312)	\$ 3,778,228

*See accompanying independent auditors' report.*

**ZUMIX, INC. AND AFFILIATE**

Consolidating Statement of Activities and Changes in Net Assets

(Supplementary Information)

For the Year Ended March 31, 2017

	<u>ZUMIX, Inc.</u>			<u>ZUMIX Firehouse, Inc.</u>			<u>Elimination</u>	<u>Consolidated</u>
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>		
Support and revenue:								
Individual donations	\$ 106,148	\$ -	\$ 106,148	\$ -	\$ -	\$ -	\$ -	\$ 106,148
In-kind donations	64,861	-	64,861	-	-	-	-	64,861
Corporate donations	91,892	-	91,892	-	-	-	(36,000)	55,892
Foundation donations	507,918	120,167	628,085	-	-	-	-	628,085
Events	44,323	-	44,323	-	-	-	-	44,323
Government grants	82,993	-	82,993	-	-	-	-	82,993
Program fees	152,664	-	152,664	-	-	-	-	152,664
Interest income	3,591	-	3,591	1,246	-	1,246	-	4,837
Amortization of deferred income from below-market interest rate loans	-	-	-	16,663	-	16,663	-	16,663
Rental income	34,682	-	34,682	38,875	-	38,875	(36,000)	37,557
Sale of product	4,493	-	4,493	-	-	-	-	4,493
Net gain on extinguishment of debt	-	-	-	876,894	-	876,894	-	876,894
Other income	-	-	-	-	-	-	-	-
Net assets released from restriction	226,005	(226,005)	-	15,966	(15,966)	-	-	-
<b>Total support and revenue</b>	<b>1,319,570</b>	<b>(105,838)</b>	<b>1,213,732</b>	<b>949,644</b>	<b>(15,966)</b>	<b>933,678</b>	<b>(72,000)</b>	<b>2,075,410</b>
Expenses:								
Youth programs	999,911	-	999,911	163,833	-	163,833	(82,980)	1,080,764
Community arts program	132,685	-	132,685	-	-	-	-	132,685
Total program expenses	1,132,596	-	1,132,596	163,833	-	163,833	(82,980)	1,213,449
Management and general	112,592	-	112,592	8,022	-	8,022	(2,610)	118,004
Fundraising	81,264	-	81,264	7,102	-	7,102	(2,610)	85,756
<b>Total expenses</b>	<b>1,326,452</b>	<b>-</b>	<b>1,326,452</b>	<b>178,957</b>	<b>-</b>	<b>178,957</b>	<b>(88,200)</b>	<b>1,417,209</b>
Increase (decrease) in net assets	(6,882)	(105,838)	(112,720)	770,687	(15,966)	754,721	16,200	658,201
Net assets, beginning of year	2,865,578	226,240	3,091,818	490,458	15,966	506,424	(558,850)	3,039,392
Net assets, end of year	\$ 2,858,696	\$ 120,402	\$ 2,979,098	\$ 1,261,145	\$ -	\$ 1,261,145	\$ (542,650)	\$ 3,697,593

*See accompanying independent auditors' report.*



**ZUMIX, INC. AND AFFILIATE**

Consolidating Statement of Cash Flows  
(Supplementary Information)

For the Year Ended March 31, 2017

	<b>ZUMIX</b>			
	<u><b>ZUMIX, Inc.</b></u>	<u><b>Firehouse, Inc.</b></u>	<u><b>Elimination</b></u>	<u><b>Consolidated</b></u>
Cash flows from operating activities:				
Increase (decrease) in net assets	\$ (112,720)	\$ 754,721	\$ 16,200	\$ 658,201
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:				
Amortization of deferred financing and debt issuance costs	-	958	-	958
Amortization of deferred income	-	(16,663)	-	(16,663)
Amortization of discount on mortgage notes payable	-	16,663	-	16,663
Depreciation	60,524	124,416	(16,200)	168,740
Net gain on extinguishment of debt	-	(876,894)	-	(876,894)
Changes in operating assets and liabilities:				
Decrease in contributions receivable	55,170	2,875	-	58,045
Decrease in prepaid expenses	1,228	-	-	1,228
Increase in accounts payable and accrued expenses	15,764	-	-	15,764
Net cash provided by (used in) operating activities	<u>19,966</u>	<u>6,076</u>	<u>-</u>	<u>26,042</u>
Cash flows from investing activities:				
Decrease in amounts held for escrow	-	130,000	-	130,000
Purchases of property and equipment	(42,666)	-	-	(42,666)
Net cash used in investing activities	<u>(42,666)</u>	<u>130,000</u>	<u>-</u>	<u>87,334</u>
Net increase (decrease) in cash and cash equivalents	(22,700)	136,076	-	113,376
Cash and cash equivalents, beginning of year	<u>515,712</u>	<u>37,728</u>	<u>-</u>	<u>553,440</u>
Cash and cash equivalents, end of year	<u>\$ 493,012</u>	<u>\$ 173,804</u>	<u>\$ -</u>	<u>\$ 666,816</u>
Supplemental Information:				
Non-cash activity:				
Workers paid directly by a third party	\$ 58,813	\$ -	\$ -	\$ 58,813
Contributed professional services	630	-	-	630
Contributions of supplies and items for sale	5,418	-	-	5,418
	-	-	-	-
Total non-cash activity	<u>\$ 64,861</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 64,861</u>

See accompanying independent auditors' report.