

HEADWATERS FOUNDATION FOR JUSTICE
FINANCIAL STATEMENTS
YEARS ENDED JUNE 30, 2016 AND 2015

**HEADWATERS FOUNDATION FOR JUSTICE
TABLE OF CONTENTS
YEARS ENDED JUNE 30, 2016 AND 2015**

INDEPENDENT AUDITORS' REPORT	1
FINANCIAL STATEMENTS	
STATEMENTS OF FINANCIAL POSITION	3
STATEMENTS OF ACTIVITIES	4
STATEMENTS OF FUNCTIONAL EXPENSES	5
STATEMENTS OF CASH FLOWS	7
NOTES TO FINANCIAL STATEMENTS	8

INDEPENDENT AUDITORS' REPORT

Board of Directors
Headwaters Foundation for Justice
Minneapolis, Minnesota

We have audited the accompanying financial statements of Headwaters Foundation for Justice which comprise the statements of financial position as of June 30, 2016 and 2015, and the related statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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 financial statements.

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

Board of Directors
Headwaters Foundation for Justice

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Headwaters Foundation for Justice as of June 30, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

CliftonLarsonAllen LLP

CliftonLarsonAllen LLP

Minneapolis, Minnesota
September 26, 2016

**HEADWATERS FOUNDATION FOR JUSTICE
STATEMENTS OF FINANCIAL POSITION
JUNE 30, 2016 AND 2015**

	2016	2015
ASSETS		
Cash and Cash Equivalents	\$ 851,918	\$ 1,118,107
Pledges Receivable, Net	19,001	48,480
Grants and Other Receivables	14,183	8,000
Prepaid Expenses and Other	28,029	16,304
Property and Equipment, Net	26,874	31,812
Investments	3,009,118	3,151,393
Program Related Investments	410,834	510,834
Interest in the Net Assets of The Minneapolis Foundation	896,767	960,143
Total Assets	\$ 5,256,724	\$ 5,845,073
LIABILITIES AND NET ASSETS		
LIABILITIES		
Accounts Payable	\$ 47,552	\$ 22,963
Fiscal Agency Payable	-	38,124
Accrued Expenses	24,188	10,766
Deferred Rent Payable	8,852	4,785
Tenant Security Deposits	1,880	880
Total Liabilities	82,472	77,518
NET ASSETS		
Unrestricted	587,408	1,182,543
Temporarily Restricted	174,864	173,032
Permanently Restricted	4,411,980	4,411,980
Total Net Assets	5,174,252	5,767,555
Total Liabilities and Net Assets	\$ 5,256,724	\$ 5,845,073

See accompanying Notes to Financial Statements.

**HEADWATERS FOUNDATION FOR JUSTICE
STATEMENTS OF ACTIVITIES
YEARS ENDED JUNE 30, 2016 AND 2015**

	2016				2015			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUES, GAINS, AND OTHER SUPPORT								
Contributions and Grants	\$ 659,746	\$ 222,500	\$ -	\$ 882,246	\$ 577,329	\$ -	\$ 621,505	\$ 1,198,834
Contributions – Donor Advised Funds	321,635	-	-	321,635	911,051	-	-	911,051
Program Revenue	-	-	-	-	15,712	-	-	15,712
Investment Income (Loss)	118,131	(94,467)	-	23,664	98,037	35,891	-	133,928
Change in Beneficial Interests in								
The Minneapolis Foundation Fund	(15,446)	(4,210)	-	(19,656)	-	23,926	-	23,926
Special Events, Net of Expenses of \$69,365 and \$62,116, Respectively	67,151	-	-	67,151	66,164	-	-	66,164
Other Operating Revenue	76,891	-	-	76,891	93,375	-	-	93,375
Net Assets Released from Restriction	121,991	(121,991)	-	-	584,642	(584,642)	-	-
Total Revenues, Gains, and Other Support	1,350,099	1,832	-	1,351,931	2,346,310	(524,825)	621,505	2,442,990
EXPENSES								
Program Services	1,499,042	-	-	1,499,042	1,413,975	-	-	1,413,975
Supporting Services:								
Management and General	241,944	-	-	241,944	254,104	-	-	254,104
Fund Development	204,248	-	-	204,248	212,807	-	-	212,807
Total Supporting Services	446,192	-	-	446,192	466,911	-	-	466,911
Total Expenses	1,945,234	-	-	1,945,234	1,880,886	-	-	1,880,886
CHANGE IN NET ASSETS	(595,135)	1,832	-	(593,303)	465,424	(524,825)	621,505	562,104
Net Assets - Beginning of Year	1,182,543	173,032	4,411,980	5,767,555	717,119	697,857	3,790,475	5,205,451
NET ASSETS - END OF YEAR	<u>\$ 587,408</u>	<u>\$ 174,864</u>	<u>\$ 4,411,980</u>	<u>\$ 5,174,252</u>	<u>\$ 1,182,543</u>	<u>\$ 173,032</u>	<u>\$ 4,411,980</u>	<u>\$ 5,767,555</u>

See accompanying Notes to Financial Statements.

**HEADWATERS FOUNDATION FOR JUSTICE
STATEMENT OF FUNCTIONAL EXPENSES
YEAR ENDED JUNE 30, 2016**

	Program Services					Supporting Services			
	Grantmaking	Donor	AALF	Giving	Total	Management and General	Fund	Total	Total
		Advised		Project			Development		
Salaries and Benefits	\$ 167,071	\$ 21,233	\$ -	\$ 41,391	\$ 229,694	\$ 98,365	\$ 140,008	\$ 238,373	\$ 468,067
Consultants	5,000	-	-	60,000	65,000	-	-	-	65,000
Accountants	14,000	-	-	-	14,000	94,896	-	94,896	108,896
Office Expenses	8,722	5,249	-	3,205	17,176	544	8,208	8,752	25,928
Information Technology	11,303	7,039	-	3,254	21,596	4,078	1,806	5,884	27,480
Occupancy	9,360	6,583	-	3,004	18,947	-	1,718	1,718	20,665
Conference Conventions and Meetings	21,282	11	-	11,644	32,937	2,560	5,963	8,523	41,460
Depreciation and Amortization	-	-	-	-	-	10,135	-	10,135	10,135
Insurance	1,793	1,364	-	663	3,819	830	300	1,130	4,949
Memberships	-	-	-	-	-	3,594	-	3,594	3,594
Other Expense	581	14	-	1,907	2,502	25,298	6,245	31,543	34,045
Bad Debt Expense	-	-	-	4,972	4,972	-	40,000	40,000	44,972
Total Expenses before Grants	<u>239,112</u>	<u>41,492</u>	<u>-</u>	<u>130,040</u>	<u>410,644</u>	<u>240,300</u>	<u>204,248</u>	<u>444,548</u>	<u>855,192</u>
Grants (Net of Donor Advised Grants)	138,085	-	-	125,399	263,484	1,644	-	1,644	265,128
Donor Advised Funds Grants	-	824,914	-	-	824,914	-	-	-	824,914
Total Grants	<u>138,085</u>	<u>824,914</u>	<u>-</u>	<u>125,399</u>	<u>1,088,398</u>	<u>1,644</u>	<u>-</u>	<u>1,644</u>	<u>1,090,042</u>
Total Expenses	<u>\$ 377,197</u>	<u>\$ 866,406</u>	<u>\$ -</u>	<u>\$ 255,439</u>	<u>\$ 1,499,042</u>	<u>\$ 241,944</u>	<u>\$ 204,248</u>	<u>\$ 446,192</u>	<u>\$ 1,945,234</u>
Percentages	<u>19%</u>	<u>45%</u>	<u>0%</u>	<u>13%</u>	<u>77%</u>	<u>12%</u>	<u>10%</u>	<u>23%</u>	<u>100%</u>

See accompanying Notes to Financial Statements.

**HEADWATERS FOUNDATION FOR JUSTICE
STATEMENT OF FUNCTIONAL EXPENSES
YEAR ENDED JUNE 30, 2015**

	Program Services					Supporting Services			
	Grantmaking	Donor	AALF	Giving	Total	Management and General	Fund	Total	Total
		Advised		Project			Development		
Salaries and Benefits	\$ 188,853	\$ 20,381	\$ 23,660	\$ 16,609	\$ 249,503	\$ 151,865	\$ 136,829	\$ 288,694	\$ 538,197
Consultants	10,705	-	43,953	46,000	100,658	21,655	37,650	59,305	159,963
Accountants	-	-	-	-	-	22,585	-	22,585	22,585
Office Expenses	11,995	1,511	2,764	542	16,812	2,276	11,246	13,522	30,334
Information Technology	8,448	881	574	132	10,035	4,441	6,430	10,871	20,906
Occupancy	23,220	3,971	1,529	1,570	30,290	13,906	6,790	20,696	50,986
Conference Conventions and Meetings	32,526	15	22,718	5,768	61,027	9,385	9,104	18,489	79,516
Depreciation and Amortization	-	-	-	-	-	8,494	-	8,494	8,494
Insurance	2,598	850	-	-	3,448	660	755	1,415	4,863
Memberships	-	-	-	-	-	484	240	724	724
Other Expense	70	214	-	-	284	18,353	3,763	22,116	22,400
Total Expenses before Grants	<u>278,415</u>	<u>27,823</u>	<u>95,198</u>	<u>70,621</u>	<u>472,057</u>	<u>254,104</u>	<u>212,807</u>	<u>466,911</u>	<u>938,968</u>
Grants (Net of Donor Advised Grants)	248,100	-	45,000	-	293,100	-	-	-	293,100
Donor Advised Funds Grants	-	648,818	-	-	648,818	-	-	-	648,818
Total Grants	<u>248,100</u>	<u>648,818</u>	<u>45,000</u>	<u>-</u>	<u>941,918</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>941,918</u>
Total Expenses	<u>\$ 526,515</u>	<u>\$ 676,641</u>	<u>\$ 140,198</u>	<u>\$ 70,621</u>	<u>\$ 1,413,975</u>	<u>\$ 254,104</u>	<u>\$ 212,807</u>	<u>\$ 466,911</u>	<u>\$ 1,880,886</u>
Percentages	<u>28%</u>	<u>36%</u>	<u>7%</u>	<u>4%</u>	<u>75%</u>	<u>14%</u>	<u>11%</u>	<u>25%</u>	<u>100%</u>

See accompanying Notes to Financial Statements.

**HEADWATERS FOUNDATION FOR JUSTICE
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2016 AND 2015**

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in Net Assets	\$ (593,303)	\$ 562,104
Adjustment to Reconcile Change in Net Assets to Net Cash Provided (Used) by Operating Activities:		
Depreciation and Amortization	10,135	8,494
Contributions Received for Long-Term Purposes	-	(621,505)
Net Realized and Unrealized (Gain) Loss on Investments	26,940	(45,384)
Change in Beneficial Interest in Minneapolis Foundation	19,656	(23,926)
Change in Allowance for Uncollectible Pledges	(1,008)	-
(Increase) Decrease in Assets:		
Pledges Receivable	30,487	105,005
Grants and Other Receivables	(6,183)	118,962
Prepaid Expenses and Other	(11,725)	(6,695)
Increase (Decrease) in Liabilities:		
Accounts Payable	24,589	19,800
Fiscal Agency Payable	(38,124)	38,124
Accrued Expenses	13,422	(4,428)
Grants Payable	-	(10,000)
Deferred Rent Payable	4,067	273
Tenant Security Deposits	1,000	(468)
Net Cash Provided (Used) by Operating Activities	(520,047)	140,356
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Fixed Assets	(5,197)	(2,942)
Repayment of Program Related Investments	100,000	-
Purchase of Investments	(369,605)	(633,209)
Proceeds from Sale of Investments	528,660	314,426
Net Cash Provided (Used) by Investing Activities	253,858	(321,725)
CASH FLOWS FROM FINANCING ACTIVITIES		
Contributions Received for Long-Term Purposes	-	621,505
NET CHANGE IN CASH AND CASH EQUIVALENTS	(266,189)	440,136
Cash and Cash Equivalents - Beginning of Year	1,118,107	677,971
CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 851,918	\$ 1,118,107

See accompanying Notes to Financial Statements.

**HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Foundation

Headwaters Foundation for Justice (the Foundation) is a community foundation whose mission is to amplify the power of community to advance equity and justice. Through grantmaking and capacity building support to grassroots organizations, our goal is to foster just and sustainable communities that embrace social, racial, economic and environmental equity. To achieve this goal, all of Headwaters' programs are designed to advance two objectives: changing systems of power, and increasing the power of disenfranchised communities. Our community-led grantmaking process is the touchstone of our foundation.

Description of Program Services

Grantmaking – This program includes the process of grantee outreach, proposal review, grant tracking, record keeping, grants evaluation and internal grants management. Grantmaking programs include:

- The Giving Project is an innovative new model for funding grassroots groups or projects engaged in social change organizing to achieve social, economic, environmental, and racial justice in diverse communities throughout Minnesota. In fiscal year 2016, the Giving Project awarded \$140,000 in 12 grants.
- The Fund of the Sacred Circle is directed toward American Indian led grassroots groups or projects in Minnesota and Wisconsin addressing issues of injustice in Native communities. The fund reaffirms the self-determination of American Indians to define and address the needs of their communities in culturally appropriate ways. In fiscal year 2016, The Fund of Sacred Circle awarded \$50,000 in 5 grants;
- Bush Foundation Community Innovation Grants support community problem solving processes around the region.
- Emergency Fund for Black Lives is a short-term temporary fund making general operating grants to Black Lives Matter Minneapolis and Neighborhoods Organizing for Change. In fiscal year 2016, \$104,000 in grants was awarded to 2 grantees.
- Community Innovation Granting is a new program for Headwaters in collaboration with the Bush Foundation. The grants program is set up to support community problem solving in Minnesota. In fiscal year 2016, \$411,511 was awarded in 45 grants.

Donor Advised Funds – Enable individual donors to advance their philanthropic goals and direct resources to social change groups locally, nationally, and internationally. Headwaters staff educate donors about social injustice issues, connect them to organizations that match their interests, and provide technical grantmaking assistance. In fiscal year 2016, Headwaters allocated \$408,400 in 107 Donor Advised Grants.

**HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Description of Program Services (Continued)

African American Leadership Forum (AALF) –

African Leadership Forum (Twin Cities) is an effort devoted to developing a comprehensive urban agenda coming directly from the African American community. This agenda addresses all of the opportunity structures that contribute to the quality of life for African Americans in the twin cities. In 2015, AALF formed its own Organization and became a fiscal agency relationship for Headwaters Foundation. As of the year ended June 30, 2016, the Foundation did not hold a fiscal agency liability on behalf of AALF and no longer had a fiscal agency relationship.

African American Leadership Forum (AALF) National is a fiscal agency for Headwaters Foundation started in 2008 to build capacity among the African American community leaders. The northwest region includes 4 areas: twin cities, MN; Des Moines, IA; Portland, OR; and Seattle, WA. AALF National has mobilized and supported community owned and community driven efforts to improve the social and economic well-being of all African Americans.

Basis of Presentation

The Foundation's financial statements are presented using the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Net assets, revenues and gains and losses are classified based on the existence or absence of donor imposed restriction. Accordingly, net assets of the Foundation and changes therein are classified and reported as follows:

Unrestricted – Those resources over which the board of directors has discretionary control.

Temporarily Restricted – Those resources subject to donor imposed restrictions that are satisfied by actions of the Foundation or passage of time.

Permanently Restricted – Those resources subject to a donor imposed restriction that they be maintained permanently by the Foundation. The donors of these resources permitted the Foundation to use all or part of the income earned, including capital appreciation on related investments, for unrestricted or temporarily restricted purposes. Permanently restricted net assets include the original contributions related to the General Endowment Fund, the Fund of the Sacred Circle and the Headwaters Foundation for Justice Fund of The Minneapolis Foundation.

**HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Foundation considers cash on hand and on deposit in banks, short-term and highly liquid investments to be cash equivalents. Money market investment funds held for endowment purposes are excluded from this classification. At times the balance of deposits may exceed federally insured limits.

Pledges Receivable

Pledges receivable are stated at the amount management expects to collect from balances outstanding at year-end. Based on management's assessment of the outstanding balances, it has concluded that realization losses on balance outstanding at year-end will be immaterial. The allowance for the years ended June 30, 2016 and 2015 was \$-0- and \$1,008, respectively.

Grants and Other Receivables

Grants and other receivables consist primarily of cost-reimbursement grants where costs have been incurred prior to year-end and amounts drawn down subsequent to year-end. All amounts are deemed collectible by management and due within one year.

Revenue Recognition

Contributions, including unconditional promises to give, are recognized as unrestricted, temporarily restricted or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Donor restricted support is reported as an increase in the temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities as net assets released from restrictions. The Foundation has elected to present temporarily restricted contributions, when restrictions are fulfilled in the same time period as received, within the unrestricted net asset class.

Contributions restricted for the acquisition of long-lived assets are considered released from restriction on a straight-line basis over the estimated useful lives of the assets acquired.

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property and Equipment

Property, which consists of leasehold improvements, and equipment, which consists of office furniture and equipment, is stated at cost, if purchased or fair value at date of acquisition for donated property. Depreciation on equipment is computed using the straight line method over an estimated useful life of three to five year. Amortization of property is computed over the term of the lease. When assets are retired or otherwise dispose of, the recorded value and related accumulated depreciation or amortization is removed from the accounts and any resulting gain or loss is reflected as revenue or expense for the period.

Equipment purchased at a cost of less than \$1,000 is expensed when acquired.

Investments

The Foundation reports its investments at fair value, based on quoted market prices. Donated investments are recorded at their fair value on the date of donation. Investment income and realized and unrealized gains and losses are reflected on the statements of activities as investment income or loss.

Program-Related Investments

Program-related investments consist of notes receivable from organizations that conduct activities that fulfill the charitable purposes of the Foundation. Program-related investments are initially recorded on the statements of financial position at cost when approved. Uncollected interest earned on these notes receivable is recorded as earned accrued interest receivable, which is included in Prepaid Expenses and Other on the statements of financial position. Program-related investments are recoverable over periods ranging up to 15 years. Should the lender fail to make progress towards their program goals the Foundation can require repayment. In the event that a program-related investment is subsequently determined to be uncollectible or the value is permanently impaired, the Foundation may record the uncollectible amount as a grant appropriation or record an impairment reserve. There were no allowance or impairment reserve recorded for the years ended June 30, 2016 and 2015.

Interest in the Net Assets of The Minneapolis Foundation

The Foundation has an interest in the net assets of The Minneapolis Foundation Fund. Accounting for the benefits of the fund follows the provisions of Statement of Financial Accounting Standards relating to the *Transfers of Assets to a Not-for-Profit Foundation or Charitable Trust that Raises or Holds Contributions for Others*.

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Interest in the Net Assets of The Minneapolis Foundation (Continued)

The Minneapolis Foundation holds a fund for the benefit of the Foundation. The fund has two components; transfers to the fund by the Foundation and matching contributions to the fund by The Minneapolis Foundation. Funds transferred to the fund by the Foundation are recognized as an asset at the estimated fair market value by the Foundation and are classified as permanently restricted. Matching funds from The Minneapolis Foundation are recognized as an asset of The Minneapolis Foundation and are not reflected on the statements of financial position of the Foundation. Annual distributions related to this portion of the fund are reported as contributions to the Foundation in the period received and are recorded as temporarily restricted for grantmaking to indigenous-led organizations in Minnesota and Wisconsin. Annual adjustments to the fair values of the amounts reported as assets are recognized as gains or losses and affect unrestricted net assets.

Fair Value of Measurement

Fair value measurement standards established a framework for measuring fair value, a fair value hierarchy based on the quality of inputs used to measure fair value, and requires expanded disclosures about fair value measurements.

The Foundation accounts for its investments at fair value. The Foundation has categorized its investments, based on the priority of the inputs to the valuation technique, into a three-level fair value hierarchy.

The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument.

Financial assets and liabilities recorded on the statements of financial position are categorized based on the inputs to the valuation techniques as follows:

Level 1 – Financial assets and liabilities are valued using inputs that are unadjusted quoted prices in active markets accessible at the measurement date of identical financial assets and liabilities. The inputs include those traded on an active exchange, such as the New York Stock Exchange, as well as U.S. Treasury and other U.S. government and agency mortgage-backed securities that are traded by dealers or brokers in active over-the-counter markets.

Level 2 – Financial assets and liabilities are valued using inputs quoted prices for similar assets, or inputs that are observable, either directly or indirectly for substantially the full term through corroboration with observable market data. Level 2 includes private collateralized mortgage obligations, municipal bonds, and corporate debt securities.

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fair Value of Measurement (Continued)

Level 3 – Financial assets and liabilities are valued using pricing inputs which are unobservable for the asset, inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset. Level 3 includes private equity, venture capital, hedge funds and real estate. Securities valued using Level 3 inputs include fund held on behalf of Headwaters Foundation for Justice at The Minneapolis Foundation. The underlying securities held at the Minneapolis Foundation are valued using quote market prices; however, the Foundation's interest in the funds held is valued using additional inputs and assumptions.

Endowment Funds

Interpretation of Relevant Law – In approving endowment, spending and related policies, as part of the prudent and diligent discharge of its duties, The board of directors of the Foundation has relied upon the actions, reports, information, advice and counsel taken or provided by its duly constituted committees, the duly appointed officers the Foundation, and legal counsel, and in doing so has interpreted the law to require the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds, absent explicit donor direction to the contrary.

As a result of this interpretation, the Foundation 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 to the fund in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

In accordance with UPMIFA, the Foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

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 Foundation to retain as a fund of perpetual duration. In accordance with Generally Accepted Accounting Principles, deficiencies of this nature are reported in unrestricted net assets. Deficiencies result from unfavorable market fluctuations that may occur throughout the life of the investment and continued appropriation for certain programs deemed prudent by the board of directors. As of June 30, 2016 and 2015, there were deficiencies of \$264,310 and \$-0-, respectively.

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Endowment Funds (Continued)

Spending Policy and the Relationship of the Investment Objectives to the Spending Policy – The Foundation uses a total return concept in determining allowable distributions from the Endowment Funds, as follows:

General Endowment Fund and Fund of the Sacred Circle: Distributions are determined based on the Fund's average investment balance over 16 trailing quarters, using a distribution rate of 5% per annum.

Headwaters Foundation for Justice Fund of The Minneapolis Foundation: Headwaters may request distributions from the Fund. Distributions from the Fund will be at the discretion of The Minneapolis Foundation's Board of Trustees, but the Foundation will have the right to submit its recommendations with respect to distributions of income from the Fund. The Foundation's current policy is to distribute 4% of the trailing 12 quarter average fair market value of the Fund.

Return Objectives and Risk Parameters – The Foundation has adopted investment and spending policies that attempt to provide growth of principal value to support future income needs. The secondary objective is to provide current income during the formative years of the endowment. Endowment assets include those assets of donor-restricted funds that the Foundation must hold in perpetuity or for a donor-specified period 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 produce results that exceed the price and yield results of the S&P 500 index or the statistical universe for similar funds while assuming a moderate level of investment risk.

Strategies Employed for Achieving Objectives – To Satisfy its long-term rate-of-return objectives, the Foundation 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). The Foundation 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.

Endowment Distribution Policy

The Foundation uses total return concept in determining allowable distributions from the Endowment Funds, as follows:

General Endowment Fund and Fund of the Sacred Circle

Distributions are determined based on the Fund's average investment balance over 16 trailing quarters, using a distribution rate of 5% per annum.

**HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Endowment Distribution Policy (Continued)

Headwaters Foundation for Justice Fund of The Minneapolis Foundation

Headwaters may request distributions from the Fund. Distributions from the Fund will be at the discretion of The Minneapolis Foundation's Board of Trustees, but the Foundation will have the right to submit its recommendations with respect to distributions of income from the Fund. The Foundation's current policy is to distribute 4% of the trailing 12 quarter average fair market value of the Fund.

Grants

Grants are recognized as expenses when approved by the board of directors. Refunds and revisions of grants may occur when grant program needs are less than the awarded amount or the grantee does not meet grant requirements.

In-Kind Contributed Material and Services

Contributions of donated noncash assets are recorded at their fair values in the period received. Donated services are recognized as contributions if the services require specialized skills, are performed by persons with those skills and would otherwise be purchased. In-kind contributions consisted of in-kind goods and services of \$93,305 and \$62,218 at June 30, 2016 and 2015, respectively.

Functional Allocation of Expenses

The expenses incurred to provide the various programs and other activities have been summarized on a functional basis in the statements of functional expenses. Except for certain expenses allocated directly, expenses are allocated among the program and supporting services categories based upon estimate of time expended by employees in each functional area.

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 Exempt Status

The Foundation is tax-exempt under Section 501(c)(3) of the Internal Revenue Code (IRC) and Minnesota Statute 290.05. It is classified as a Foundation that is not a private foundation under Section 509(a)(2) of the IRC and contributions by donors are tax deductible.

**HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Tax Exempt Status (Continued)

The Foundation follows accounting standards for uncertain tax positions and files as a tax-exempt organization. During 2016 and 2015, the Foundation has not recognized any liability for uncertain tax positions. The Foundation's tax returns are subject to review and examination by federal and state authorities.

Subsequent Events

The Foundation has evaluated subsequent events from the statement of financial position date through September 26, 2016, the date at which the financial statements were available to be issued, and determined there are no other items to disclose.

NOTE 2 PLEDGES RECEIVABLE

Pledges receivable at June 30 are summarized as follows:

	2016	2015
Pledges Receivable	\$ 19,001	\$ 50,000
Less: Unamortized Discount	-	(512)
Net Pledges Receivable before Allowance	19,001	49,488
Allowance	-	(1,008)
Net Pledges Receivable	<u>\$ 19,001</u>	<u>\$ 48,480</u>

Multi-year commitments were discounted to present value using an imputed interest rate of 1.58%. At June 30, 2016, all pledges are due to be collected within one year.

NOTE 3 INVESTMENTS

Investments consisted of the following at June 30:

	2016	2015
Cash and Cash Equivalents	\$ 52,898	\$ 33,146
Domestic Equity	1,040,847	1,112,347
International Equity	500,786	515,837
Fixed Income	801,778	815,836
Equity Mutual Funds	612,809	674,227
Total	<u>\$ 3,009,118</u>	<u>\$ 3,151,393</u>

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 3 INVESTMENTS (CONTINUED)

Net investment return consisted of the following for the years ended June 30:

	2016	2015
Investment Income	\$ 50,604	\$ 88,544
Realized Gains	127,977	15
Net Unrealized Gains (Losses)	(154,917)	45,369
Net Investment Return	<u>\$ 23,664</u>	<u>\$ 133,928</u>

NOTE 4 PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at June 30:

	2016	2015
Office Furniture and Equipment	\$ 161,497	\$ 158,261
Accumulated Depreciation and Amortization	(134,623)	(126,449)
Net Property and Equipment	<u>\$ 26,874</u>	<u>\$ 31,812</u>

Depreciation and amortization expense totaled \$10,135 and \$8,494 for the years ended June 30, 2016 and 2015, respectively.

NOTE 5 FAIR VALUE MEASUREMENTS

The Foundation uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. For additional information on how the Foundation values all other assets and liabilities refer to Note 1 – Summary of Significant Accounting Policies.

Assets measured at fair value on a recurring basis at June 30 are as follows:

	2016			Total
	Level 1	Level 2	Level 3	
Investments:				
Domestic Equity	\$ 1,040,847	\$ -	\$ -	\$ 1,040,847
International Equity	500,786	-	-	500,786
Fixed Income	801,778	-	-	801,778
Equity Mutual Funds	315,264	297,545	-	612,809
Interest in the Net Assets of The Minneapolis Foundation	-	-	896,767	896,767
Total	<u>\$ 2,658,675</u>	<u>\$ 297,545</u>	<u>\$ 896,767</u>	<u>\$ 3,852,987</u>

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 5 FAIR VALUE MEASUREMENTS (CONTINUED)

	2015			Total
	Level 1	Level 2	Level 3	
Investments:				
Domestic Equity	\$ 1,112,347	\$ -	\$ -	\$ 1,112,347
International Equity	515,837	-	-	515,837
Fixed Income	815,836	-	-	815,836
Equity Mutual Funds	315,800	358,427	-	674,227
Interest in the Net Assets of The Minneapolis Foundation	-	-	960,143	960,143
Total	<u>\$ 2,759,820</u>	<u>\$ 358,427</u>	<u>\$ 960,143</u>	<u>\$ 4,078,390</u>

Assets Measured Using Net Asset Value per Share (or its Equivalent)

The Foundation values certain investment holdings at fair value using their net asset value and has the ability to redeem its investments with the investee at the net asset value per share (or its equivalent) at the measurement date.

Fair Value Measurements of Investments in Certain Entities That Calculate Net Asset Value per Share (or its Equivalent) as of June 30, 2016 and 2015:

	Net Asset Value	Unfunded Commitments	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Boston Common Small Cap Social Fund	\$ 297,545	-	90 days	Monthly

Boston Common Small Cap Social Fund invests primarily in socially screened U.S. small capitalization equity securities with low valuations. The objective of the Fund is to achieve long-term capital appreciation and the fair value of the fund is estimated using the net asset value per share of the investments.

The Foundation's interest in the net assets of The Minneapolis Foundation have been estimated by management in the absence of readily determinable market values based on information provided by the fund manager. The following table presents the changes in the fair value of the Interest in the Net Assets of The Minneapolis Foundation, Level 3 financial assets for the years ended June30:

	2016	2015
Balance at the Beginning of the Year	\$ 960,143	\$ 969,165
Change in Beneficial Interests in The Minneapolis Foundation Fund	(19,656)	23,926
Distributions	(43,720)	(32,948)
Balance at the End of the Year	<u>\$ 896,767</u>	<u>\$ 960,143</u>

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 6 PROGRAM-RELATED INVESTMENTS

Program-related investments consist of the following notes receivable at June 30:

	<u>2016</u>	<u>2015</u>
Nonprofit Assistance Fund:		
Matures September 2015	\$ -	\$ 225,834
Matures September 2016	100,834	-
Matures September 2018	125,000	-
Community Reinvestment Fund:		
Matures September 2016	-	100,000
Matures September 2017	125,000	125,000
Matures November 2018	60,000	60,000
Total	<u>\$ 410,834</u>	<u>\$ 510,834</u>

NOTE 7 ENDOWMENT COMPOSITION AND CHANGES TO ENDOWMENT NET ASSETS

Endowment net assets consisted of the following donor established funds as of June 30:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2016 Total</u>
General Endowment	\$ (205,143)	\$ -	\$ 3,186,156	\$ 2,981,013
Fund of the Sacred Circle	-	24,865	306,922	331,787
Interest in the Net Assets of The Minneapolis Foundation	(59,167)	-	918,902	859,735
Total	<u>\$ (264,310)</u>	<u>\$ 24,865</u>	<u>\$ 4,411,980</u>	<u>\$ 4,172,535</u>

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2015 Total</u>
General Endowment	\$ -	\$ 93,931	\$ 3,186,156	\$ 3,280,087
Fund of the Sacred Circle	-	25,401	306,922	332,323
Interest in the Net Assets of The Minneapolis Foundation	-	4,210	918,902	923,112
Total	<u>\$ -</u>	<u>\$ 123,542</u>	<u>\$ 4,411,980</u>	<u>\$ 4,535,522</u>

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

**NOTE 7 ENDOWMENT COMPOSITION AND CHANGES TO ENDOWMENT NET ASSETS
(CONTINUED)**

Changes in net assets consisted of the following for the years ended June 30:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment Investments				
July 1, 2014	\$ -	\$ 235,448	\$ 3,790,475	\$ 4,025,923
Investment Return:				
Net Investment Income	139,642	47,115	-	186,757
Change in Interest in Net Assets of The Minneapolis Foundation	<u>32,947</u>	<u>(9,021)</u>	<u>-</u>	<u>23,926</u>
Total Investment Return	172,589	38,094	-	210,683
Contributions	-	-	621,505	621,505
Endowment Loan	-	(150,000)	-	(150,000)
Provision for Uncollectible Pledges	-	-	-	-
Appropriations of Endowment Assets for Expenditure	<u>(172,589)</u>	<u>-</u>	<u>-</u>	<u>(172,589)</u>
Endowment Investments				
June 30, 2015	-	123,542	4,411,980	4,535,522
Investment Return:				
Net Investment Loss	(61,830)	(94,467)	-	(156,297)
Change in Interest in Net Assets of The Minneapolis Foundation	<u>(15,446)</u>	<u>(4,210)</u>	<u>-</u>	<u>(19,656)</u>
Total Investment Return	(77,276)	(98,677)	-	(175,953)
Contributions	-	-	-	-
Endowment Loan	-	-	-	-
Provision for Uncollectible Pledges	-	-	-	-
Appropriations of Endowment Assets for Expenditure	<u>(187,034)</u>	<u>-</u>	<u>-</u>	<u>(187,034)</u>
Endowment Investments				
June 30, 2016	<u>\$ (264,310)</u>	<u>\$ 24,865</u>	<u>\$ 4,411,980</u>	<u>\$ 4,172,535</u>

During 2015, the Foundation borrowed \$150,000 from endowment assets to be used as working capital. The loan is intended to provide an internal source of funds for fluctuating cash needs during the fiscal year 2016. The Foundation plans to accrue monthly interest at 3% rate based on the monthly balance of the amount loan until it is repaid.

**HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015**

NOTE 8 NET ASSETS

Temporarily Restricted

Temporarily restricted net assets consisted of the following:

	2016	2015
Fund of the Sacred Circle Endowment	\$ 24,865	\$ 25,401
Restricted for Time	87,499	40,000
Endowment Funds	-	98,141
Social Change Fund	-	9,490
Giving Project	37,500	-
Listening Project	25,000	-
Total	<u>\$ 174,864</u>	<u>\$ 173,032</u>

Restrictions Released

Net assets restrictions were released as a result of the following conditions being met:

	2016	2015
Time	\$ 112,500	\$ 71,674
Purpose:		
Social Change Fund	9,491	63,286
African American Leadership Forum	-	277,959
Endowment Loan and Program Purposes	-	171,723
Total	<u>\$ 121,991</u>	<u>\$ 584,642</u>

Permanently Restricted

Permanently restricted net assets consisted of the following:

	2016	2015
General Endowment	\$ 3,186,156	\$ 3,186,156
Fund of the Sacred Circle	306,922	306,922
Headwaters Foundation for Justice		
Fund of the Minneapolis Foundation	918,902	918,902
Total	<u>\$ 4,411,980</u>	<u>\$ 4,411,980</u>

NOTE 9 DONOR ADVISED FUNDS

The Foundation held donor advised funds amounting to \$425,018 and \$933,326 as of June 30, 2016 and 2015, respectively. Donors of the funds have the right to advise the Foundation related to grants from the funds; however, The Foundation's Board of Directors retains the right to direct the grants. The donor advised funds are included within Unrestricted net assets on the statements of financial position.

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 10 RETIREMENT PLAN

Employees of the Foundation meeting certain eligibility requirements are eligible to participate in a contributory 401(k) retirement plan. The Foundation contributes a discretionary amount to the plan which was \$19,557 and \$18,082 for the years ended June 30, 2016 and 2015, respectively.

NOTE 11 OPERATING LEASES

The Foundation leases office space under a lease that calls for escalating lease payments through September 30, 2020. The Foundation has subleased portions of office space to four sub-lessees under agreements with expiration dates through June 30, 2015.

Rent expense totaled \$20,665 and \$50,987, net of sublease income of \$69,614 and \$38,749 for the years ended June 30, 2016 and 2015, respectively.

Future minimum lease payments are as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2017	\$ 69,843
2018	56,945
2019	59,457
2020	61,969
2021	64,483
Thereafter	17,533
Total	<u>\$ 330,230</u>

As of June 30, 2016, future minimum lease payments of the long-term subleases are as follows:

<u>Year Ending June 30,</u>	<u>Amount</u>
2017	\$ 73,129
2018	25,835
2019	26,739
2020	27,675
2021	4,639
Total	<u>\$ 158,016</u>

NOTE 12 CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject Headwaters Foundation for Justice to concentrations of credit risk consist principally of temporary cash investments and pledges receivable. The Foundation places its temporary cash investments with high quality financial institutions and seeks to limit the amount of credit exposure to any one financial institution.

HEADWATERS FOUNDATION FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

NOTE 13 INTEREST IN THE NET ASSETS OF THE MINNEAPOLIS FOUNDATION FUND

The Foundation has established a fund with The Minneapolis Foundation, under terms of the agreement and Memorandum of Understanding. The Minneapolis Foundation has established a separate fund known as the “Headwaters Foundation for Justice Fund” (the Fund). Amounts contributed by the Foundation to the Fund will be matched, up to \$750,000, by contributions to the Fund from The Minneapolis Foundation. The Fund will be used in carrying out its charitable purposes, especially with respect to funding social justice programs as reflected by Headwaters Foundation’s existing and historical grantmaking and capacity building programs and initiatives. As previously mentioned in Note 1, distributions from the Fund will be at the discretion of The Minneapolis Foundation’s Board of Trustees, but the Headwaters Foundation will have the right to submit its recommendations with respect to distributions of income from the Fund. The value of the underlying assets of the Fund, including the portion contributed by The Minneapolis Foundation, was \$1,793,287 and \$1,920,021 at June 30, 2016 and 2015, respectively.

The plan governing the administration of the Fund indicates The Minneapolis Foundation’s Board of Trustees has the power to modify or eliminate any restriction, condition, limitation or trust imposed with respect to the Fund, if, in the sole judgment of the Board of Trustees, such restriction, condition, limitation or trust becomes necessary, incapable of fulfillment or inconsistent with the charitable needs of the community served by The Minneapolis Foundation.

That portion of the funds derived from amounts placed in the funds by the Headwaters Foundation for Justice are included in the statement of financial position. The balance of the funds are derived from the matching amounts placed there by the Minneapolis Foundation are not included in statements of financial position due to the variance power they hold.

NOTE 14 RELATED PARTY TRANSACTIONS

Headwaters Foundation for Justice received \$180,253 and \$122,013 in contributions from board members during the years ended June 30, 2016 and 2015, respectively.