Polk Bros. Foundation, Inc.

Financial Report

August 31, 2018

Contents

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Independent Auditor's Report

To the Board of Directors
Polk Bros. Foundation, Inc.

We have audited the accompanying financial statements of Polk Bros. Foundation, Inc. (the "Foundation"), which comprise the statement of financial position as of August 31, 2018 and 2017 and the related statements of activities and changes in net assets 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.

Auditor's 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 auditor's 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Polk Bros. Foundation, Inc. as of August 31, 2018 and 2017 and the change 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.

Emphasis of Matter

As disclosed in Note 3, the financial statements include investments valued at net asset value of $112.1 million (26 percent of net assets) at August 31, 2018 and of $119.2 million (27 percent of net assets) at August 31, 2017, whose fair value has been estimated in the absence of observable inputs used to determine the market value. Management's estimates are based on information provided by the investment managers. Our opinion is not modified with respect to this matter.

Plante & Moran, PLLC

November 6, 2018

Statement of Financial Position

August 31, 2018 and 2017

	2018	2017
Assets		
Current Assets		
Cash and cash equivalents	$ 4,261,350	$ 4,078,144
Investments	428,662,957	430,804,550
Other assets - Prepaid excise and income taxes	-	106,000
Total assets	**$ 432,924,307**	**$ 434,988,694**
Liabilities and Net Assets		
Current Liabilities		
Deferred excise tax	$ 1,030,000	$ 1,162,000
Income taxes payable	58,000	-
Total current liabilities	1,088,000	1,162,000
Net Assets - Unrestricted	431,836,307	433,826,694
Total liabilities and net assets	**$ 432,924,307**	**$ 434,988,694**

See notes to financial statements.

Statement of Activities and Changes in Net Assets

Years Ended August 31, 2018 and 2017

	2018	2017
Changes in Unrestricted Net Assets		
Revenue, gains, and other support:		
Dividends from investments other than partnerships	$ 1,725,466	$ 1,894,746
Interest from investments other than partnerships	77,851	27,431
Net realized gains from partnerships	24,550,837	3,612,349
Net realized gains from sales of securities other than partnerships	4,290,725	3,480,594
Unrealized (losses) gains from investments	(2,892,918)	30,001,379
Capital gain dividends	2,831,806	2,565,030
Miscellaneous income	2,519	15,660
Total revenue, gains, and other support	30,586,286	41,597,189
Grants and other expenses:		
Grants	27,932,834	27,759,335
Support services:		
Administrative expenses	3,089,118	2,820,015
Investment expenses	1,253,595	1,160,979
Deferred excise tax (income) expense	(132,000)	207,300
Provision for excise and income taxes	433,126	224,787
Total grants and other expenses	32,576,673	32,172,416
(Decrease) Increase in Net Assets	(1,990,387)	9,424,773
Net Assets - Beginning of year	433,826,694	424,401,921
Net Assets - End of year	**$ 431,836,307**	**$ 433,826,694**

Statement of Cash Flows

Years Ended August 31, 2018 and 2017

	2018	2017
Cash Flows from Operating Activities		
(Decrease) increase in net assets	$ (1,990,387)	$ 9,424,773
Adjustments to reconcile (decrease) increase in net assets to net cash and cash equivalents from operating activities:		
Net realized gains from partnerships	(24,550,837)	(3,612,349)
Net realized gains from sales of securities	(4,290,725)	(3,480,594)
Change in unrealized gains on investments	2,892,918	(30,001,379)
Investments redeemed for fees	953,595	873,479
Prepaid excise and income taxes	106,000	(46,000)
Dividends receivable	(45,041)	(2,511)
Deferred excise tax	(132,000)	207,300
Excise and income taxes payable	58,000	-
Net cash used in operating activities	(26,998,477)	(26,637,281)
Cash Flows from Investing Activities		
Proceeds from sales of securities	24,212,226	25,093,323
Purchases of securities	(32,524,903)	(28,548,137)
Purchases of partnership interests	(35,035,200)	(24,452,324)
Liquidating distributions and return of capital from partnerships	70,529,560	54,154,799
Net cash provided by investing activities	27,181,683	26,247,661
Net Increase (Decrease) in Cash and Cash Equivalents	183,206	(389,620)
Cash and Cash Equivalents - Beginning of year	4,078,144	4,467,764
Cash and Cash Equivalents - End of year	**$ 4,261,350**	**$ 4,078,144**
Supplemental Disclosure of Cash Flow Information - Cash paid for taxes	$ 270,326	$ 271,153

See notes to financial statements.

Note 1 - Nature of Business

Polk Bros. Foundation, Inc. (the "Foundation") is a private independent foundation dedicated to building and strengthening Chicago's families and communities, especially those most affected by poverty. The Foundation focuses its work at the intersection of Chicago's most pressing issues to address the complex roots and devastating effects of poverty, challenge inequity, and ensure that all Chicagoans have the opportunity to reach their full potential. Since its founding in 1988, the Foundation has partnered with more than 3,000 Chicago nonprofits to build strong communities and families, increase access to quality education and the arts, improve health, and strengthen organizations and the sectors in which they work.

Note 2 - Significant Accounting Policies

Basis of Presentation

The financial statements of the Foundation have been prepared on the basis of generally accepted accounting principles (GAAP). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect amounts reported in the financial statements. Actual results could differ from those estimates.

Classification of Net Assets

Net assets are classified as unrestricted, temporarily restricted, or permanently restricted depending on the presence and characteristics of donor-imposed restrictions. The Foundation's net assets consisted only of unrestricted net assets as of August 31, 2018 and 2017.

Cash and Cash Equivalents

The Foundation considers all highly liquid investments purchased with original maturities of three months or less to be cash equivalents. The Foundation maintains its cash equivalents in bank deposit accounts, which exceed federally insured limits. Substantially all of the Foundation's cash equivalents are held at Northern Trust. The Foundation has not experienced any losses in such accounts. The Foundation believes it is not exposed to any significant credit risk on cash equivalents.

Investments

Investments are reported at fair value. Investment income or loss (including realized gains and losses on investments, changes in unrealized holding gains and losses, interest, and dividends) on investments is included in the statement of activities and changes in net assets and is recorded on the accrual basis of accounting. Gains and losses on securities transactions are accounted for using the specific identification method.

Net realized gains and losses from sales of securities and from the sale of shares distributed by certain limited partnership investments are separately presented in the statement of activities and changes in net assets.

The Foundation's investments are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to these risk factors, it is reasonably possible that changes in value of investments will occur in the near term and could materially affect the amounts reported in the financial statements.

Furniture and Equipment

Purchases of furniture, equipment, and leasehold improvements are charged to expense rather than capitalized. As a result, depreciation expense is not reflected in the financial statements. This policy does not have a material effect on the financial statements as a whole.

Note 2 - Significant Accounting Policies (Continued)

Deferred Excise Taxes

The Foundation provides for deferred excise taxes, which represent taxes on the net unrealized appreciation of investments using a 1 percent rate for the years ended August 31, 2018 and 2017.

Income Taxes

The Foundation is exempt from federal income taxes under Section 501(c)(3) of the United States Internal Revenue Code. As a private Foundation, the Foundation is subject to an excise tax of 2 percent on net investment income or 1 percent if the Foundation meets certain specified distribution requirements. In addition, the Foundation is subject to unrelated business income taxes on a portion of the income provided by certain investment partnerships. Total current federal excise tax expense for the years ended August 31, 2018 and 2017 was $429,719 and $194,036, respectively. Total deferred federal excise tax income was $132,000 for the year ended August 31, 2018, and total deferred federal excise tax expense was $207,300 for the year ended August 31, 2017.

Functional Allocation of Expenses

Costs of providing the program and support services have been reported on a functional basis in the statement of activities and changes in net assets. Costs have been allocated between the various programs and support services on several bases and estimates. Although the methods of allocation used are considered appropriate, other methods could be used that would produce different amounts.

Upcoming Accounting Pronouncements

The Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, *Leases*, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-to-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease-related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the Foundation's year ending August 31, 2021 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The change will not have a material impact on the financial statements of the Foundation.

In August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. ASU No. 2016-14 requires significant changes to the financial reporting model of organizations that follow FASB not-for-profit rules, including changing from three classes of net assets to two classes: net assets with donor restrictions and net assets without donor restrictions. The ASU will also require changes in the way certain information is aggregated and reported by the Foundation, including required disclosures about the liquidity and availability of resources. The new standard is effective for the Foundation’s year ending August 31, 2019 and thereafter and must be applied on a retrospective basis. The Foundation is currently gathering appropriate information to implement those disclosure changes in a timely manner.

Subsequent Events

The financial statements and related disclosures include evaluation of events up through and including November 6, 2018, which is the date the financial statements were available to be issued.

Note 3 - Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in the financial statements and provide a framework for establishing that fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

The following tables present information about the Foundation's assets measured at fair value on a recurring basis at August 31, 2018 and 2017 and the valuation techniques used by the Foundation to determine those fair values.

Fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that the Foundation has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets and other inputs, such as interest rates and yield curves, that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, or similar techniques taking into account the characteristics of the asset.

Net asset value inputs include interests in investment companies at year end whereby the fair value of the investment held is estimated based on net asset value per share (or its equivalent) of the investment company.

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Foundation's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

	Assets Measured at Fair Value on a Recurring Basis at August 31, 2018			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at August 31, 2018
Common stock funds	$ 84,087,728	$ -	$ -	$ 84,087,728
Fixed-income partnerships and funds	28,374,514	-	-	28,374,514
Total	$ 112,462,242	$ -	$ -	112,462,242
Alternative investments - Measured at NAV:				
Private equity partnerships and funds				62,197,543
Hedged equity partnerships and funds				70,896,309
Absolute return partnerships and funds				55,108,980
Real estate partnerships and funds				15,424,752
Commodity partnerships and funds				23,665,564
Fixed-income partnerships and funds				10,804,334
Domestic and international equity partnerships and funds				78,103,233
Total alternative investments - Measured at NAV				316,200,715
Total assets				$ 428,662,957

Note 3 - Fair Value Measurements (Continued)

	Assets Measured at Fair Value on a Recurring Basis at August 31, 2017			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at August 31, 2017
Common stock funds	$ 80,750,303	$ -	$ -	$ 80,750,303
Fixed-income partnerships and funds	26,537,302	-	-	26,537,302
Total	$ 107,287,605	$ -	$ -	107,287,605
Alternative investments - Measured at NAV:				
Private equity partnerships and funds				49,799,618
Hedged equity partnerships and funds				65,255,310
Absolute return equity partnerships and funds				63,264,708
Real estate partnerships and funds				18,531,614
Commodity partnerships and funds				31,998,638
Fixed-income partnerships and funds				18,890,527
Domestic and international equity partnerships and funds				75,776,530
Total alternative investments - Measured at NAV				323,516,945
Total assets				$ 430,804,550

As of August 31, 2018 and 2017, investments valued at NAV of $112.1 million and $119.2 million, respectively, were valued in the absence of observable inputs used to determine market value.

Level 1

Estimated fair values for the Foundation's common stock funds and a portion of the fixed-income funds and partnerships are based on quoted market prices in active markets.

Investments in Partnerships and Funds that Calculate Net Asset Value per Share

The Foundation holds shares or interests in investment companies at year end whereby the fair value of the investment held is estimated based on net asset value per share (or its equivalent) of the investment company.

Note 3 - Fair Value Measurements (Continued)

At year end, the fair value, unfunded commitments, and redemption rules for investments held at NAV are as follows:

	August 31, 2018	August 31, 2017	August 31, 2018		
	Fair Value	Fair Value	Unfunded Commitments	Redemption Frequency, if Eligible	Redemption Notice Period
Private equity partnerships and funds (a)	$ 62,197,543	$ 49,799,618	$ 47,151,029	N/A	N/A
Hedged equity partnerships and funds (b)	70,896,309	65,255,310	-	Monthly, quarterly, semiannually, annually	30-90 days
Absolute return partnerships and funds (c)	55,108,980	63,264,708	-	Monthly, quarterly, semiannually, annually	30-100 days
Real estate partnerships and funds (a)	15,424,752	18,531,614	9,338,949	N/A	N/A
Commodity partnerships and funds (a)	23,665,564	31,998,638	14,585,866	N/A	N/A
Fixed-income partnerships and funds (d)	10,804,334	18,890,527	-	Annually	90 days
Domestic and international equity partnerships and funds (e)	78,103,233	75,776,530	-	Weekly, monthly, quarterly	6-90 days
Total	$ 316,200,715	$ 323,516,945	$ 71,075,844		

(a) This category includes private equity, real estate, and commodities partnerships and funds. These investments are not redeemable. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets in the funds. The remaining terms of these investments range up to in excess of 10 years. The fair values of the investments in this category have been estimated using net asset value as the practical expedient provided by the investment managers.

(b) This category includes investments in hedge funds and partnerships, which invest both long and short, primarily in publicly traded securities. The fair values of the investments in this category have been estimated using net asset value of the investments. As of August 31, 2018, all of the investments in this category have passed their initial lockup periods. Some of the investments in this category include fewer liquid assets, which may be restricted from redemption until the asset is realized.

(c) This category includes absolute return partnerships and funds, which invest in a variety of strategies and securities with the objective of achieving an absolute level of return. The fair values of the investments in this category have been estimated using net asset value of the investments. As of August 31, 2018, all of the investments in this category except one (with a net asset value of $9,720,566) have passed their initial lockup periods. Some of the investments in this category include fewer liquid assets, which may be restricted from redemption until the asset is realized.

(d) This category includes investments in fixed-income partnerships and funds, which focus on global fixed-income arbitrage opportunities overlaying specified benchmarks, including the S&P 500 index and T-bills. The fair values of the investments in this category have been estimated using net asset value of the investments. As of August 31, 2018, all of the investments in this category can be redeemed annually.

(e) This category includes investments in partnerships and funds, which focus primarily on long-only investments in domestic and international equity securities, as well as investments in international fixed-income securities. The fair values of the investments in this category have been estimated using net asset value of the investments. As of August 31, 2018, all of the investments in this category can be redeemed weekly, monthly, or quarterly.

Note 4 - Investments

Investments consisted of the following at August 31, 2018:

	2018	
	Cost	Fair Value
Investments:		
Common stock funds	$ 69,802,316	$ 84,087,728
Fixed-income partnerships and funds	35,452,284	39,178,848
Private equity partnerships and funds	43,944,344	62,197,543
Hedged equity partnerships and funds	32,332,367	70,896,309
Absolute return equity partnerships and funds	46,119,613	55,108,980
Real estate partnerships and funds	11,664,587	15,424,752
Commodity partnerships and funds	26,268,989	23,665,564
Domestic and international equity partnerships and funds	60,070,225	78,103,233
Total	$ 325,654,725	$ 428,662,957

Investments consisted of the following at August 31, 2017:

	2017	
	Cost	Fair Value
Investments:		
Common stock funds	$ 63,908,674	$ 80,750,303
Fixed-income partnerships and funds	39,152,712	45,427,829
Private equity partnerships and funds	33,707,005	49,799,618
Hedged equity partnerships and funds	32,123,167	65,255,310
Absolute return equity partnerships and funds	43,828,640	63,264,708
Real estate partnerships and funds	14,971,125	18,531,614
Commodity partnerships and funds	27,347,145	31,998,638
Domestic and international equity partnerships and funds	59,608,680	75,776,530
Total	$ 314,647,148	$ 430,804,550

Note 5 - Income from Partnerships/Gain from All Investments

A summary of the composition of the Foundation's income from partnerships from their individual tax returns is included below, along with a reconciliation to total gains from all investments:

	2018	2017
Partnerships		
Realized gains from partnerships	$ 24,550,837	$ 3,612,349
Other sources of income from tax returns that are part of the Foundation's unrealized gains	10,256,258	9,575,682
Total income from tax returns	34,807,095	13,188,031
Additional change in unrealized (losses) gains	(10,006,097)	17,534,611
Total income from partnerships	24,800,998	30,722,642
Net realized gain from sales of securities other than partnerships	4,290,725	3,480,594
Capital gain dividends	2,831,806	2,565,030
Change in unrealized (loss) gain from investments other than partnerships	(3,143,079)	2,891,086
Total gain on investments	$ 28,780,450	$ 39,659,352

Note 6 - Lease Commitments

The Foundation is obligated under an operating lease for its office space in Chicago through June 30, 2027.

The future minimum lease payments are as follows:

Years Ending August 31	Amount
2019	$ 151,300
2020	154,329
2021	157,479
2022	160,871
2023	163,784
Thereafter	658,473
Total	$ 1,446,236

Occupancy expense for 2018 and 2017 was $144,839 and $167,384, respectively.

Note 7 - Grants Approved but Not Paid

The Foundation has conditionally approved future grant commitments of $9,297,500 and $14,110,000 for the years ended August 31, 2018 and 2017, respectively. These amounts have not been recorded as liabilities because all grants are formally awarded on a year-by-year basis. In addition, the Foundation reserves the right to cancel a grant at any time if it determines that the organization receiving the grant is not administering the project and grant funds in accordance with the proposal approved by the Foundation's board.

Note 8 - Retirement Plan

The Foundation sponsors a defined contribution 401(k) plan for all eligible employees, as defined. The employees may make elective contributions to the 401(k) plan in accordance with IRS regulations. The Foundation made contributions to the 401(k) plan equal to between 10 and 12 percent of the eligible participants' compensation for 2018 and 2017.

Retirement plan expense for the years ended August 31, 2018 and 2017 amounted to $190,977 and $165,479, respectively.