

Children's Discovery Museum of San Jose

Financial Statements

August 31, 2018



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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Children's Discovery Museum of San Jose
San Jose, California

We have audited the accompanying financial statements of Children's Discovery Museum of San Jose (a California nonprofit corporation) (the "Museum"), which comprise the statement of financial position as of August 31, 2018, and the related statements of activities, functional expenses, and cash flows for the year 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 audit. We conducted our audit 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 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 Children's Discovery Museum of San Jose as of August 31, 2018, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads "Armanino LLP". The signature is written in a cursive, flowing style.

Armanino^{LLP}
San Jose, California

January 17, 2019

Children's Discovery Museum of San Jose
Statement of Financial Position
August 31, 2018

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
ASSETS				
Current assets				
Cash and cash equivalents	\$ 1,753,528	\$ 413,796	\$ -	\$ 2,167,324
Contributions receivable, current portion	250,457	686,862	-	937,319
Donated rent receivable, current portion	-	153,722	-	153,722
Inventory	45,109	-	-	45,109
Prepaid expenses	177,590	-	-	177,590
Other current assets	3,870	-	-	3,870
Total current assets	<u>2,230,554</u>	<u>1,254,380</u>	<u>-</u>	<u>3,484,934</u>
Property and equipment, net	<u>8,204,687</u>	<u>-</u>	<u>-</u>	<u>8,204,687</u>
Other assets				
Investments	4,570,652	250,578	1,161,095	5,982,325
Contributions receivable, net of current portion	17,259	270,345	-	287,604
Donated rent receivable, net of current portion	-	8,323,475	-	8,323,475
Total other assets	<u>4,587,911</u>	<u>8,844,398</u>	<u>1,161,095</u>	<u>14,593,404</u>
Total assets	<u>\$ 15,023,152</u>	<u>\$ 10,098,778</u>	<u>\$ 1,161,095</u>	<u>\$ 26,283,025</u>
LIABILITIES AND NET ASSETS				
Current liabilities				
Accounts payable and accrued liabilities	\$ 98,638	\$ -	\$ -	\$ 98,638
Accrued payroll and related benefits	552,341	-	-	552,341
Deferred revenue	75,815	-	-	75,815
Customer deposits	17,738	-	-	17,738
Total current liabilities	<u>744,532</u>	<u>-</u>	<u>-</u>	<u>744,532</u>
Net assets				
Unrestricted				
Board-designated				
Endowment	3,073,933	-	-	3,073,933
Operating reserve	2,000,000	-	-	2,000,000
Fixed asset reserve	1,000,000	-	-	1,000,000
Total board-designated	<u>6,073,933</u>	<u>-</u>	<u>-</u>	<u>6,073,933</u>
Property and equipment	8,204,687	-	-	8,204,687
Total unrestricted	<u>14,278,620</u>	<u>-</u>	<u>-</u>	<u>14,278,620</u>
Temporarily restricted	-	10,098,778	-	10,098,778
Permanently restricted	-	-	1,161,095	1,161,095
Total net assets	<u>14,278,620</u>	<u>10,098,778</u>	<u>1,161,095</u>	<u>25,538,493</u>
Total liabilities and net assets	<u>\$ 15,023,152</u>	<u>\$ 10,098,778</u>	<u>\$ 1,161,095</u>	<u>\$ 26,283,025</u>

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

Children's Discovery Museum of San Jose
Statement of Activities
For the Year Ended August 31, 2018

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Support and revenue				
Support				
Grants and contributions	\$ 1,109,310	\$ 1,752,063	\$ -	\$ 2,861,373
Special events, net of \$123,197	1,307,949	-	-	1,307,949
Donations in-kind	<u>604,741</u>	<u>-</u>	<u>-</u>	<u>604,741</u>
Total support	<u>3,022,000</u>	<u>1,752,063</u>	<u>-</u>	<u>4,774,063</u>
Revenue				
Admissions	2,210,216	-	-	2,210,216
Membership	1,046,658	-	-	1,046,658
Net realized and unrealized gain on investments	496,101	4,025	-	500,126
Other income	486,151	-	-	486,151
Retail services	297,379	-	-	297,379
Interest and dividends	132,338	17,062	-	149,400
Program fees	148,117	-	-	148,117
Exhibit rental	<u>15,160</u>	<u>-</u>	<u>-</u>	<u>15,160</u>
Total revenue	<u>4,832,120</u>	<u>21,087</u>	<u>-</u>	<u>4,853,207</u>
Total support and revenue	7,854,120	1,773,150	-	9,627,270
Net assets released from restriction	<u>1,732,477</u>	<u>(1,732,477)</u>	<u>-</u>	<u>-</u>
Total support, revenue, and net assets released from restriction	<u>9,586,597</u>	<u>40,673</u>	<u>-</u>	<u>9,627,270</u>
Functional expenses				
Program services				
Exhibits	2,801,814	-	-	2,801,814
Educational programs	4,460,551	-	-	4,460,551
Retail services	<u>438,397</u>	<u>-</u>	<u>-</u>	<u>438,397</u>
Total program services	<u>7,700,762</u>	<u>-</u>	<u>-</u>	<u>7,700,762</u>
Supporting services				
Management and general	1,326,808	-	-	1,326,808
Development and fundraising	<u>487,823</u>	<u>-</u>	<u>-</u>	<u>487,823</u>
Total supporting services	<u>1,814,631</u>	<u>-</u>	<u>-</u>	<u>1,814,631</u>
Total functional expenses	<u>9,515,393</u>	<u>-</u>	<u>-</u>	<u>9,515,393</u>
Change in net assets	71,204	40,673	-	111,877
Net assets, beginning of year	<u>14,207,416</u>	<u>10,058,105</u>	<u>1,161,095</u>	<u>25,426,616</u>
Net assets, end of year	<u>\$ 14,278,620</u>	<u>\$ 10,098,778</u>	<u>\$ 1,161,095</u>	<u>\$ 25,538,493</u>

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

Children's Discovery Museum of San Jose
Statement of Functional Expenses
For the Year Ended August 31, 2018

	Program Services				Supporting Services			Total
	Exhibits	Educational Programs	Retail Services	Total Program Services	Management and General	Development and Fundraising	Total Supporting Services	
Expenses								
Salaries and benefits								
Salaries	\$ 405,004	\$ 2,612,024	\$ 124,297	\$ 3,141,325	\$ 581,375	\$ 228,569	\$ 809,944	\$ 3,951,269
Employee benefits	48,688	122,953	25,111	196,752	113,704	38,479	152,183	348,935
Payroll taxes	29,207	197,920	9,381	236,508	41,387	14,263	55,650	292,158
Total salaries and benefits	482,899	2,932,897	158,789	3,574,585	736,466	281,311	1,017,777	4,592,362
Occupancy	324,000	288,000	14,400	626,400	72,000	21,600	93,600	720,000
Repairs and maintenance	393,044	251,647	21,388	666,079	33,793	14,029	47,822	713,901
Outside services	41,188	226,607	21,710	289,505	262,229	69,569	331,798	621,303
Small equipment	240,031	228,634	1,283	469,948	26,427	6,176	32,603	502,551
Printing	6,983	230,014	637	237,634	1,902	860	2,762	240,396
Utilities	130,218	76,346	6,735	213,299	6,740	4,491	11,231	224,530
Cost of goods sold	-	-	153,898	153,898	-	-	-	153,898
Conferences and meetings	18,819	29,239	6,235	54,293	11,079	15,701	26,780	81,073
Insurance	38,068	25,377	1,912	65,357	3,239	1,551	4,790	70,147
Travel	3,159	37,493	490	41,142	266	-	266	41,408
Telephone	5,434	13,438	2,467	21,339	7,150	5,858	13,008	34,347
Dues and subscriptions	2,451	4,367	1,104	7,922	18,655	869	19,524	27,446
Office supplies	1,670	5,066	987	7,723	2,904	6,121	9,025	16,748
Postage and shipping	1,848	2,602	4,561	9,011	897	1,700	2,597	11,608
Training	-	-	-	-	10,605	-	10,605	10,605
Automobile	2,821	1,085	-	3,906	-	-	-	3,906
Expenses before depreciation	1,692,633	4,352,812	396,596	6,442,041	1,194,352	429,836	1,624,188	8,066,229
Depreciation	1,109,181	107,739	41,801	1,258,721	132,456	57,987	190,443	1,449,164
Total expenses	<u>\$ 2,801,814</u>	<u>\$ 4,460,551</u>	<u>\$ 438,397</u>	<u>\$ 7,700,762</u>	<u>\$ 1,326,808</u>	<u>\$ 487,823</u>	<u>\$ 1,814,631</u>	<u>\$ 9,515,393</u>
Percentage of total	<u>29.4 %</u>	<u>46.9 %</u>	<u>4.6 %</u>	<u>80.9 %</u>	<u>14.0 %</u>	<u>5.1 %</u>	<u>19.1 %</u>	<u>100.0 %</u>

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

Children's Discovery Museum of San Jose
Statement of Cash Flows
For the Year Ended August 31, 2018

Cash flows from operating activities	\$ 111,877
Change in net assets	\$ 111,877
Adjustments to reconcile change in net assets to net cash used in operating activities	
Net realized and unrealized gain on investments	(500,126)
Proceeds from contributions restricted for purchase of property and equipment	(1,239,718)
Depreciation	1,449,164
Donated rent receivable	144,098
Changes in operating assets and liabilities	
Contributions receivable	372,338
Inventory	(1,644)
Prepaid expenses	(4,379)
Accounts payable and accrued liabilities	(323,571)
Accrued payroll and related benefits	(7,186)
Deferred revenue	(1,393)
Customer deposits	(3,762)
Net cash used in operating activities	<u>(4,302)</u>
Cash flows from investing activities	
Purchase of investments	(4,141,999)
Proceeds from sale of investments	4,620,141
Purchase of property and equipment	(1,157,749)
Net cash used in investing activities	<u>(679,607)</u>
Cash flows from financing activities	
Proceeds from contributions restricted for purchase of property and equipment	<u>1,239,718</u>
Net cash provided by financing activities	<u>1,239,718</u>
Net increase in cash and cash equivalents	555,809
Cash and cash equivalents, beginning of year	<u>1,611,515</u>
Cash and cash equivalents, end of year	<u><u>\$ 2,167,324</u></u>

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

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2018

1. NATURE OF OPERATIONS

Children's Discovery Museum of San Jose ("the Museum" or "CDM") is a California nonprofit public benefit corporation organized in 1982 and incorporated in 1983. The Museum operates a children's museum which addresses the educational needs of children, youth, and their families in Santa Clara County through participatory exhibits and programs that engage the senses and challenge the mind.

Exhibits

Children's Discovery Museum of San Jose has served over 9 million adults and children since opening its doors in the spring of 1990. In the 2017-2018 fiscal year, the Museum provided engaging learning opportunities to over 333,900 families and 32,930 group visitors.

The Museum exhibits encourage touching, exploring, manipulating and experimenting, and cut across the disciplines of art, science and the humanities. The Museum's theme is connections; the context is community - the myriad relationships within and between the man-made and natural worlds and the way those relationships are expressed here in our own backyard. While the majority of exhibits focus on children to age 10 and their parents and caregivers, The Wonder Cabinet serves the needs of the Museum's youngest visitors as an early learning environment with exhibits designed to support the cognitive, emotional and social development of infants, toddlers and preschoolers. Whether children are role-playing a firefighter on the authentic fire engine in the Streets of San Jose exhibit, using colorful plastic balls to study how water rushes and flows in WaterWays, or experimenting with surface tension by playing with bubbles, they are actively engaged in learning, inspired by their own curiosity to investigate how things work and to understand more about the world in which we live.

The Museum offers 28,000 square feet of exhibition space in 13 dedicated galleries, each housing 8-10 interactive exhibits which respond to the distinctive need for children to learn through concrete interactions. In operation for over 25 years, the Museum and its staff strive to enhance the visitor experience and, in October, 2017, the Museum essentially doubled its exhibit space when Bill's Backyard: Bridge to Nature opened. Contributions to this 27,500 square foot outdoor learning center included the City of San Jose, the County of Santa Clara, the California State Coastal Conservancy, the Santa Clara Valley Open Space Authority, FIRST 5 Santa Clara County, the Santa Clara Valley Water District, Agilent Technologies Foundation, the Super Bowl 50 Fund, the Sharks Foundation and Sunlight Giving.

Bill's Backyard provides opportunities for unstructured play as well as a large outdoor classroom for facilitated activities and nature investigations. Signage in English, Spanish and Vietnamese focuses visitor interactions on the uniqueness of outdoor play, such as build, roll, climb, plant, and observe, to name a few. Ten different species of animals and bugs were cast in bronze and placed appropriately throughout the area to allow children to discover them in their natural habitat. A 7,200 gallon rain-harvest system is used to irrigate the native landscape and to teach visitors about water conservation at the same time. By bringing nature to children, CDM hopes to create a spark so that children will then seek out other outdoor opportunities close to their home, and become environmental stewards as they grow up.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2018

1. NATURE OF OPERATIONS (continued)

Exhibits (continued)

In addition, the Museum replicated some of the outdoor activities in Bill's Backyard at the Educare California at Silicon Valley site, further complementing the activity area developed by the Museum when the school opened in 2016.

Among the Museum's new projects to be completed in the next 2-3 years is the creation of a Potter the Otter traveling exhibit, with funding from FIRST 5, in 2 versions to meet the interest expressed by large and small institutions, such as museums and libraries. The undeveloped 4,000 square foot of land adjoining Bill's Backyard is currently being designed and will offer a gathering and presentation space for school groups. Initial funding for this area has been secured from the Xu Family Charitable Foundation.

Educational Programs

The Museum provides on-site programs which complement its exhibits and support visitor interactions and learning opportunities. In 2017-2018, the Museum provided programs for over 50,000 participants. The on-site Art Studio in The Wonder Cabinet and Art Loft are examples of the Museum's commitment to visual arts education experiences, while the Lee and Diane Brandenburg Theatre and Cadence Amphitheatre offer performing experiences. The Museum employs a three-pronged approach to the arts: engagement with and viewing the work of professional artists; exploring the other children's art; and individually creating their own works of art in various formats. Throughout the year, the Museum invites the community to participate in various cultural festivals, which represent the region's ethnic composition. These events include weekend events, such as Diwali, Dia de los Tres Reyes Magos, Lunar New Year, Children of the Dragon, and single day or evening events, such as Dia de los Muertos, the Lantern Festival, Lunadas Familiares and Menorahs and Miracles: A Hanukkah Celebration.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2018

1. NATURE OF OPERATIONS (continued)

Educational Programs (continued)

Beyond Children's Discovery Museum of San Jose's exhibit galleries, the educational programs bring resources and innovative learning techniques to schools, libraries and community centers; encourage young adults to become active citizens by impacting their environment and serving their community; stimulate curiosity and promote an inquiry-based learning; and reach the children and youth in our community most in need of extra support, with experiences designed to ensure that children know their own worth, respect their own knowledge, and achieve their greatest potential. Highly successful programs, such as BioSITE (Students Investigating Their Environment), engage high school students in mentoring elementary school students to value their local river by gathering important water quality information and sharing the information with the scientific research community; Summer of Service provides middle school youth volunteer opportunities at local food banks and shelters, senior centers, parks and preschools. Throughout the year, the Museum opens during evening hours for Play Your Way events, which welcome families with children on the autism spectrum the opportunity to explore and engage with the exhibits in a quieter period, as well as showcasing area resources for these families. In 2017, the Museum joined the Museums for All initiative, sponsored by the Association of Children's Museums and the Institute of Museum and Library Services, which encourages families to visit museums regularly through reduced admission. During the first year, CDM welcomed over 5,800 visitors through this program.

National Leadership Grant funding from the Institute of Museum and Library Services, in September, 2017, funded CDM's expansion of its Cultural Competence Learning Institute (CCLI) in collaboration with the Association of Children's Museums and the Association of Science-Technology Centers to work with 15-18 museums from across museum sectors. The ultimate goal of CCLI is to develop, track, promote and sustain organizational change within individual institutions and field-wide in order to build museums' capacity to engage with issues of inclusion and cultural competence. CDM and its partners believe that CCLI's peer-driven approach to diversity and inclusion responds to the need voiced by the broader museum field and can help to shift 25 years of conversation about diversity to tangible actions that will empower museums to provide high quality, inclusive experiences that reflect and respond to the needs of their entire community.

Based on the success of one of the Museum's signature programs, BioSITE, which has been promoting environmental education for 25 years in schools, the Museum has begun offering companion programs for museum visitors and area families. The classroom area in Bill's Backyard is an ideal location for small groups, and the development of the adjacent area discussed above will welcome larger groups when completed in the next few years.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2018

1. NATURE OF OPERATIONS (continued)

Retail Services

Located at the entrance to the Museum, the retail store has offered educationally-based products for sale which expanded on concepts encountered through interaction with Museum exhibits and programs, since the Museum's inception. However, given the rise of major online retailers, such as Amazon, the financial success of many small retail establishments is not possible. After considerable review, the Museum has decided to close the current retail space and transfer its use to income-producing programs, such as birthday parties and fee-based programs. A kiosk with a small number of items for purchase will be developed in the future.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation and financial statement presentation

The financial statements of Children's Discovery Museum of San Jose have been prepared on the accrual basis of accounting.

The Museum reports information regarding its 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* - include those assets over which the Board of Directors has discretionary control in carrying out the operations of the Museum. Under this category, the Museum maintains an operating fund, any net assets designated by the Board for specific purposes and the unrestricted property and equipment fund. The Board has established a goal to include a full six months of the coming year's estimated expense in Operating Reserve. Board designations are not donor-imposed restrictions and are subject to change at the Board's discretion.
- *Temporarily restricted net assets* - include those assets which are subject to donor restriction and for which the applicable restriction was not met as of the year end of the current reporting period.
- *Permanently restricted net assets* - include those assets which are subject to a non-expiring donor restriction, such as endowments.

Cash and cash equivalents

Cash and cash equivalents include highly liquid investments and investments with a maturity of three months or less, and exclude donor restricted receipts and amounts designated for long-term purposes. The Museum maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The Museum has not experienced any losses in such accounts. Management believes it is not exposed to any significant risk on cash accounts.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventory

Inventory consists of gift shop merchandise. The merchandise is stated at the lower of cost or market on a first-in/first-out basis. The reported inventory cost as of August 31, 2018, was \$45,109.

Investments

Investments in marketable securities with readily determinable fair values and all investments in mutual funds and other securities are reported at their fair values on the statement of financial position. Unrealized gains and losses are included in the change in net assets.

Fair value is defined as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."

A hierarchy has been established to prioritize the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest ranking to fair values determined using unadjusted quoted prices in active markets for identical assets (Level 1) and the lowest ranking to fair values determined using methodologies and models with unobservable inputs (Level 3). Observable inputs are those that market participants would use in pricing the asset based on market data obtained from sources independent of the Museum. Unobservable inputs reflect the Museum's assumption about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The fair value hierarchy is categorized into three levels based on the inputs as follows:

- *Level 1* - Values are unadjusted quoted prices for identical assets and liabilities in active markets accessible at the measurement date.
- *Level 2* - Inputs include quoted prices for similar assets or liabilities in active markets, quoted prices from those willing to trade in markets that are not active, or other inputs that are observable or can be corroborated by market data for the term of the instrument. Such inputs include market interest rates and volatilities, spreads and yield curves.
- *Level 3* - Certain inputs are unobservable (supported by little or no market activity) and significant to the fair value measurement. Unobservable inputs reflect the Museum's best estimate of what hypothetical market participants would use to determine a transaction price for the asset or liability at the reporting date.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property and equipment

Property and equipment are recorded at cost or estimated fair value for donated items. Equipment purchases over \$1,000 are capitalized. Costs related to the development and construction of exhibits are capitalized. The Museum does not recognize depreciation on capitalized individual works of art (included as part of exhibits) whose economic benefit or service potential is used up so slowly that the estimated useful life of the assets is extraordinarily long. The cost of repairs and maintenance which do not improve or extend the lives of the respective assets are expensed currently. Depreciation is computed on the straight-line method based on the estimated useful lives of the assets, which range from 3 to 40 years. Depreciation is charged to the activity benefiting from the use of the property or equipment.

Accrued vacation

Accrued vacation represents vacation earned, but not taken as of August 31, 2018, and is included in "accrued payroll and related benefits" on the statement of financial position. The accrued vacation balance as of August 31, 2018 was \$293,443.

Deferred revenue

As of August 31, 2018, the Museum had deferred revenue of \$75,815 from advance admissions and the sale of gift cards.

Customer deposits

As of August 31, 2018, the Museum has received deposits of \$17,738 for future pinscreen sales and birthday party and facility rentals.

Revenue recognition

The Museum recognizes support and revenue on the accrual basis of accounting. Revenue from grants which have been classified as "exchange transactions" and program fees are recognized as revenue in the period in which the service is provided.

Contributions

Contributions are recognized when the donor makes a pledge to give that is, in substance, an unconditional promise. Contributions are recorded as unrestricted, temporarily restricted, or permanently restricted depending on the nature of donor restrictions. Restricted contributions are reported as increases in restricted net assets. When the restriction is met the amount is shown as a reclassification of restricted net assets to unrestricted net assets.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Donations in-kind

Donated equipment and other donated goods are recorded at their estimated fair value as of the date of the donation. Donated rent is recorded at its estimated fair value based on prevailing rent rates when lease agreements are entered into and/or amended. Contributed services, which enhance nonfinancial assets or require a specialized skill and which the Museum would have paid for if not donated, are recorded at the estimated fair value at the time the services are rendered.

Allocation of functional expenses

Directly identifiable expenses are charged to program and supporting services. Expenses related to more than one function are charged to program and supporting services on the basis of square footage of occupied space or number of employees per department.

Advertising

The Museum's policy is to expense advertising costs as the costs are incurred. Advertising expenses for the year ended August 31, 2018 was \$184,411.

Income taxes

Children's Discovery Museum of San Jose is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code and state income taxes under Section 23701(d) of the California Revenue Taxation Code. However, income from certain activities not directly related to the Museum's tax-exempt purpose is subject to taxation as unrelated business income. In addition, the Museum qualifies for the charitable contribution deduction under Section 170(b)(1)(A) of the Internal Revenue Code and has been classified as an organization that is not a private foundation under Section 509(a)(1) of the Internal Revenue Code.

Uncertainty in income taxes

Generally accepted accounting principles provide accounting and disclosure guidance about positions taken by an organization in its tax returns that might be uncertain. Management has considered its tax positions and believes that all of the positions taken by the Museum in its federal and state exempt organization tax returns are more likely than not to be sustained upon examination.

The Museum's federal returns for the years ended August 31, 2017, 2016, and 2015 could be subject to examination by federal taxing authorities, generally for three years after they are filed. The Museum's state returns for the years ended August 31, 2017, 2016, 2015, and 2014 could be subject to examination by state taxing authorities, generally for four years after they are filed.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2018

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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 at the date of the financial statements and the reported amounts of support, revenue and expenses during the period. Accordingly, actual results could differ from those estimates.

Subsequent events

Management of the Museum has evaluated events and transactions subsequent to August 31, 2018 for potential recognition or disclosure in the financial statements. The Museum did not have subsequent events that required recognition or disclosure in the financial statements for the fiscal year ended August 31, 2018. Subsequent events have been evaluated through the date the financial statements became available to be issued, January 17, 2019.

3. INVESTMENTS

The following table sets forth by level, within the fair value hierarchy, the Museum's assets at fair value as of August 31, 2018:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Stocks and mutual funds	\$ 4,700,270	\$ -	\$ -	\$ 4,700,270
Cash and cash equivalents	1,177,313	-	-	1,177,313
Venture capital funds	-	-	102,327	102,327
Interest receivable	<u>2,415</u>	<u>-</u>	<u>-</u>	<u>2,415</u>
	<u>\$ 5,879,998</u>	<u>\$ -</u>	<u>\$ 102,327</u>	<u>\$ 5,982,325</u>

Fair values for investments, except venture capital funds, are determined by reference to quoted market prices and other relevant information generated by market transactions. Fair values for investments in venture capital funds are determined by the fund managers based on the estimated values of underlying investment holdings.

Children's Discovery Museum of San Jose
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3. INVESTMENTS (continued)

The following table sets forth a summary of changes in the fair value of Level 3 investments for the year ended August 31, 2018:

	ENF III Fund	ENF VII Fund	Total
Balance, beginning of year	\$ 6,553	\$ 77,669	\$ 84,222
Net gain (loss)	20,317	(2,212)	18,105
Balance, end of year	\$ 26,870	\$ 75,457	\$ 102,327

The net loss in venture capital funds investments included in the change in unrestricted net assets is composed of \$18,105 in a net unrealized gain.

Investment earnings during the year consist of the following:

Interest and dividends	\$ 149,400
Net realized and unrealized gain on investments	500,126
	\$ 649,526

4. CONTRIBUTIONS RECEIVABLE

Contributions receivable represent unconditional promises given by donors and are recorded at net realizable value.

Contributions receivable consist of the following:

Receivable in less than one year	\$ 937,319
Receivable in one to five years	287,604
	\$ 1,224,923

Of the contributions receivable at August 31, 2018, 35% and 20% are due from two donors.

5. DONATED RENT RECEIVABLE

The Museum entered into a non-cancelable lease with the Redevelopment Agency of the City of San Jose in June 1987 and amended the lease in February 1990. Under this agreement for no rental payments, the Museum operates, maintains and manages the Museum facility and site with the exception of structural components, which are maintained by the City of San Jose. The initial term of the lease is 55 years with four renewal options of 11 years each.

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5. DONATED RENT RECEIVABLE (continued)

As the lease is non-cancelable, the Museum recognized the benefit of this lease agreement as donated rent receivable and temporarily restricted support. The Museum has established the fair market value of the rent under the agreement at \$720,000 per year. The annual rent expense is included in the statement of activities and statement of functional expenses. The net present value of the future contribution benefit has been computed at a discount rate of 6.68% based upon prevailing rates when the lease agreement was entered into and is recorded as donated rent receivable on the statement of financial position.

Donated rent receivable consisted of the following:

<u>Year ending August 31,</u>	
2019	\$ 153,722
2020	163,992
2021	174,947
2022	186,633
2023	199,100
Thereafter	<u>7,598,803</u>
	8,477,197
Current portion	<u>(153,722)</u>
	<u><u>\$ 8,323,475</u></u>

6. PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

Exhibits	\$ 10,159,483
Leasehold improvements	4,112,858
Equipment	2,548,656
Furniture and fixtures	123,364
Vehicles	37,494
Construction in progress	<u>50,385</u>
	17,032,240
Accumulated depreciation	<u>(8,827,553)</u>
	<u><u>\$ 8,204,687</u></u>

Depreciation expense for the year ended August 31, 2018 was \$1,449,164.

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7. RETIREMENT PLAN

The Museum maintains a tax deferred 403(b) retirement plan to provide retirement benefits for all eligible employees. The Plan provides for Museum employees to contribute an amount from their compensation, subject to limitations set by the Internal Revenue Code. The Museum has a separate defined contribution retirement plan, which allows the Museum to make an employer contribution up to a maximum of 5% of all eligible employee compensation. Participants are immediately vested in their salary deferral and employer contributions. There were no employer contributions made during the year ended August 31, 2018.

8. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following:

Donated rent receivable	\$ 8,477,197
Programs and exhibits	1,242,967
Endowment accumulated earnings - unappropriated	<u>378,614</u>
	<u><u>\$ 10,098,778</u></u>

Temporarily restricted net assets released from restriction during the year were as follows:

Donated rent receivable	\$ 144,098
Programs and exhibits	1,504,918
Endowment accumulated earnings - appropriated	<u>83,461</u>
	<u><u>\$ 1,732,477</u></u>

9. PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets consist of endowment fund investments which represent the principal amount of gifts and bequests accepted with the donor stipulation that the principal be maintained intact in perpetuity or for a specified period, with only the income to be utilized for operations (see Note 13).

10. DONATIONS IN-KIND

The estimated fair value of rent, fixtures and furnishings, computer software and hardware, professional services, and supplies received are recorded as donations.

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10. DONATIONS IN-KIND (continued)

Donations in-kind were received by the Museum as follows:

Rent	\$ 575,902
Supplies	4,375
Services	<u>24,464</u>
	<u>\$ 604,741</u>

11. CONTINGENCIES

Grants and contracts awarded to Children's Discovery Museum of San Jose are subject to the funding agencies' criteria, contract terms and regulations under which expenditures may be charged and are subject to audit under such terms, regulations, and criteria. Occasionally, such audits may determine that certain costs incurred against the grants do not comply with the established criteria that govern them. In such cases, the Museum could be held responsible for repayments to the funding agency for the costs or be subject to the reductions of future funding in the amount of the costs. Management does not anticipate any material questioned costs for the contracts and grants administered during the period.

12. RELATED PARTY TRANSACTIONS

The Museum's volunteer executive board members are active in both oversight of the fundraising events activities and in making private contributions. During the year ended August 31, 2018, in-kind donations received from the board members totaled \$3,343. During the year ended August 31, 2018, contributions received from board members totaled \$523,242 and contributions from their employers or affiliation totaled \$687,578.

13. ENDOWMENT

The Museum's endowment consists of two individual funds. Its endowment includes donor-restricted and board-designated endowment funds. As required by Generally Accepted Accounting Principles (GAAP), net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

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13. ENDOWMENT (continued)

Interpretation of relevant law

The Board of Directors of the Museum has interpreted the California version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Museum classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Museum in a manner consistent with the standard of prudence prescribed by the California version of UPMIFA.

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

- (1) The duration and preservation of the fund
- (2) The purposes of the Museum and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The expected total return from income and the appreciation of investments
- (6) Other resources of the Museum
- (7) The investment policies of the Museum

Investment return objectives, risk parameters and strategies - goals and performance measurement

- Based on a Total Return Investment Objective, the primary goal for the Portfolio is to exceed the inflation rate as measured by the Consumer Price Index (CPI) by not less than four (4) percentage points on an annual (calendar) basis, net of investment management fees. A secondary goal is to exceed by not less than one (1) percentage point the return of the appropriate benchmark indices over a three (3) to five (5) year period, net of investment management fees. (70% Standard & Poor's Equity Index, and 30% Barclay's Intermediate Government/ Corporate Bond Index.)
- The performance results will be calculated in conformance with the Association for Investment Management and Research (AIMR) Performance Presentation Standards.
 1. Total returns, including realized and unrealized gains and losses plus income.
 2. Accrual accounting for fixed income securities.

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13. ENDOWMENT (continued)

Investment return objectives, risk parameters and strategies - goals and performance measurement (continued)

3. Time-weighted rate of return using monthly valuation and geometric linking.
4. The pricing of all assets must be based on a reasonable estimate of current value. Standardized pricing quotations must be used when available.

Spending policy

Unless otherwise specified in a governing gift agreement, the payout policy for an endowed fund may be up to 5% of the fund's value, based on a 12 quarter rolling average calculated as of August 31, 2018. Where the fund has not been in existence for 12 quarters, the actual number of quarters that the fund has been in existence will be used. The intent of the policy is to set a maximum amount for spending, but not to mandate that such an amount be spent. Disbursements will be made in two installments, half at the end of December and half at the end of June.

The Board will review the spending policy annually, and update, if necessary.

Endowment composition

Endowment net asset composition by type is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ -	\$ 378,614	\$ 1,161,095	\$ 1,539,709
Board-designated endowment funds	<u>3,073,933</u>	<u>-</u>	<u>-</u>	<u>3,073,933</u>
	<u>\$ 3,073,933</u>	<u>\$ 378,614</u>	<u>\$ 1,161,095</u>	<u>\$ 4,613,642</u>

Changes in donor-restricted endowment net assets for the year are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance, beginning of year	<u>\$ -</u>	<u>\$ 440,988</u>	<u>\$ 1,161,095</u>	<u>\$ 1,602,083</u>
Interest and dividends	-	17,062	-	17,062
Net unrealized gain on investments	-	4,025	-	4,025
Appropriations	<u>-</u>	<u>(83,461)</u>	<u>-</u>	<u>(83,461)</u>
	<u>-</u>	<u>(62,374)</u>	<u>-</u>	<u>(62,374)</u>
Balance, end of year	<u>\$ -</u>	<u>\$ 378,614</u>	<u>\$ 1,161,095</u>	<u>\$ 1,539,709</u>

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13. ENDOWMENT (continued)

Endowment composition (continued)

Changes in board-designated endowment net assets for the fiscal year ended August 31, 2018 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance, beginning of year	\$ 2,711,314	\$ -	\$ -	\$ 2,711,314
Interest and dividends	132,338	-	-	132,338
Net unrealized gain on investments	496,101	-	-	496,101
Appropriations	<u>(265,820)</u>	<u>-</u>	<u>-</u>	<u>(265,820)</u>
	<u>362,619</u>	<u>-</u>	<u>-</u>	<u>362,619</u>
Balance, end of year	<u>\$ 3,073,933</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,073,933</u>