

Children's Discovery Museum of San Jose

Financial Statements

August 31, 2019



TABLE OF CONTENTS

	<u>Page No.</u>
Independent Auditor's Report	1 - 2
Statement of Financial Position	3
Statement of Activities	4
Statement of Functional Expenses	5
Statement of Cash Flows	6
Notes to Financial Statements	7 - 24

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, 2019, 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, 2019, 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.

Change in Accounting Principle

As described in Note 4 to the financial statements, the Museum has adopted ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities* and ASU 2018-08, *Not-For-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. Our opinion is not modified with respect to that matter.

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 16, 2020

Children's Discovery Museum of San Jose
Statement of Financial Position
August 31, 2019

	Without Donor Restrictions	With Donor Restrictions	Total
ASSETS			
Current assets			
Cash and cash equivalents	\$ 861,724	\$ 1,007,384	\$ 1,869,108
Contributions receivable, current portion	180,333	650,175	830,508
Donated rent receivable, current portion	-	163,991	163,991
Inventory	14,275	-	14,275
Prepaid expenses	323,654	-	323,654
Other current assets	3,870	-	3,870
Total current assets	<u>1,383,856</u>	<u>1,821,550</u>	<u>3,205,406</u>
Property and equipment, net	<u>7,544,134</u>	<u>-</u>	<u>7,544,134</u>
Other assets			
Investments	4,631,933	1,436,291	6,068,224
Contributions receivable, net of current portion	-	250,000	250,000
Donated rent receivable, net of current portion	-	8,159,483	8,159,483
Total other assets	<u>4,631,933</u>	<u>9,845,774</u>	<u>14,477,707</u>
Total assets	<u>\$ 13,559,923</u>	<u>\$ 11,667,324</u>	<u>\$ 25,227,247</u>
LIABILITIES AND NET ASSETS			
Current liabilities			
Accounts payable and accrued liabilities	\$ 122,397	\$ -	\$ 122,397
Accrued payroll and related benefits	546,594	-	546,594
Deferred revenue	95,255	-	95,255
Customer deposits	3,000	-	3,000
Total current liabilities	<u>767,246</u>	<u>-</u>	<u>767,246</u>
Net assets			
Without donor restrictions			
Board-designated			
Endowment	2,248,543	-	2,248,543
Operating reserve	2,000,000	-	2,000,000
Fixed asset reserve	1,000,000	-	1,000,000
Total board-designated	5,248,543	-	5,248,543
Property and equipment	7,544,134	-	7,544,134
Total without donor restrictions	<u>12,792,677</u>	<u>-</u>	<u>12,792,677</u>
With donor restrictions			
Restricted for a specified purpose	-	1,849,597	1,849,597
Donated rent receivable	-	8,323,474	8,323,474
Unappropriated earnings on perpetual endowment	-	333,158	333,158
Perpetual endowment	-	1,161,095	1,161,095
Total with donor restrictions	<u>-</u>	<u>11,667,324</u>	<u>11,667,324</u>
Total net assets	<u>12,792,677</u>	<u>11,667,324</u>	<u>24,460,001</u>
Total liabilities and net assets	<u>\$ 13,559,923</u>	<u>\$ 11,667,324</u>	<u>\$ 25,227,247</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, 2019

	Without Donor Restrictions	With Donor Restrictions	Total
Support and revenue			
Support			
Grants and contributions	\$ 831,914	\$ 1,627,660	\$ 2,459,574
Special events, net of \$138,482	1,171,244	-	1,171,244
Donations in-kind	1,071,975	-	1,071,975
Total support	<u>3,075,133</u>	<u>1,627,660</u>	<u>4,702,793</u>
Revenue			
Admissions	2,103,786	-	2,103,786
Membership	1,003,988	-	1,003,988
Other income	464,910	-	464,910
Program fees	161,789	-	161,789
Retail services	136,059	-	136,059
Investment income, net	70,837	33,434	104,271
Exhibit rental	3,872	-	3,872
Loss on disposition of property and equipment	(6,545)	-	(6,545)
Total revenue	<u>3,938,696</u>	<u>33,434</u>	<u>3,972,130</u>
Total support and revenue	7,013,829	1,661,094	8,674,923
Net assets released from restriction	<u>1,253,643</u>	<u>(1,253,643)</u>	<u>-</u>
Total support, revenue, and net assets released from restriction	<u>8,267,472</u>	<u>407,451</u>	<u>8,674,923</u>
Functional expenses			
Program services			
Exhibits	2,972,452	-	2,972,452
Educational programs	4,809,156	-	4,809,156
Retail services	230,705	-	230,705
Total program services	<u>8,012,313</u>	<u>-</u>	<u>8,012,313</u>
Support services			
Management and general	1,253,157	-	1,253,157
Development and fundraising	487,945	-	487,945
Total support services	<u>1,741,102</u>	<u>-</u>	<u>1,741,102</u>
Total functional expenses	<u>9,753,415</u>	<u>-</u>	<u>9,753,415</u>
Change in net assets (see Notes 2 and 3)	(1,485,943)	407,451	(1,078,492)
Net assets, beginning of year	<u>14,278,620</u>	<u>11,259,873</u>	<u>25,538,493</u>
Net assets, end of year	<u>\$ 12,792,677</u>	<u>\$ 11,667,324</u>	<u>\$ 24,460,001</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, 2019

	Program Services				Support Services			
	Exhibits	Educational Programs	Retail Services	Total Program Services	Management and General	Development and Fundraising	Total Support Services	Total
Expenses								
Salaries and benefits								
Salaries	\$ 411,790	\$ 2,806,185	\$ 49,287	\$ 3,267,262	\$ 558,232	\$ 235,668	\$ 793,900	\$ 4,061,162
Employee benefits	66,152	147,369	10,987	224,508	72,249	45,150	117,399	341,907
Payroll taxes	<u>29,472</u>	<u>214,548</u>	<u>4,273</u>	<u>248,293</u>	<u>39,718</u>	<u>16,677</u>	<u>56,395</u>	<u>304,688</u>
Total salaries and benefits	507,414	3,168,102	64,547	3,740,063	670,199	297,495	967,694	4,707,757
Outside services	44,426	392,634	8,537	445,597	286,132	58,421	344,553	790,150
Repairs and maintenance	399,815	274,160	19,478	693,453	30,842	19,633	50,475	743,928
Occupancy	324,000	288,000	14,400	626,400	72,000	21,600	93,600	720,000
Small equipment	206,517	196,504	225	403,246	30,167	2,720	32,887	436,133
Utilities	133,510	78,265	6,906	218,681	6,906	4,604	11,510	230,191
Printing	2,463	170,368	437	173,268	611	5,084	5,695	178,963
Cost of goods sold	-	-	84,294	84,294	-	-	-	84,294
Insurance	41,297	24,243	2,374	67,914	1,863	1,424	3,287	71,201
Conferences and meetings	839	39,630	1,844	42,313	12,004	10,556	22,560	64,873
Telephone	6,838	17,315	3,223	27,376	8,942	7,656	16,598	43,974
Travel	48	31,126	-	31,174	815	-	815	31,989
Office supplies	2,279	9,482	1,125	12,886	8,350	6,992	15,342	28,228
Dues and subscriptions	4,043	12,553	770	17,366	3,305	1,268	4,573	21,939
Training	-	-	-	-	7,771	-	7,771	7,771
Postage and shipping	484	1,128	2,283	3,895	1,174	1,944	3,118	7,013
Automobile	<u>1,674</u>	<u>663</u>	<u>-</u>	<u>2,337</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,337</u>
Total expenses before depreciation	1,675,647	4,704,173	210,443	6,590,263	1,141,081	439,397	1,580,478	8,170,741
Depreciation	<u>1,296,805</u>	<u>104,983</u>	<u>20,262</u>	<u>1,422,050</u>	<u>112,076</u>	<u>48,548</u>	<u>160,624</u>	<u>1,582,674</u>
	<u>\$ 2,972,452</u>	<u>\$ 4,809,156</u>	<u>\$ 230,705</u>	<u>\$ 8,012,313</u>	<u>\$ 1,253,157</u>	<u>\$ 487,945</u>	<u>\$ 1,741,102</u>	<u>\$ 9,753,415</u>
Percentage of total	<u>31 %</u>	<u>49 %</u>	<u>2 %</u>	<u>82 %</u>	<u>13 %</u>	<u>5 %</u>	<u>18 %</u>	<u>100 %</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, 2019

Cash flows from operating activities	
Change in net assets	\$ (1,078,492)
Adjustments to reconcile change in net assets to net cash used in operating activities	
Net realized and unrealized loss on investments	58,174
Proceeds from contributions restricted for purchase of property and equipment	(743,248)
Donated capitalized art studio costs and computer equipment	(320,985)
Depreciation	1,582,674
Donated rent receivable amortization	153,723
Loss on disposal of property and equipment	6,545
Changes in operating assets and liabilities	
Contributions receivable	144,415
Inventory	30,834
Prepaid expenses	(146,064)
Accounts payable and accrued liabilities	23,759
Accrued payroll and related benefits	(5,747)
Deferred revenue	19,440
Customer deposits	(14,738)
Net cash used in operating activities	<u>(289,710)</u>
Cash flows from investing activities	
Purchase of investments	(519,929)
Proceeds from sale of investments	375,856
Purchase of property and equipment	<u>(607,681)</u>
Net cash used in investing activities	<u>(751,754)</u>
Cash flows from financing activities	
Proceeds from contributions restricted for purchase of property and equipment	<u>743,248</u>
Net cash provided by financing activities	<u>743,248</u>
Net decrease in cash and cash equivalents	(298,216)
Cash and cash equivalents, beginning of year	<u>2,167,324</u>
Cash and cash equivalents, end of year	<u><u>\$ 1,869,108</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, 2019

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 9.4 million adults and children since opening its doors in the spring of 1990. In the 2018-2019 fiscal year, the Museum provided engaging learning opportunities to over 291,380 family and 30,400 group visitors.

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.

Approaching 30 years of operation, the Museum and its staff strive to enhance the visitor experience in its 28,000 square feet of indoor 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. As the first museum to receive major renovation support from The Good Tidings Foundation and the LeRoy Neiman Foundation, along with a 5-year program support commitment, CDM was honored to rebrand the visual arts exploration area as the LeRoy Neiman Art Studio.

The Museum essentially doubled its exhibit space when Bill's Backyard: Bridge to Nature opened in 2017. Located in a half-acre adjacent to the building, 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 local species of animals and insects 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. Additionally, the Museum has increased its programming presence at the Educare California at Silicon Valley site by replicating some of its Bill's Backyard activities in an outdoor play area.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

1. NATURE OF OPERATIONS (continued)

Exhibits (continued)

After securing a \$1 million donation from the Xu Family Charitable Foundation, CDM retained Brad Cox Architects for conceptual design to achieve the goals of the 4,000 parcel adjacent to Bill's Backyard: 1) a workspace for school groups and families to engage in interactive STEM programs pre- and post-Museum visits; 2) a standalone landscape and natural experiences that reinforce math in nature, such as the Fibonacci sequence and spirals; and 3) a secondary Museum entrance with admissions features that can be operated when needed. Preliminary cost estimates are underway, which will be followed by construction planning and permitting through the City's Public Works Department, and a formal fundraising campaign, with the space targeted for opening to the public in 2021-2022.

Traveling exhibit projects undertaken by the Museum in 2018-2019 include the creation of a Potter the Otter exhibit, with funding from FIRST 5 Santa Clara County, and the refurbishment of Hello from Japan!, an exhibit created by the Children's Museum of Manhattan and originally traveled by the Association of Children's Museums. Hello from Japan! will be installed at CDM through January 2020, and illustrates a society where the past, present and future aesthetics and customs harmoniously coexist. Following this installation, Hello from Japan! will begin a 2-3-year tour concurrent with CDM's successful Voyage to Vietnam; both exhibits were originally created as part of the Freeman Asian Cultural Exhibit Series.

Exhibit projects on the horizon include the installation of A Seat at the Table, an Institute of Museum and Library Services-funded initiative (IMLS) which seeks to highlight the commonalities of cultures using culinary tools, handwritten notes from adults attending cultural festivals throughout San Jose, and a community poem simply written by selecting phrases and sentiments left behind by festival participants. Recent support from IMLS will support a planning grant to determine the feasibility of designing a traveling exhibit about the Persian Nowruz Festival with MIIM Design Group. Continuing its outreach to the community, CDM has received funding support from ZOOM to develop a 600 square foot children's play area in Terminal B at the San Jose airport. Further, Hensel Phelps has agreed to serve as general contractor for the project on a pro bono basis. Opening date of the play area is targeted for late-2020.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

1. NATURE OF OPERATIONS (continued)

Educational Programs

The Museum provides on-site and outreach programs which complement its exhibits and support visitor interactions and learning opportunities. In 2018-2019, the Museum provided targeted programs for over 51,000 participants. The on-site Art Studio in The Wonder Cabinet and recently renovated LeRoy Neiman Art Studio are examples of the Museum's commitment to visual arts education experiences, while the Lee and Diane Brandenburg Theatre and Cadence Amphitheatre offer performing arts experiences. The Museum employs a three-pronged approach to the arts: engagement with and viewing the work of professional artists; exploring other children's art; and creating individual 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.

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, providing 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 two years, CDM has welcomed 16,974 visitors through this program. Looking to increase its support of families with special needs, Afternoons for All Abilities was developed to offer a quieter Museum environment and specially-crafted activities on the second Tuesday of each month.

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. Building on Richard Louv's call-to-action, a pilot program, Happy Trails, was created to invite low income families with very young children to learn about nature exploration through facilitated workshops and culminating with a half-day field trip to a local open space preserve.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

1. NATURE OF OPERATIONS (continued)

Educational Programs (continued)

National Leadership Grant funding from the IMLS 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. Building on the CCLI initiative, CDM partnered with the Exploratorium to offer Cambio, a professional development institute combining CCLI and the Exploratorium's GENIAL to support informal science practitioners working with Latinx audiences, and received a 5-year funding commitment from the National Science Foundation.

CDM continuously strives to understand and to improve its service to its visitors. This year, CDM became the 27th museum cohort in the Collaboration for Ongoing Visitor Engagement Surveys (COVES) led by the Museum of Science, Boston. Participation in this collaborative will enable CDM systematically to survey its visitors about their museum experience. The Museum was also accepted as a cohort to the American Alliance of Museums' Facing Change Initiative, a national year-long Board diversity program.

Retail Services

Located at the entrance to the Museum, the retail store had offered educationally-based products for sale which expanded on concepts encountered through interaction with Museum exhibits and programs. However, given the rise of major online retailers, such as Amazon, the financial success of many small retail establishments was not possible. After considerable review, the Museum closed the retail space in December 2018, and transitioned its use to the Teal Party Room, an income-producing program. The increased number and size of party bookings were favorably received by the Museum audience.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

2. CHANGE IN NET ASSETS

During the year ended August 31, 2019, the Museum experienced a decrease in net assets of \$1,078,492 as reported in the statement of activities. A significant amount of the decrease can be attributed to depreciation expense and donated rent receivable amortization.

The following schedule reflects an intermediate measure of the change in net assets excluding depreciation expense and donated rent receivable amortization:

	Without Donor Restrictions	With Donor Restrictions	Total
Change in net assets	\$ (1,485,943)	\$ 407,451	\$ (1,078,492)
Add back:			
Depreciation expense	1,582,674	-	1,582,674
Donated rent receivable amortization	<u>-</u>	<u>153,723</u>	<u>153,723</u>
Change in net assets excluding depreciation and donated rent receivable amortization	<u>\$ 96,731</u>	<u>\$ 561,174</u>	<u>\$ 657,905</u>

3. CONDITIONAL PROMISES TO GIVE

Conditional promises to give are recognized when the Museum meets the terms of the conditions.

Conditional promises to give as of August 31, 2019 consisted of the following:

Recognizable in one year or less	
Cambio project - reimbursement based	\$ 171,419
Potter the Otter Traveling exhibit - achieve deliverable requirements	<u>130,177</u>
	<u>301,596</u>
Recognizable in more than one year	
Cambio project - reimbursement based	319,987
Cambio project - reimbursement based and contingent on the availability of funds and the scientific progress of the project	<u>695,121</u>
	<u>1,015,108</u>
	<u>\$ 1,316,704</u>

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting 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 two classes of net assets: without donor restrictions and with donor restrictions.

- *Net assets without donor restrictions* - 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. Board designations are not donor-imposed restrictions and are subject to change at the Board's discretion.
- *Net assets with donor restrictions* - 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 and also include those assets which are subject to a non-expiring donor restriction, such as endowments.

Change in accounting principle

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. ASU 2016-14 makes certain improvements to current reporting requirements, including:

1. Reducing the classes of net assets from three (unrestricted, temporarily restricted, and permanently restricted) to two (without donor restrictions and with donor restrictions).
2. Enhancing disclosures about:
 - a. Amounts and purposes of governing board designations, appropriations, and similar actions that result in self-imposed limits on the use of resources without donor-imposed restrictions.
 - b. Composition of net assets with donor restrictions and how the restrictions affect the use of resources.
 - c. Qualitative information about management of liquid resources and quantitative information about the availability of liquid resources to meet cash needs for general expenditures within one year of the statement of financial position date.
 - d. Amounts of expenses by both their natural classification and their functional classification in one location as a separate statement or in the notes to the financial statements.
 - e. Methods used to allocate costs among program and support functions.
 - f. Underwater endowment funds.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Change in accounting principle (continued)

3. Reporting investment return net of external and direct internal investment expenses.
4. Use, in the absence of explicit donor stipulations, the placed-in-service approach for reporting expirations of restrictions on gifts of cash or other assets to be used to acquire or construct a long-lived asset and reclassify any amounts from net assets with donor restrictions to net assets without donor restrictions for such long-lived assets that have been placed in service as of the beginning of the period of adoption (thus eliminating the current option to release the donor-imposed restriction over the estimated useful life of the acquired asset).

The amendments have been applied on a retrospective basis in 2018.

In June 2018, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update 2018-08, *Not-For-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made* to clarify and improve the scope and the accounting guidance for contributions received and contributions made. Specifically, this update is to assist entities in evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) or exchange (reciprocal) transactions, as well as determining whether a contribution is conditional. The Museum has adopted ASU 2018-08 during the year ended August 31, 2019.

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.

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 Museum closed the gift shop in December 2018 given the rise of major online retailers (see Note 1). The remaining inventory on hand as of August 31, 2019 was \$14,275.

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."

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments (continued)

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.

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, 2019, and is included in "accrued payroll and related benefits" on the statement of financial position. The accrued vacation balance as of August 31, 2019 was \$292,229.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Deferred revenue

As of August 31, 2019, the Museum had deferred revenue of \$95,255 from advance admissions and the sale of gift cards.

Customer deposits

As of August 31, 2019, the Museum has received deposits of \$3,000 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 contributions without donor restrictions and contributions with donor restrictions, depending on the nature of donor restrictions. Contributions with donor restrictions are reported as increases in net assets with donor restrictions. When the restriction is met the amount is shown as a reclassification of net assets with donor restrictions to net assets without donor restrictions.

Conditional grants and contributions

Conditional grants and contributions are recognized when the Museum meets the terms of the conditions.

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

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Advertising

The Museum's policy is to expense advertising costs as the costs are incurred. Advertising expenses for the year ended August 31, 2019 was \$133,287.

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, 2018, 2017 and 2016 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, 2018, 2017, 2016 and 2015 could be subject to examination by state taxing authorities, generally for four years after they are filed.

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, 2019 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, 2019. Subsequent events have been evaluated through the date the financial statements became available to be issued, January 16, 2020.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

5. INFORMATION REGARDING LIQUIDITY AND FUNDS AVAILABLE

As part of the Museum's liquidity management it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due.

Short-term contributions receivable consists of grants, bequests and pledges receivable expected to be received within one year from August 31, 2019. Unrestricted short-term grants, bequests and pledges receivable will be available to support general operations of the Museum.

Long-term investments include endowment funds consisting of donor-restricted and board-designated endowments. Income from donor-restricted endowments is restricted until appropriated in accordance with the California version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) and, therefore, is not available for general expenditure until appropriated. As described in Note 15, the endowment has a spending rate of up to 5%. Accordingly, approximately \$77,256 of appropriations from the endowment will be available within the next 12 months.

The following is a quantitative disclosure which describes assets that are available within one year of August 31, 2019 to fund general expenditures and other obligations when they become due:

Financial assets	
Cash and cash equivalents	\$ 1,869,108
Investments	6,068,224
Contributions receivable	<u>1,080,508</u>
	<u>9,017,840</u>
Less: amounts unavailable for general expenditure within one year	
Net assets restricted for a specified purpose	(1,849,597)
Board-designated endowment	(2,248,543)
Board-designated for fixed assets reserve	(1,000,000)
Unappropriated earnings on perpetual endowment (\$333,158 less planned appropriation of \$77,256)	(255,902)
Perpetual endowment	<u>(1,161,095)</u>
	<u>(6,515,137)</u>
	<u>\$ 2,502,703</u>

As of August 31, 2019, the Museum had \$2,502,703 of financial assets available to meet cash needs for general expenditures. In addition, the board-designated endowment of \$2,248,543 and the board-designated for fixed assets reserve of \$1,000,000 could be made available in their entirety if needed.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

6. INVESTMENTS

The following table sets forth by level, within the fair value hierarchy, the Museum's assets at fair value as of August 31, 2019:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Fair Value</u>
Stocks and mutual funds	\$ 4,813,945	\$ -	\$ -	\$ 4,813,945
Cash and cash equivalents	1,203,501	-	-	1,203,501
Venture capital funds	-	-	47,997	47,997
Interest receivable	<u>2,781</u>	<u>-</u>	<u>-</u>	<u>2,781</u>
	<u>\$ 6,020,227</u>	<u>\$ -</u>	<u>\$ 47,997</u>	<u>\$ 6,068,224</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.

The following table sets forth a summary of changes in fair value of Level 3 investments for the year as follows:

	<u>ENF III Fund</u>	<u>ENF VII Fund</u>	<u>Total</u>
Balance, beginning of year	\$ 26,870	\$ 75,457	\$ 102,327
Net loss	(188)	(27,460)	(27,648)
Distribution	<u>(26,682)</u>	<u>-</u>	<u>(26,682)</u>
Balance, end of year	<u>\$ -</u>	<u>\$ 47,997</u>	<u>\$ 47,997</u>

The net loss in venture capital funds investments included in the change in unrestricted net assets is composed of \$27,648 in a net unrealized loss.

Net investment income during the year consist of the following:

Interest and dividends	\$ 163,345
Net realized and unrealized loss on investments	(58,174)
Investment expenses	<u>(900)</u>
	<u>\$ 104,271</u>

7. CONTRIBUTIONS RECEIVABLE

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

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

7. CONTRIBUTIONS RECEIVABLE (continued)

Contributions receivable consisted of the following:

Receivable in less than one year	\$ 830,508
Receivable in one to five years	<u>250,000</u>
	<u>\$ 1,080,508</u>

Of the contributions receivable at August 31, 2019, 46%, and 27% are due from two donors.

8. 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.

As the lease is non-cancelable, the Museum recognized the benefit of this lease agreement as donated rent receivable and net assets with donor restrictions. 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>	
2020	\$ 163,991
2021	174,947
2022	186,633
2023	199,100
2024	212,400
Thereafter	<u>7,386,403</u>
	8,323,474
Current portion	<u>(163,991)</u>
	<u>\$ 8,159,483</u>

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

9. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following:

Exhibits	\$ 10,418,886
Leasehold improvements	4,282,777
Equipment	2,580,319
Furniture and fixtures	123,364
Vehicles	37,494
Construction in progress	<u>325,380</u>
	17,768,220
Accumulated depreciation	<u>(10,224,086)</u>
	<u><u>\$ 7,544,134</u></u>

Depreciation expense for the year ended August 31, 2019 was \$1,582,674.

10. 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, 2019.

11. NET ASSETS WITH DONOR RESTRICTIONS

Net assets with donor restrictions consisted of the following:

Donated rent receivable	\$ 8,323,474
Programs and exhibits	1,849,597
Unappropriated earnings on perpetual endowment	333,158
Perpetual endowment	<u>1,161,095</u>
	<u><u>\$ 11,667,324</u></u>

Net assets with donor restrictions released from restriction during the year were as follows:

Donated rent receivable amortization	\$ 153,723
Programs and exhibits	1,021,030
Appropriated earnings on perpetual endowment	<u>78,890</u>
	<u><u>\$ 1,253,643</u></u>

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

12. 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.

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

Rent	\$ 566,277
Art studio costs (capitalized)	175,000
Computer equipment (capitalized)	145,985
Supplies	106,243
Professional services	<u>78,470</u>
	<u><u>\$ 1,071,975</u></u>

13. 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.

14. 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, 2019, in-kind donations received from the board members totaled \$791, with in-kind contributions from their employers totaling \$239,620. During the year ended August 31, 2019, cash contributions received from board members totaled \$431,098, and cash contributions from their employers totaled \$620,682.

15. 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.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

15. 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 net assets with donor restrictions - perpetual endowment (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 net assets with donor restrictions - unappropriated earnings on perpetual endowment 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.

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

15. 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, 2019. 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>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Perpetual endowment	\$ -	\$ 1,161,095	\$ 1,161,095
Unappropriated earnings on perpetual endowment	-	333,158	333,158
Board-designated endowment funds	<u>2,248,543</u>	<u>-</u>	<u>2,248,543</u>
	<u>\$ 2,248,543</u>	<u>\$ 1,494,253</u>	<u>\$ 3,742,796</u>

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

	<u>Unappropriated Earnings on Perpetual Endowment</u>	<u>Perpetual Endowment</u>	<u>Total</u>
Balance, beginning of year	\$ 378,614	\$ 1,161,095	\$ 1,539,709
Interest and dividends	33,434	-	33,434
Appropriations	<u>(78,890)</u>	<u>-</u>	<u>(78,890)</u>
Balance, end of year	<u>\$ 333,158</u>	<u>\$ 1,161,095</u>	<u>\$ 1,494,253</u>

Children's Discovery Museum of San Jose
Notes to Financial Statements
August 31, 2019

15. ENDOWMENT (continued)

Endowment composition (continued)

Changes in board-designated endowment net assets for the year are as follows:

Balance, beginning of year	\$ 3,073,933
Interest and dividends	129,911
Net realized and unrealized loss on investments	(58,174)
Investment fees	(900)
Appropriations	<u>(896,227)</u>
Balance, end of year	<u><u>\$ 2,248,543</u></u>