

Kidspace: A Participatory Museum

Financial Statements

December 31, 2017
(With Comparative Totals for 2016)



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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Kidspace: A Participatory Museum
Pasadena, California

We have audited the accompanying financial statements of Kidspace: A Participatory Museum (a California nonprofit corporation) (the "Museum"), which comprise the statement of financial position as of December 31, 2017, 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 Kidspace: A Participatory Museum as of December 31, 2017, 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.

Other Matter

Management has chosen to supplement the basic financial statements with management's discussion and analysis presented on page 3. Such information is not required by accounting standards generally accepted in the United States of America, but management considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Report on Summarized Comparative Information

We have previously audited Kidspace: A Participatory Museum's 2016 financial statements, and our report dated June 22, 2017 expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2016, is consistent, in all material respects, with the audited financial statements from which it has been derived.



Armanino^{LLP}
Los Angeles, California

May 14, 2018

Kidspace: A Participatory Museum
Management's Discussion and Analysis (Unaudited)
December 31, 2017

Introduction

This management's discussion and analysis of the financial performance of Kidspace: A Participatory Museum ("Kidspace") provides an overview of Kidspace's financial activities for the year ended December 31, 2017. It should be read in conjunction with the accompanying financial statements of Kidspace.

Financial Highlights

- 2017 was a banner year for Kidspace with three major objectives achieved.
 - The Museum successfully closed out our \$13M *Campaign for the Future of Kidspace* by year end 2017.
 - Kidspace paid off notes payable that totaled \$2,598,167 from the initial construction of the Museum.
 - Kidspace broke another attendance record serving over 371,000 guests, largely due to the new outdoor exhibits put into place by our successful capital campaign.
- Kidspace shows an increase in net assets from operations of \$394,429 for 2017 after adjusting for \$1,402,441 of non-cash expenses for depreciation and amortization.

Kidspace: A Participatory Museum
Statement of Financial Position
December 31, 2017
(With Comparative Totals for 2016)

	2017	2016
ASSETS		
Cash	\$ 495,266	\$ 1,286,545
Investments	513,182	1,454,333
Contributions receivable, net	719,689	1,124,729
Inventory	45,074	42,145
Prepaid and other current assets	55,387	35,457
Donated use of long lived asset	632,491	653,400
Property and equipment	16,333,502	17,511,934
Total assets	\$ 18,794,591	\$ 22,108,543
LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable	\$ 97,730	\$ 95,333
Accrued expenses	211,986	175,952
Deferred revenue	466,039	437,004
Notes payable	-	2,598,167
Total liabilities	775,755	3,306,456
Commitments and contingencies (Note 11)		
Net assets		
Unrestricted	16,079,518	15,049,646
Temporarily restricted	1,439,318	3,252,441
Permanently restricted	500,000	500,000
Total net assets	18,018,836	18,802,087
Total liabilities and net assets	\$ 18,794,591	\$ 22,108,543

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

Kidspace: A Participatory Museum
Statement of Activities
For the Year Ended December 31, 2017
(With Comparative Totals for 2016)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2017 Total</u>	<u>2016 Total</u>
Revenues, gains and other support					
Grants and contributions	\$ 286,773	\$ 490,640	\$ -	\$ 777,413	\$ 1,081,838
Gift store revenue, net	188,915	-	-	188,915	168,360
Facility rental	5,730	-	-	5,730	9,668
Other program revenue	264,352	-	-	264,352	200,808
Cafe loss, net	(61,174)	-	-	(61,174)	(59,348)
Admissions and memberships	2,723,076	-	-	2,723,076	2,401,644
Birthday fee	249,946	-	-	249,946	222,962
Special events, net	297,529	-	-	297,529	281,068
Other revenue	19,696	-	-	19,696	25,470
In-kind contributions	137,636	-	-	137,636	83,743
Miscellaneous	48,840	-	-	48,840	29,267
Net assets released from restriction	<u>2,441,986</u>	<u>(2,441,986)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total revenues, gains and other support	<u>6,603,305</u>	<u>(1,951,346)</u>	<u>-</u>	<u>4,651,959</u>	<u>4,445,480</u>
Functional expenses					
Program services	4,792,226	-	-	4,792,226	4,444,922
Management and general	444,288	-	-	444,288	406,547
Fundraising	423,457	-	-	423,457	471,182
Total functional expenses	<u>5,659,971</u>	<u>-</u>	<u>-</u>	<u>5,659,971</u>	<u>5,322,651</u>
Change in net assets from operations	<u>943,334</u>	<u>(1,951,346)</u>	<u>-</u>	<u>(1,008,012)</u>	<u>(877,171)</u>
Non-operating activities					
Investment income	94,913	138,223	-	233,136	73,374
Loss on disposal of property and equipment	<u>(8,375)</u>	<u>-</u>	<u>-</u>	<u>(8,375)</u>	<u>(180,833)</u>
Total non-operating activities	<u>86,538</u>	<u>138,223</u>	<u>-</u>	<u>224,761</u>	<u>(107,459)</u>
Change in net assets	1,029,872	(1,813,123)	-	(783,251)	(984,630)
Net assets, beginning of year	<u>15,049,646</u>	<u>3,252,441</u>	<u>500,000</u>	<u>18,802,087</u>	<u>19,786,717</u>
Net assets, end of year	<u>\$ 16,079,518</u>	<u>\$ 1,439,318</u>	<u>\$ 500,000</u>	<u>\$ 18,018,836</u>	<u>\$ 18,802,087</u>

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

Kidspace: A Participatory Museum
Statement of Functional Expenses
For the Year Ended December 31, 2017
(With Comparative Totals for 2016)

	<u>Program Services</u>	<u>Management and General</u>	<u>Fundraising</u>	<u>2017 Total</u>	<u>2016 Total</u>
Personnel expenses					
Salaries and wages	\$ 1,661,112	\$ 198,110	\$ 301,321	\$ 2,160,543	\$ 1,957,325
Employee benefits	150,730	17,976	27,342	196,048	214,189
Payroll taxes	<u>122,887</u>	<u>14,656</u>	<u>22,291</u>	<u>159,834</u>	<u>144,682</u>
Total personnel expenses	1,934,729	230,742	350,954	2,516,425	2,316,196
Outside services	235,490	48,514	9,679	293,683	318,027
Education expenses	341,745	1,031	1,568	344,344	349,223
Utilities and maintenance	229,362	3,207	4,364	236,933	187,937
Fundraising-other	-	-	39,086	39,086	108,980
Marketing	257,075	-	768	257,843	246,793
Office expense and supplies	134,023	22,325	8,386	164,734	158,976
Interest expense	-	67,729	-	67,729	84,948
In-kind expenses	52,081	60,466	-	112,547	83,743
Insurance	76,623	246	271	77,140	73,096
Other expenses	50,451	4,048	3,542	58,041	51,618
Depreciation and amortization	1,370,587	4,410	4,839	1,379,836	1,310,157
Travel and conferences	105,142	-	-	105,142	28,553
Gift store expenses	<u>4,918</u>	<u>1,570</u>	<u>-</u>	<u>6,488</u>	<u>4,404</u>
	<u>\$ 4,792,226</u>	<u>\$ 444,288</u>	<u>\$ 423,457</u>	<u>\$ 5,659,971</u>	<u>\$ 5,322,651</u>

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

Kidspace: A Participatory Museum
Statement of Cash Flows
For the Year Ended December 31, 2017
(With Comparative Totals for 2016)

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities		
Change in net assets	\$ (783,251)	\$ (984,630)
Adjustments to reconcile change in net assets to net cash used in operating activities		
Depreciation and amortization	1,402,441	1,331,621
Loss on disposal of property and equipment	8,375	180,833
Net realized and unrealized gains on investments	(220,819)	(48,728)
Contributed property and equipment	(25,089)	-
Contributions restricted for long-lived assets	(844,007)	(1,394,990)
Changes in operating assets and liabilities		
Inventory	(2,929)	903
Contributions receivable	405,040	239,502
Prepaid and other current assets	(19,930)	(2,505)
Accounts payable	2,397	(97,717)
Accrued expenses	36,034	32,544
Deferred revenue	29,035	90,358
Net cash used in operating activities	<u>(12,703)</u>	<u>(652,809)</u>
Cash flows from investing activities		
Proceeds from sales of investments	1,490,012	936,831
Purchases of investments	(328,042)	(170,786)
Purchase of property and equipment	(186,386)	(881,184)
Net cash provided by (used in) investing activities	<u>975,584</u>	<u>(115,139)</u>
Cash flows from financing activities		
Repayments on notes payable	(2,598,167)	(300,862)
Contributions restricted for long-lived assets	844,007	1,394,990
Net cash provided by (used in) financing activities	<u>(1,754,160)</u>	<u>1,094,128</u>
Net increase (decrease) in cash	(791,279)	326,180
Cash, beginning of year	<u>1,286,545</u>	<u>960,365</u>
Cash, end of year	<u>\$ 495,266</u>	<u>\$ 1,286,545</u>

Supplemental disclosure of cash flow information

Cash paid during the year interest	\$ 67,729	\$ 84,948
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Supplemental schedule of noncash investing and financing activities

Contributed property and equipment	\$ 25,089	\$ -
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The accompanying notes are an integral part of these financial statements.

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

1. NATURE OF OPERATIONS

Kidspace: A Participatory Museum (the "Museum" or "Kidspace") is a nonprofit corporation which operates a children's museum in Pasadena, California.

The vision of Kidspace is an evolution of the Museum's innovative activities that began over 35 years ago. The focus on kid-driven experiences descends directly from the Museum's early ideal of "A Participatory Museum." The many major and minor accomplishments of the Museum provide a rich background for what is to come.

As the premier children's museum in Southern California, Kidspace is putting plans in place to remain so for years to come. Throughout its history, the Museum has been ahead of the curve in the museum field, from pioneering hands-on, participatory experiences to embracing the unique power of outdoor learning. In recent years, the Museum has seen a record-breaking upswing in attendance through the opening of one-of-a-kind experiences such as the Galvin Physics Forest, the Imagination Workshop, Early Childhood Education Center, and the Arroyo Adventure.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting and financial statement presentation

The financial statements and accompanying notes of the Museum have been prepared using the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP").

The Museum's financial statements are presented on the basis of unrestricted, temporarily restricted, and permanently restricted net assets.

Net assets and changes therein are classified as follows:

- *Unrestricted net assets* - net assets not subject to donor-imposed restrictions.
- *Temporarily restricted net assets* - net assets subject to donor-imposed restrictions that will be met by actions of the Museum and/or the passage of time.
- *Permanently restricted net assets* - net assets subject to donor-imposed restrictions that they be maintained in perpetuity by the Museum.

Revenues are reported as increases in unrestricted net assets unless use of the related asset is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Investment income and gains or losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor restriction or by law.

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Contributions and promises to give

Contributions received are reported as unrestricted, temporarily restricted or permanently restricted, depending upon donor restrictions, if any.

Contributions, including unconditional promises to give, are recognized as revenues in the period the promise is received. Conditional promises to give are not recognized until they become unconditional; that is when the conditions on which they depend are substantially met. Contributions that are promised in one year but are not expected to be collected until after the end of that year are discounted at an appropriate discount rate commensurate with the risks involved. Amortization of any such discounts is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for doubtful contributions receivable is provided based upon management's judgment including such factors as prior collection history, type of contribution and current aging of contributions receivable.

Cash and cash equivalents

The Museum maintains cash and cash equivalents with major financial institutions. The Museum considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Concentration of credit risk

The Museum places its cash and investments with high-credit, quality financial institutions. At times, such cash may be in excess of the FDIC insurance limit. Concentration of credit risk for contributions receivable are generally limited due to the dispersion of these items over a wide donor base. The Museum continually monitors its receivables and establishes valuation reserves as considered appropriate.

Investments

Investment transactions are recorded on trade date. Realized gains and losses on sales of investments are determined on the specific identification basis. Unrealized gains or losses on investments resulting from gain value fluctuations are recorded in the statement of activities during the year.

Fair value measurements

The Museum determines the fair values of its assets and liabilities based on a fair value hierarchy that includes three levels of inputs that may be used to measure fair value (Level 1, Level 2 and Level 3). This hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Kidspac: A Participatory Museum
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurements (continued)

- *Level 1* - Quoted market prices are available in active market for identical assets or liabilities as of the reporting date.
- *Level 2* - Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.
- *Level 3* - Pricing inputs are unobservable and shall be used to measure fair value to the extent that observable inputs are not available. The inputs into the determination of fair value are based upon the best information available and require significant management judgment or estimation.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

The following methods and assumptions were used to estimate the fair value of assets and liabilities:

- Investments (Level 1). Investments in equity and debt securities are valued at their fair values as determined primarily by quoted market prices. Investments without quoted market prices, including real estate investments, are valued at fair value as determined by third-party appraisals, management's estimates or a combination of both.
- Contributions receivable (Level 3). Contributions receivable are valued based on unobservable inputs that are developed based on the best information available in the circumstances. Contributions receivable are not measured at fair value on a recurring basis subsequent to initial recognition.

Contributed goods and services

Contributions of donated noncash assets are recorded at fair value in the period received. Contributions of donated services are recognized if the services received (a) create or enhance long-lived assets, or (b) require specialized skills provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. For the year ended December 31, 2017, Kidspac received in-kind goods and services of \$137,636.

The Museum receives a significant amount of donated services from unpaid volunteers who assist in fund-raising and special projects. No donated services have been recognized in the statement of activities because the criteria for recognition have not been satisfied.

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property and equipment

The Museum capitalizes all property and equipment with a cost greater than \$1,000 with an estimated useful life in excess of one year. Property and equipment is carried at cost or, if donated, at the estimated fair value on the date of the contribution. Minor repairs and maintenance are charged against earnings as incurred. Major repairs and maintenance that extend the useful life of the respective asset are capitalized.

Depreciation and amortization of property and equipment is computed using the straight-line method over the following estimated useful lives:

Buildings	40 years
Exhibits	5 - 40 years
Furniture and equipment	3 - 10 years

Inventory

Inventory consists of products such as educational books, toys, games and crafts. Inventory is valued at the lower of cost or market. The Museum utilizes the weighted average method of inventory valuation.

Deferred revenue

Fees for services, which are paid for in advance, are deferred and recognized as revenue in the period when the services are rendered.

Long lived assets

The Museum reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the book value of the assets may not be recoverable. No impairment losses were recognized during the year ended December 31, 2017.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires Museum management to make estimates and assumptions that affect certain reported amounts and disclosures. Uses of estimates include, but are not limited to, accounting for fair value of investments, the allowance for doubtful accounts and contributions receivable and depreciation. Actual results could differ from those estimates.

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax status

The Museum is a qualified charitable organization exempt from federal income and California franchise taxes under the provisions of Sections 501(c)(3) of the Internal Revenue Code and 23701(d) of the California Revenue and Taxation Code, respectively.

The Museum has evaluated its current tax positions and has concluded that as of December 31, 2017, the Museum does not have any significant uncertain tax positions for which a reserve would be necessary.

Functional expenses

The direct costs of providing the Museum's programs and other activities which are identifiable have been allocated to the related programs or supporting services. Indirect or shared costs are allocated among program and support services by a method that best measures the relative degree of benefit.

Advertising costs

Advertising costs are expensed as incurred. Advertising costs for the year ended December 31, 2017 were \$212,544 and are included in marketing in the statement of functional expenses.

Summarized financial information

The financial statements include certain prior year summarized comparative information in total but not by net asset classification. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Museum's financial statements for the year ended December 31, 2016, from which the summarized information was derived.

Subsequent events

Subsequent events have been evaluated through May 14, 2018, the date that these financial statements were issued. There were no subsequent events that would require adjustments to or disclosures in these financial statements.

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

3. INVESTMENTS

The following table sets forth by level, within the fair value hierarchy, the Museum's assets at fair value as of December 31, 2017:

	Level 1	Level 2	Level 3	Fair Value
Equity mutual funds	\$ 413,667	\$ -	\$ -	\$ 413,667
Fixed income	99,515	-	-	99,515
	\$ 513,182	\$ -	\$ -	\$ 513,182

Investment earnings (losses) during the year consist of the following:

Net realized and unrealized gains	\$ 220,819
Interest and dividend income	12,317
	\$ 233,136

4. CONTRIBUTIONS RECEIVABLE

A discount rate of 2.5% has been used to calculate the present value of pledges receivable.

Contributions receivable consist of the following:

Receivables in less than one year	\$ 335,187
Receivables in one to five years	396,500
	731,687
Less: unamortized discount	(11,998)
	\$ 719,689

5. DONATED USE OF LONG-LIVED ASSET

The Museum leases the property that the museum is located on from the City of Pasadena for a lease cost of \$1 per year. The term of the lease was for fifty years through 2048. The fair market value of this lease was recorded as revenue in the period the property was contributed and the related assets will be expensed as rent over the fifty-year term of the lease. Kidspace is responsible for the renovation, operation and maintenance of the premises.

The terms of the lease stipulate that the property will be returned to the City of Pasadena at the end of the lease. Accordingly, the asset has been classified as temporarily restricted in the accompanying financial statements. The amortization expense of donated use of long-lived asset for the year ended December 31, 2017 was \$20,909. Amortization expense of \$20,909 will be recorded each year through the end of the lease.

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

5. DONATED USE OF LONG-LIVED ASSET (continued)

Donated use of the long-lived asset consists of the following:

Long lived asset	\$ 1,045,440
Accumulated amortization	<u>(412,949)</u>
	<u>\$ 632,491</u>

6. PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

Buildings	\$ 16,817,014
Exhibits	10,167,659
Furniture and equipment	758,780
Construction in progress	<u>144,852</u>
	27,888,305
Accumulated depreciation	<u>(11,554,803)</u>
	<u>\$ 16,333,502</u>

Depreciation expense for the year ended December 31, 2017, was \$1,381,532 (including \$22,605 recorded as café expense).

7. LINE OF CREDIT

During the year ended December 31, 2004, the Museum procured a line of credit for \$10,000,000 for construction of pavilion expansion and exhibits. In October 2013, the Museum converted the line of credit into long-term debt and obtained a line of credit agreement with a bank for a maximum facility of \$300,000. In November 2017, the line of credit was increased to a maximum amount of \$1,000,000. Interest on the line of credit is variable based on the lender's reference rate less 0.5% and due monthly. The Bank's rate was 4.00% at December 31, 2017. The line of credit expires in November 2018. There was no outstanding balance on the line of credit at December 31, 2017.

The line of credit is secured by substantially all of the assets and personal property of Kidspace. The line of credit contains various covenants and restrictions which include, among others, (i) a debt service coverage ratio; (ii) a maximum debt to unrestricted net assets ratio; (iii) minimum unrestricted net assets; and (iv) a minimum bank depository balance requirement. The Museum is in compliance with all covenants as of December 31, 2017.

8. NOTES PAYABLE

The Museum had two notes payable that totaled \$2,598,167 at December 31, 2016. Both notes were paid in full during 2017. Interest expense of \$67,729 was recognized on the notes payable during the year ended December 31, 2017.

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

9. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following:

Capital campaign	\$ 729,299
Donated use of long-lived asset	632,491
Programs and exhibits	55,632
Unexpended endowment earnings	<u>21,897</u>
	<u>\$ 1,439,319</u>

Included within this amount is \$719,689 of contributions receivable as disclosed in Note 4.

10. ENDOWMENT

The Museum's endowment consists of \$500,000 of contributions restricted by donors for investments in perpetuity. Its endowment includes only donor-restricted endowment funds. As required by generally accepted accounting principles (GAAP), net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The primary long-term financial objective for the Museum's endowment is to preserve the real (inflation-adjusted) purchasing power of endowment assets and income after accounting for endowment spending, inflation and costs of portfolio management. The endowment is also managed to optimize the long run total rate of return on invested assets, assuming a prudent level of risk. The goal for this rate of return is one that funds the Museum's existing spending policy and allows sufficient reinvestment to grow the endowment principal at a rate that exceeds inflation (as measured by the Consumer Price Index).

The Museum's Board of Directors is in the process of developing a spending policy that will distribute a specific payout rate of the endowment base to support the Museum's programs. Such a policy will allow for a greater predictability of spendable income for budgeting purposes and for gradual steady growth for the support of operations by the endowments. In addition, this policy will minimize the probability of invading the principal over the long term.

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

10. ENDOWMENT (continued)

Interpretation of relevant law

The Museum's Board of Directors has interpreted 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 in 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 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 organization 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

Endowment composition

Endowment net asset composition by type of fund as of December 31, 2017 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	<u>\$ -</u>	<u>\$ 21,897</u>	<u>\$ 500,000</u>	<u>\$ 521,897</u>

Kidspace: A Participatory Museum
Notes to Financial Statements
December 31, 2017

10. ENDOWMENT (continued)

Endowment composition (continued)

Changes in endowment net assets for the fiscal year ended December 31, 2017 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance, December 31, 2016	\$ -	\$ 133,674	\$ 500,000	\$ 633,674
Investment return				
Investment income	-	138,223	-	138,223
Appropriation for expenditure	<u>-</u>	<u>(250,000)</u>	<u>-</u>	<u>(250,000)</u>
Balance, December 31, 2017	<u>\$ -</u>	<u>\$ 21,897</u>	<u>\$ 500,000</u>	<u>\$ 521,897</u>

11. COMMITMENTS AND CONTINGENCIES

The Museum leases property and equipment under non-cancelable operating leases that expire between 2018 and 2021.

The scheduled minimum lease payments under the lease terms are as follows:

<u>Year Ending December 31,</u>	
2018	\$ 16,450
2019	12,901
2020	6,513
2021	<u>324</u>
	<u>\$ 36,188</u>

Lease expense for the year ended December 31, 2017 was \$16,436.

In addition, the Museum has an operating lease agreement with the City of Pasadena for the intended purpose of the museum. Under the terms of the lease, the Museum pays rent of \$1 per year over the initial fifty-year term which expires in 2048 (See Note 5). In consideration of the favorable lease terms, the Museum has agreed to numerous provisions and covenants with the City of Pasadena, which include hours of operations, displacement events, fees and admission and ownership of improvements.

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11. COMMITMENTS AND CONTINGENCIES (continued)

Legal proceedings

In the ordinary course of conducting business, the Museum becomes involved in various lawsuits. Some of these proceedings may result in judgments being assessed against the Museum which, from time to time, may have an impact on changes in net assets. The Museum believes that these proceedings, individually or in the aggregate, would not have a material effect on the accompanying financial statements.

12. EMPLOYEE BENEFIT PLANS

The Museum offers its employees a 403(b) savings plan administered by Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF), which covers substantially all of the employees to which the Museum may contribute at its discretion. The Museum made no contributions to the plan on behalf of its employees during the year ended December 31, 2017.

13. RELATED PARTY

The Museum received \$52,604 in contributions from board members and other related parties during the year ended December 31, 2017.