

Imagine Children's Museum

Financial Statements with
Independent Auditor's Report

Years Ended December 31, 2019 and 2018

Larson Gross 

Imagine Children's Museum

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Independent Auditor's Report

To the Board of Directors
Imagine Children's Museum
Everett, WA

Report on the Financial Statements

We have audited the accompanying financial statements of Imagine Children's Museum, which comprise the statement of financial position as of December 31, 2019, 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 2019 financial statements referred to above present fairly, in all material respects, the financial position of Imagine Children's Museum as of December 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 discussed in Note 11 to the financial statements, management changed its method of accounting for revenue recognition on contracts with customers due to the adoption of the Financial Accounting Standards Board's Accounting Standards Update 2014-09, "Revenue from Contracts with Customers" (Topic 606). Our opinion is not modified with respect to this matter.

Prior Period Financial Statements

The 2018 financial statements of Imagine Children's Museum as of December 31, 2018, were audited by other auditors whose report dated March 27, 2019, expressed an unmodified opinion on those statements.

Larson Gross PLLC

Bellingham, Washington

March 27, 2020

Imagine Children's Museum

Statements of Financial Position

December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Assets		
Current assets		
Cash	\$ 1,571,723	\$ 985,676
Accounts receivable	51,340	64,360
Pledges receivable	898,527	412,243
Inventory	26,068	14,039
Prepaid expenses and other assets	78,277	19,128
Investments – capital campaign	<u>3,715,000</u>	<u>2,215,000</u>
Total current assets	6,340,935	3,710,446
Noncurrent assets		
Certificate of deposit	78,058	76,514
Pledges receivable, noncurrent and net of discount	1,406,878	701,628
Property and equipment, net	6,486,776	6,543,429
Investments – board-designated reserves	5,036,337	5,001,646
Investments – endowment	<u>1,257,544</u>	<u>1,061,480</u>
Total assets	<u>\$ 20,606,528</u>	<u>\$ 17,095,143</u>
Liabilities and Net Assets		
Current liabilities		
Accounts payable	\$ 77,014	\$ 7,591
Accrued expenses	56,638	49,609
Deferred membership revenue	379,079	339,767
Deferred grant revenue	37,500	-
Gift certificates outstanding	<u>70,768</u>	<u>55,891</u>
Total current liabilities	620,999	452,858
Service award payable	<u>75,000</u>	<u>75,000</u>
Total liabilities	695,999	527,858
Net assets		
Without donor restrictions		
Investment in property and equipment	6,486,776	6,543,429
Board-designated – reserves	5,036,337	5,001,646
Undesignated	<u>1,524,135</u>	<u>273,906</u>
Total net assets without donor restrictions	13,047,248	11,818,981
With donor restrictions	<u>6,863,281</u>	<u>4,748,304</u>
Total net assets	<u>19,910,529</u>	<u>16,567,285</u>
Total liabilities and net assets	<u>\$ 20,606,528</u>	<u>\$ 17,095,143</u>

Imagine Children's Museum

Statements of Activities

Years Ended December 31, 2019 and 2018

	2019			2018		
	Without Donor Restrictions	With Donor Restrictions	Total	Without Donor Restrictions	With Donor Restrictions	Total
Support and revenue						
Admissions and program fees	\$ 999,840	\$ -	\$ 999,840	\$ 949,023	\$ -	\$ 949,023
Memberships	697,998	-	697,998	632,425	-	632,425
Contributions and grants	449,880	-	449,880	519,122	122,771	641,893
Capital campaign contributions	-	2,518,124	2,518,124	-	585,786	585,786
Special events, net of direct expenses of \$7,761 and \$4,908 for 2019 and 2018, respectively	220,183	-	220,183	246,743	-	246,743
Gift shop sales, net of cost of sales of \$71,787 and \$74,868 for 2019 and 2018, respectively	82,148	-	82,148	85,916	-	85,916
Parking revenue, net of cost of revenue of \$31,676 and \$18,625 for 2019 and 2018, respectively	35,962	-	35,962	44,966	-	44,966
Investment return (loss)	839,383	196,064	1,035,447	(197,157)	(57,673)	(254,830)
Other income	5,167	-	5,167	3,627	-	3,627
Net assets released from restrictions	599,211	(599,211)	-	142,177	(142,177)	-
Total support and revenue	3,929,772	2,114,977	6,044,749	2,426,842	508,707	2,935,549
Expenses						
Program services	2,337,022	-	2,337,022	1,835,719	-	1,835,719
Management and general	195,481	-	195,481	194,489	-	194,489
Fundraising	169,002	-	169,002	143,536	-	143,536
Total expenses	2,701,505	-	2,701,505	2,173,744	-	2,173,744
Change in net assets	1,228,267	2,114,977	3,343,244	253,098	508,707	761,805
Net assets – beginning of year	11,818,981	4,748,304	16,567,285	11,565,883	4,239,597	15,805,480
Net assets – end of year	\$ 13,047,248	\$ 6,863,281	\$ 19,910,529	\$ 11,818,981	\$ 4,748,304	\$ 16,567,285

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

Imagine Children's Museum

Statements of Functional Expenses

Years Ended December 31, 2019 and 2018

	2019				2018			
	Program Services	Management and General	Fundraising	Total	Program Services	Management and General	Fundraising	Total
Salaries and wages	\$ 1,188,240	\$ 88,617	\$ 126,508	\$ 1,403,365	\$ 975,311	\$ 107,046	\$ 107,046	\$ 1,189,403
Payroll taxes	120,220	9,084	12,968	142,272	94,494	10,371	10,371	115,236
Benefits	64,489	5,027	7,176	76,692	46,187	5,069	5,069	56,325
	<u>1,372,949</u>	<u>102,728</u>	<u>146,652</u>	<u>1,622,329</u>	<u>1,115,992</u>	<u>122,486</u>	<u>122,486</u>	<u>1,360,964</u>
Depreciation	277,138	41,411	-	318,549	259,399	38,761	-	298,160
Repairs and maintenance	187,116	444	635	188,195	42,335	6,326	-	48,661
Communications	80,731	6,809	9,727	97,267	54,844	6,020	6,020	66,884
Janitorial	57,115	8,527	-	65,642	53,586	5,882	5,882	65,350
Bank and credit card fees	49,654	-	2,613	52,267	46,818	-	-	46,818
Capital expansion planning	49,169	-	-	49,169	10,688	-	-	10,688
Utilities	44,270	1,296	-	45,566	32,869	3,608	3,608	40,085
Exhibit maintenance and mural	43,448	-	-	43,448	34,677	-	-	34,677
Education	41,550	-	-	41,550	35,520	-	-	35,520
Insurance	27,351	8,637	-	35,988	31,987	4,780	-	36,767
Advertising and community relations	25,885	5,000	-	30,885	34,951	-	-	34,951
Office	24,941	831	1,940	27,712	18,644	2,046	2,046	22,736
Printing and postage	22,141	984	984	24,109	19,849	2,178	2,178	24,205
Miscellaneous	<u>33,564</u>	<u>18,814</u>	<u>6,451</u>	<u>58,829</u>	<u>43,560</u>	<u>2,402</u>	<u>1,316</u>	<u>47,278</u>
Total expenses	<u>\$ 2,337,022</u>	<u>\$ 195,481</u>	<u>\$ 169,002</u>	<u>\$ 2,701,505</u>	<u>\$ 1,835,719</u>	<u>\$ 194,489</u>	<u>\$ 143,536</u>	<u>\$ 2,173,744</u>

Imagine Children's Museum

Statements of Cash Flows

Years Ended December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Cash flows from operating activities		
Changes in net assets	\$ 3,343,244	\$ 761,805
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation expense	318,549	298,160
Investment (return) loss	(1,030,755)	254,830
Capital campaign contributions	(2,518,124)	(585,786)
Change in discount on long-term pledges	20,241	9,374
(Increase) decrease in assets		
Accounts receivable	13,020	20,349
Pledges receivable	(31,874)	877,181
Inventory	(12,029)	3,968
Prepaid expenses and other assets	3,603	(5,692)
Increase (decrease) in liabilities		
Accounts payable	69,423	(2,157)
Accrued expenses	7,029	14,542
Deferred membership revenue	39,312	(58,591)
Deferred grant revenue	37,500	-
Gift certificates outstanding	<u>14,877</u>	<u>5,920</u>
Net cash provided by operating activities	274,016	1,593,903
Cash flows from investing activities		
Purchases of property and equipment	(261,896)	(97,376)
Change in value of certificate of deposit	(1,544)	(1,514)
Purchases of investments	<u>(700,000)</u>	<u>(2,135,000)</u>
Net cash used by investing activities	(963,440)	(2,233,890)
Cash flows from financing activities		
Cash received for capital campaign	1,338,223	561,707
Long-term debt fees deposit	<u>(62,752)</u>	<u>-</u>
Net cash provided by financing activities	<u>1,275,471</u>	<u>561,707</u>
Net increase (decrease) in cash	586,047	(78,280)
Cash – beginning of year	<u>985,676</u>	<u>1,063,956</u>
Cash – end of year	<u><u>\$ 1,571,723</u></u>	<u><u>\$ 985,676</u></u>
Supplemental Disclosure of Cash Flow Information		
Non-cash investment activity:		
Reinvestment of interest and dividends	<u><u>\$ (219,835)</u></u>	<u><u>\$ (154,365)</u></u>

Notes to Financial Statements

December 31, 2019 and 2018

Note 1 – Summary of Significant Accounting Policies

Nature of activities – Imagine Children's Museum (the Museum) was established November 27, 1991, as a nonprofit corporation in the State of Washington. The Museum is located in Everett, WA. The Museum's mission is to utilize playful learning to enrich children's lives. The Museum is committed to:

- Celebrating creativity and imagination
- Helping young learners thrive
- Instilling a community connection
- Learning experiences powered by play
- Developing unique exhibits and programs
- Reaching out to all children
- Embracing diversity and inclusion
- Nurturing child/caring adult interaction

During 2017, the Museum started a \$25 million capital campaign. The Museum anticipates adding a 40,000 square foot addition to the existing building to provide additional exhibit space, educational classrooms, outdoor play space, office space, and a shop for exhibit fabrication and maintenance. Capital campaign contributions, including pledges, raised to date totaled approximately \$6.1 million as of December 31, 2019.

Basis of accounting – The Museum prepares its financial statements on the accrual basis of accounting and accordingly reflect all significant assets, payables, and other liabilities. Revenues are recognized when earned or contributed and expenditures are recognized when incurred.

Basis of presentation – The Museum reports information regarding its financial position and activities according to two classes of net assets that are based upon the existence or absence of restrictions on use that are placed by its donors: net assets without donor restrictions and net assets with donor restrictions.

Net assets without donor restrictions – Support received that is not subject to donor-imposed restrictions and over which the Board of Directors has discretionary control.

Net assets with donor restrictions – Support received subject to donor-imposed restrictions or time restrictions that will be met either through actions of the Museum or by passage of time, including contributions restricted by the donor to be invested in perpetuity. In accordance with purposes stipulated by donors, earnings from such assets may be classified as net assets without donor restrictions or net assets with donor restrictions.

Revenues are reported as increases in net assets without donor restrictions unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in net assets without donor restrictions. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in net assets without donor restrictions unless their use is restricted by explicit donor stipulation or by law. In the period donor restrictions are met, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statement of activities as satisfaction of restrictions. In addition, if a restriction is fulfilled in the same year in which the contribution is received, the Museum reports the support as without donor restrictions.

Notes to Financial Statements

December 31, 2019 and 2018

Note 1 – Summary of Significant Accounting Policies – (Continued)

Cash and cash equivalents – Cash and cash equivalents consist of cash in banks and all highly liquid instruments purchased with an initial maturity of three months or less for statement of cash flow purposes. Cash equivalents excludes cash and cash equivalents balances included in the Museum’s investment portfolio and subject to its investment policy. The Museum maintains its cash in bank accounts that may exceed federally insured limits at times during the year. The Museum has not experienced any losses in these accounts, and management does not believe it is exposed to any significant credit risk.

Certificates of deposit – Certificates of deposit are recorded at cost plus accrued interest.

Accounts receivable – Accounts receivable, including reimbursable grants receivable, are recorded at their net realizable value. Net realizable value is equal to the gross amount of accounts receivable less an estimated allowance for doubtful accounts. Management of the Museum bases its estimates of doubtful accounts on several factors. These factors include the Museum’s prior experience collecting accounts receivable, the aging of the receivables at year-end, and management’s appraisal of current economic conditions. Based on the above factors, management considers all accounts receivables to be fully collectible and therefore has not made any allowance for uncollectible accounts receivable. All accounts receivable are expected to be collected within one year.

Pledges receivable – Unconditional promises to give (pledges) that are expected to be collected within one year are recorded at net realizable value. Pledges expected to be collected in future years are initially recorded at fair value using present value techniques incorporating risk-adjusted discount rates designed to reflect the assumptions market participants would use in pricing the asset. In subsequent years, amortization of the discounts is included in contribution revenue in the statements of activities. Management determines the allowance for uncollectible pledges based on historical experience, an assessment of economic conditions, and a review of subsequent collections. Pledges are written off when deemed uncollectible. Based on the above factors, management considers all pledges to be fully collectible and therefore has not made any allowance for uncollectible pledges.

Inventory – Inventory consists of merchandise sold in the gift shop and is valued at the lower of cost or market using the first in, first out (FIFO) method.

Property and equipment – The Museum capitalizes all property and equipment acquisitions in excess of \$1,000. Property and equipment are recorded at cost or, if acquired as a donation, at the estimated fair market value on the date acquired. Property and equipment are depreciated using the straight-line method over estimated useful lives of 3 to 30 years. Major expenditures for new property, and those which substantially increase useful lives of existing property, are capitalized. Maintenance, repairs, and minor renewals are expensed as incurred.

Investments – Investments consist of marketable securities and are recorded at fair value. Realized and unrealized investment gains and losses, interest and dividends, and investment fees are included in investment return on the statements of activities. Investment return or loss is reported as an increase or decrease in net assets without donor restrictions unless the investment return on restricted assets also is restricted by the donor or law, resulting in such investment return being recorded as with donor restrictions until time or purpose restrictions are satisfied.

Notes to Financial Statements

December 31, 2019 and 2018

Note 1 – Summary of Significant Accounting Policies – (Continued)

Revenue recognition – The transaction price is the amount of consideration to which the Museum expects to be entitled in exchange for transferring goods and services to the customer. Admissions and program fees and special events are recognized at the later of the point of sale or when the related program occurs. Memberships provided by the Museum are purchased for one-year terms. Membership revenue is the only revenue stream recognized over time and is recognized ratably over the course of the year, beginning in the month purchased. Deferred membership revenue is recorded as a contract liability when consideration is received prior to revenue being recognized. Deferred membership revenue totaled \$378,079, \$339,767, and \$398,358 at December 31, 2019, 2018, and 2017, respectively. Gift shop sales and parking revenue are recognized at the point of sale, which is when the Museum's performance obligation is satisfied.

Revenue from these activities as a percentage of total support and revenue totaled: admissions and program fees 17% and 32%; memberships 12% and 22%; and gift shop and parking, net 2% and 5%, for the years ended December 31, 2019 and 2018, respectively. The decline in percentage of total support and revenue from earned sources year-over-year is the result of capital campaign contributions making up 42% of total support and revenue in 2019, compared to 20% in 2018. Results of activities are substantially impacted by economic conditions, which can vary significantly by market and can be impacted by consumer disposable income and spending habits.

Contributions and grants – Contributions are recognized upon the earlier of receipt or when an unconditional promise to give is made. Conditional promises to give are recognized only when the conditions on which they depend are substantially met and the promises become unconditional.

Grant advances received by the Museum that are in excess of current year grant expenditures are recognized as deferred grant revenue. Such amounts are restricted funds and as such can only be maintained and used in accordance with the respective grant contracts.

Donated goods and services – Donations of goods and services are recorded at their estimated fair values at the date of donation. Donated services are recognized if the services received (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased. In addition, many volunteers have donated significant amounts of time to the Museum's activities. The services of these volunteers are not recorded in the accompanying financial statements as they do not meet the criteria for recognition.

Advertising – Advertising costs are expensed as incurred. Advertising expense is presented as advertising and promotion expense in the statements of functional expenses and totaled \$30,885 and \$34,510 for the years ended December 31, 2019 and 2018, respectively.

Sales taxes – Taxes collected from customers for amounts assessed by governmental authorities on revenue producing transactions are recorded on a net basis and are not included in the amounts on the accompanying statements of activities.

Federal income taxes – The Museum is a non-profit corporation exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. The Museum files IRS Form 990 which is open for IRS examination for three years after the filing due date.

Notes to Financial Statements

December 31, 2019 and 2018

Note 1 – Summary of Significant Accounting Policies – (Continued)

Functional allocation of expenses – The costs of providing various programs and other activities have been summarized on a functional basis in the accompanying statements of functional expenses. Accordingly, certain costs have been allocated among programs and supporting services benefited and have been allocated on a reasonable basis that is consistently applied. Salaries and wages, benefits, and payroll taxes are allocated based on time and effort. All other allocated expenses are allocated based on estimates of usage.

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. Such estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications – Certain reclassifications have been made to the prior year's financial statements to conform to the current year's financial statement presentation. The most significant reclassification was board-designated endowment net assets reclassified to donor-restricted endowment net assets based on the presence of explicit donor restrictions on the principal balance and no board appropriations of endowment earnings.

Subsequent events – In preparing the financial statements, the Museum has evaluated events and transactions for potential recognition or disclosure through March 27, 2020, the date that the financial statements were available to be issued.

Note 2 – Liquidity and Availability

Financial assets available for general expenditure within one year consist of the following at December 31:

	2019	2018
Cash	\$ 1,571,723	\$ 985,676
Certificate of deposit	78,058	76,514
Accounts receivable	51,340	64,360
Pledges receivable	2,305,405	1,113,871
Investments	10,008,881	8,278,126
Less amounts not available for general expenditure within one year		
Certificate of deposit	(78,058)	(76,514)
Pledges receivable collectible in greater than one year	(1,406,878)	(701,628)
Donor-restricted	(6,863,281)	(4,748,304)
Board-designated reserves	(5,036,337)	(5,001,646)
	<u>\$ 630,853</u>	<u>\$ (9,545)</u>

The Museum has certain donor-restricted assets limited to use, which are not available for general expenditure within one year in the normal course of operations. Accordingly, these assets have not been included in the qualitative information above.

Notes to Financial Statements

December 31, 2019 and 2018

Note 2 – Liquidity and Availability – (Continued)

The Museum holds a three-year certificate of deposit to fund the service award payable in future years.

The Museum maintains board-designated reserves and a donor-restricted endowment for purposes other than general expenditure. The board-designated reserves may be drawn upon, if necessary, to meet unexpected needs (see additional descriptions in Note 8). The non-principal balance of the donor-restricted endowment represents accumulated earnings, which have not been appropriated by the Board as of December 31, 2019. These earnings could be appropriated for general expenditure, if necessary.

As part of the Museum's liquidity management plan, cash in excess of daily requirements may be invested in short-term investments and money market funds.

Note 3 – Pledges Receivable

Pledges receivable are due according to the following schedule:

	2019	2018
Receivable in less than one year	\$ 898,527	\$ 412,243
Receivable in one to five years	1,464,686	739,195
Total pledges receivable, gross	2,363,213	1,151,438
Less discount to net present value at rates ranging from 1.13% to 4.5%	(57,808)	(37,567)
	<u>\$ 2,305,405</u>	<u>\$ 1,113,871</u>

Pledges receivable from three donors made up 71% of total pledges receivable for the year ended December 31, 2019. Pledges receivable from one donor made up 72% of total pledges receivable for the year ended December 31, 2018. Contributions from one donor made up 34% and 10% of total contribution revenue (including capital campaign contributions) for the years ended December 31, 2019 and 2018, respectively.

Note 4 – Property and Equipment

Property and equipment consist of the following at December 31:

	2019	2018
Land	\$ 3,632,752	\$ 3,632,752
Buildings and improvements	3,972,260	3,972,260
Exhibits	2,518,325	2,502,290
Furniture and equipment	518,551	507,262
Capital campaign project pre-construction	258,425	23,852
Total property and equipment, at cost	10,900,313	10,638,416
Less accumulated depreciation	(4,413,537)	(4,094,987)
Total property and equipment, net	<u>\$ 6,486,776</u>	<u>\$ 6,543,429</u>

Notes to Financial Statements

December 31, 2019 and 2018

Note 4 – Property and Equipment – (Continued)

Depreciation expense totaled \$318,549 and \$298,160 for the years ended December 31, 2019 and 2018, respectively.

Note 5 – Fair Value Measurements

Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, *Fair Value Measurements and Disclosures*, establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value.

The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy under FASB ASC 820 are described as follows:

Level 1: Observable inputs to the valuation methodology that are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2: Observable inputs to the valuation methodology other than quoted market prices (unadjusted) for identical assets or liabilities in active markets. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, quoted prices for identical assets in markets that are not active, and inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability.

Level 3: Inputs to the valuation methodology that are unobservable for the asset or liability and significant to the fair value measurement.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for the investments measured at fair value.

Money market funds, mutual funds, and equities:

Investments are measured at fair value based on the actively traded daily closing price. These investments are registered with the Securities and Exchange Commission and are required to publish their daily net asset value and to transact at that price. These investments held by the Museum are deemed to be actively traded.

Fixed income securities:

Bonds are valued using either the yields currently available on comparable securities of issuers with similar credit ratings or using a discounted cash flows approach that utilizes observable inputs, such as current yields of similar instruments, but includes adjustments for certain risks that may not be observable, such as credit and liquidity risks.

Notes to Financial Statements

December 31, 2019 and 2018

Note 5 – Fair Value Measurements – (Continued)

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Museum believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date. There have been no changes in methodologies used during the years ended December 31, 2019 and 2018.

The following tables set forth by level, within the fair value hierarchy, the Museum's investments at fair value as of December 31:

	2019			
	Level 1	Level 2	Level 3	Total
Money market funds	\$ 2,079,905	\$ -	\$ -	\$ 2,079,905
Mutal funds	3,412,566	-	-	3,412,566
Fixed income securities	4,015,014	-	-	4,015,014
Equities	501,396	-	-	501,396
Total	<u>\$ 10,008,881</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 10,008,881</u>

	2018			
	Level 1	Level 2	Level 3	Total
Money market funds	\$ 2,119,318	\$ -	\$ -	\$ 2,119,318
Mutal funds	98,419	-	-	98,419
Fixed income securities	3,771,091	-	-	3,771,091
Equities	2,289,298	-	-	2,289,298
Total	<u>\$ 8,278,126</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,278,126</u>

To assess the appropriate classification of investments within the fair value hierarchy, the availability of market data is monitored. Changes in economic conditions or valuation techniques may require the transfer of investments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period.

The Museum evaluated the significance of transfers between levels based upon the nature of the investment and size of the transfer relative to total net assets. For the years ended December 31, 2019 and 2018, there were no significant transfers between Levels 1 and 2 and no transfers in or out of Levels 3.

Note 6 – Service Award Payable

Beginning November 1, 2017, Museum employees who work five years of full-time employment or 10,400 hours will receive a service award of \$5,000. At both December 31, 2019 and 2018, the amount estimated was \$75,000.

Notes to Financial Statements

December 31, 2019 and 2018

Note 7 – Board-Designated Net Assets

The Board of Directors of the Museum is committed to ensuring that the Museum is sustainable for generations to come. The board-designated reserves help to safeguard the Museum from financial events that could significantly impact its future. Accordingly, board-designated reserves have been created and maintained for the following purposes.

- *Operating Reserve* – Funds are meant to sustain operation during an unexpected or uncontrollable event such as pandemic flu, terrorist attack, or a major street closure. It could also be used to support operations if one of the major fundraising events failed due to circumstances beyond the Museum’s control, such as weather, earthquake, etc. The Operating Reserve should approximate six months of the Museum’s operating budget.
- *Unanticipated Main Museum Facility Expense Reserve* – Funds are meant to cover costs such as upkeep, property tax, insurance, parking lot resurfacing, remediation, abatement, code changes, elevator, etc. Funds are also available for studies or other expenses related to property development.
- *Pacific & Colby Building/Parking Lot Reserve* – Funds are meant to cover costs such as upkeep, property tax, insurance, parking lot resurfacing, remediation, abatement, code changes, elevator, etc. Funds are also available for studies or other expenses related to property development.
- *Exhibit Revitalization and Major Repair Reserve* – Funds are meant to cover unfunded costs associated with emergent revitalization, major repairs, or replacement of existing exhibits such as the Outdoor Adventure.
- *Capital Expansion Transitioning Funds* – Funds are meant to cover costs associated with transitioning that needs to occur during expansion such as bringing on new staff, training, income lost from closures due to construction.

Board-designated net assets consist of the following at December 31:

	<u>2019</u>	<u>2018</u>
Operating Reserve	\$ 2,086,337	\$ 1,566,646
Unanticipated Main Museum Facility Expense Reserve	450,000	400,000
Pacific & Colby Building/Parking Lot Reserve	500,000	750,000
Exhibit Revitalization & Major Repair Reserve	1,000,000	1,000,000
Capital Expansion Transitioning Funds	<u>1,000,000</u>	<u>1,285,000</u>
	<u>\$ 5,036,337</u>	<u>\$ 5,001,646</u>

Notes to Financial Statements

December 31, 2019 and 2018

Note 8 – Net Assets with Donor Restrictions

Net assets with donor restrictions consist of the following at December 31:

	2019	2018
Capital campaign	\$ 5,605,737	\$ 3,576,757
Endowment principal	500,000	500,000
Endowment earnings not yet appropriated	757,544	561,480
Other programs	-	110,067
	<u>\$ 6,863,281</u>	<u>\$ 4,748,304</u>

Note 9 – Endowment

The Museum's endowment consists of one individual fund at December 31, 2019.

Interpretation of relevant law – The State of Washington has passed a version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA). The Board of Governors of the Museum has interpreted UPMIFA as requiring the preservation of the fair value of the original gift at the gift date of 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 a) the original value of the gifts donated to the donor-restricted endowment plus b) the original value of subsequent gifts to the donor-restricted endowment. The remaining portion of the donor-restricted endowment fund that is time- or purpose- restricted is classified as net assets with donor restrictions until those amounts are appropriated for expenditure by the Museum in a manner consistent with the standards of UPMIFA.

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

- Duration and preservation of the fund
- Purposes of the Museum and the donor restricted endowment fund
- General economic conditions
- Possible effects of inflation and deflation
- Expected total return from income and the appreciation of investments
- Other resources of the Museum
- Investment policies of the Museum

The composition of net assets by type of endowment fund at December 31 is as follows:

	2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Donor-restricted principal	\$ -	\$ 500,000	\$ 500,000
Earnings not yet appropriated	-	757,544	757,544
Total endowment net assets	<u>\$ -</u>	<u>\$ 1,257,544</u>	<u>\$ 1,257,544</u>

Notes to Financial Statements

December 31, 2019 and 2018

Note 9 – Endowment – (Continued)

	2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Donor-restricted principal	\$ -	\$ 500,000	\$ 500,000
Earnings not yet appropriated	-	561,480	561,480
Total endowment net assets	<u>\$ -</u>	<u>\$ 1,061,480</u>	<u>\$ 1,061,480</u>

Changes in endowment net assets for the years ended December 31 consist of:

	2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, beginning of year	\$ -	\$ 1,061,480	\$ 1,061,480
Endowment investment return	-	196,064	196,064
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 1,257,544</u>	<u>\$ 1,257,544</u>

	2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, beginning of year	\$ -	\$ 1,119,153	\$ 1,119,153
Endowment investment loss	-	(57,673)	(57,673)
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 1,061,480</u>	<u>\$ 1,061,480</u>

Return objectives and risk parameters – It is the policy of the Museum to invest its endowments in order to support operations in perpetuity. The Museum has developed investment guidelines which have been designed to allow for sufficient flexibility in the management oversight process to capture investment opportunities as they may occur, while at the same time setting forth reasonable risk control parameters to ensure prudence and care in the execution of the investment program.

The endowment investment objective is to ensure that the future growth of the fund is sufficient to offset normal inflation plus reasonable spending, thereby preserving the constant dollar value and purchasing power of the fund. This will be accomplished through carefully planned and executed long-term investment strategy. The objective of the investment strategy is to enhance the fund's long-term viability by maximizing the value of the fund within a prudent risk level.

Strategies employed for achieving objectives – To satisfy its long-term rate-of-return objectives, the Museum seeks an investment return, over a full market cycle, which exceeds the amount distributed for use plus the average rate of inflation over that market cycle. The target asset allocation for endowment investments is 50-70% equity, 25-45% fixed income investments, with the balance in cash equivalents and other investments. Within these broad categories, the Museum seeks investments that provide diversification and enhance fund returns.

Notes to Financial Statements

December 31, 2019 and 2018

Note 9 – Endowment – (Continued)

Spending policy and how the investment objectives relate to spending policy – The Board of Directors has approved an endowment spending policy that allows for continuing support of Museum operations. The policy allows for annual distributions from the endowment of 4% of the assets based on a three-year rolling average. The Museum did not take any distributions from the endowment during 2019 and 2018.

Funds with deficiencies – From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level the Museum is required to retain as a fund of perpetual duration pursuant to donor stipulation or UPMIFA (underwater endowments). The Museum has interpreted UPMIFA to permit spending from underwater endowments in accordance with prudent measures required under law. In accordance with GAAP, deficiencies of this nature are reported in net assets with donor restrictions. There were no deficiencies of this nature for the years ended December 31, 2019 and 2018.

Note 10 – Retirement Plan

The Museum sponsors a Simple IRA plan (the Plan). Employees that received \$5,000 in gross wages in the prior year and the current year are eligible for the Plan. The employer contribution for eligible employees is 3% of gross wages and totaled \$15,862 and \$16,283 for the years ended December 31, 2019 and 2018, respectively.

Note 11 – Impact of Accounting Method Change

The FASB issued new guidance that created Topic 606, *Revenue from Contracts with Customers*, in ASC. Topic 606 supersedes the revenue recognition requirements in FASB ASC 605, *Revenue Recognition*, and requires the recognition of revenue when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled in exchange for those goods or services. The Museum adopted the requirements of the new guidance as of January 1, 2019, utilizing the modified retrospective method of transition. The Museum did not recognize any adjustments in changes in revenue, net assets, or any other financial statement line item as a result of adopting ASC 606.

Note 12 – Subsequent Event

On January 30, 2020, the World Health Organization declared the coronavirus outbreak a "Public Health Emergency of International Concern" and on March 10, 2020, declared it to be a pandemic. Actions taken around the world to help mitigate the spread of the coronavirus include restrictions on travel, and quarantines in certain areas, and forced closures for certain types of public places and businesses. The coronavirus and actions taken to mitigate it have had and are expected to continue to have an adverse impact on the economies and financial markets of many countries, including the geographical area in which the Museum operates. While it is unknown how long these conditions will last and what the complete financial effect will be to the Museum, to date, the Museum is experiencing declining revenue; temporarily discontinued operations; and significant changes in the fair value of investments. It is reasonably possible that estimates made in the financial statements have been, or will be, materially and adversely impacted in the near term as a result of these conditions.