

# Marine Corps Heritage Foundation and Affiliate

## Consolidated Audited Financial Statements and Other Financial Information

*Year ended December 31, 2018  
with Report of Independent Auditors*

Marine Corps Heritage Foundation  
and Affiliate

Consolidated Audited Financial Statements  
and Other Financial Information

Year ended December 31, 2018

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## Report of Independent Auditors

Board of Directors  
Marine Corps Heritage Foundation  
Triangle, Virginia

We have audited the accompanying consolidated financial statements of Marine Corps Heritage Foundation and Affiliate (the Foundation) which comprise the consolidated statement of financial position as of December 31, 2018, and the related consolidated statements of activities, functional expenses and cash flows for the year then ended and the related notes to the consolidated financial statements.

### ***Management's Responsibility for the Consolidated Financial Statements***

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 over financial reporting. 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Foundation as of December 31, 2018 and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**Emphasis of Matter**

As discussed in Note A to the financial statements, management adopted ASU 2016-14 *Not for Profit Entities (topic 958) Presentation of Financial Statements of Not-for-Profit-Entities*. The adoption did result in a reclassification of the Museum and Heritage Center balance of \$74,104,293 from net assets with donor restriction to net assets without donor restriction, effective January 1, 2018, which is reflected on the consolidated statement of activities. Our opinion is not modified with respect to this matter.

**Other Matter**

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The Consolidating Statement of Financial Position as of December 31, 2018, and Consolidating Statement of Activities for the year then ended, are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

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

Vienna, Virginia  
April 22, 2019

Marine Corps Heritage Foundation  
and Affiliate

Consolidated Statement of Financial Position

December 31, 2018

**Assets**

Cash and cash equivalents	\$	2,666,682
Investments		14,652,780
Accounts receivable		341,647
Pledges receivable, net		6,514,085
Prepaid expenses		198,535
Heritage Center, net		81,003,840
Construction in progress		23,792,558
Fixed assets, net		974,078
Cash surrender value of life insurance policies		138,104
Retirement plan assets		<u>331,354</u>
Total assets	\$	<u>130,613,663</u>

**Liabilities and net assets**

Liabilities:

Accounts payable and accrued expenses	\$	455,488
Notes payable		7,447,236
Retirement plan liabilities		<u>331,354</u>
Total liabilities		8,234,078

Net assets:

Without donor restrictions		120,264,475
With donor restrictions		<u>2,115,110</u>
Total net assets		<u>122,379,585</u>
Total liabilities and net assets	\$	<u>130,613,663</u>

See accompanying notes to the consolidated financial statements.

Marine Corps Heritage Foundation  
and Affiliate

Consolidated Statement of Activities

Year ended December 31, 2018

	Without Donor <u>Restrictions</u>	With Donor <u>Restrictions</u>	<u>Total</u>
<b>Revenue, gains and other support</b>			
Contributions	\$ 9,496,508	\$ 265,385	\$ 9,761,893
Museum gift shop income	338,451	-	338,451
Theater/rifle range revenue	218,797	-	218,797
Other revenue	182,088	-	182,088
Special events	184,187	-	184,187
In-kind support	71,031	16,232	87,263
Investment income, net	167,003	29,360	196,363
Net assets released from restrictions	<u>214,833</u>	<u>(214,833)</u>	<u>-</u>
Total revenue, gains and other support	10,872,898	96,144	10,969,042
<b>Expenses</b>			
Program services:			
Museum & Heritage Center	8,426,666	-	8,426,666
Marine Corps University History Division	303,177	-	303,177
Other historical support	<u>465,564</u>	<u>-</u>	<u>465,564</u>
Total program services	9,195,407	-	9,195,407
Supporting services:			
Fundraising	2,478,103	-	2,478,103
General and administrative	<u>992,541</u>	<u>-</u>	<u>992,541</u>
Total supporting services	<u>3,470,644</u>	<u>-</u>	<u>3,470,644</u>
Total expenses	<u>12,666,051</u>	<u>-</u>	<u>12,666,051</u>
Change in net assets, before change in fair value of investments	(1,793,153)	96,144	(1,697,009)
Change in fair value of investments	<u>(251,550)</u>	<u>(17,098)</u>	<u>(268,648)</u>
Change in net assets	(2,044,703)	79,046	(1,965,657)
Reclassification of net assets	(483,990)	483,990	-
Net assets, beginning of year	48,688,875	75,656,367	124,345,242
Adoption of ASU 2016-14, beginning of year	<u>74,104,293</u>	<u>(74,104,293)</u>	<u>-</u>
Net assets, end of year	<u>\$ 120,264,475</u>	<u>\$ 2,115,110</u>	<u>\$ 122,379,585</u>

See accompanying notes to the consolidated financial statements.

# Marine Corps Heritage Foundation and Affiliate

## Consolidated Statement of Functional Expenses

Year ended December 31, 2018

	Program Services				Supporting Services			
	Museum & Heritage Center	Marine Corps University History Division	Other historical support	Total Program Expenses	Fundraising	General and administrative	Total Supporting Expenses	Total Expenses
Accounting and auditing	\$ 60,893	\$ 1,156	\$ 2,971	\$ 65,020	\$ 22,249	\$ 10,933	\$ 33,182	\$ 98,202
Advertising	161,791	-	3,876	165,667	-	10,353	10,353	176,020
Awards	-	-	19,985	19,985	-	-	-	19,985
Bank charges	3,330	-	-	3,330	-	12,135	12,135	15,465
Bad debt	-	-	-	-	116,348	-	116,348	116,348
Consulting	182,127	-	-	182,127	201,583	1,805	203,388	385,515
Credit card fees	33,599	-	-	33,599	24,201	24,201	48,402	82,001
Depreciation	193,820	754	1,938	196,512	14,513	7,132	21,645	218,157
Depreciation - Heritage Center	5,144,435	-	-	5,144,435	-	-	-	5,144,435
Direct marketing	360,810	-	-	360,810	1,294,671	466,930	1,761,601	2,122,411
Dues and subscriptions	9,234	-	-	9,234	491	338	829	10,063
Educational support	126,936	-	-	126,936	-	-	-	126,936
Facilities development	65,908	-	-	65,908	-	-	-	65,908
Gifts	-	-	-	-	-	387	387	387
Insurance	91,416	-	-	91,416	-	19,440	19,440	110,856
Interest	370,188	-	-	370,188	-	-	-	370,188
Loss on disposal of assets	-	-	-	-	-	304	304	304
Maintenance	115,339	297	764	116,400	79,482	32,791	112,273	228,673
Marketing	32,610	10,973	10,973	54,556	33,252	-	33,252	87,808
Meetings	14,343	-	-	14,343	146	30,871	31,017	45,360
Museum and historical support	265,225	92,533	158,822	516,580	-	-	-	516,580
Museum expenses - LLC	27,942	-	-	27,942	-	-	-	27,942
Office expense	6,809	-	-	6,809	1,094	13,871	14,965	21,774
Postage and shipping	482	-	-	482	7,166	4,674	11,840	12,322
Printing	5,922	-	-	5,922	6,610	-	6,610	12,532
Professional fees	38,361	-	-	38,361	-	5,995	5,995	44,356
Salaries, taxes, and benefits - Foundation	682,311	31,844	81,885	796,040	629,840	321,941	951,781	1,747,821
Salaries, taxes, and benefits - Museum, History Division, and Band Support	263,081	163,533	10,896	437,510	-	-	-	437,510
Special events	4,310	-	151,842	156,152	-	-	-	156,152
Staff training	2,249	-	-	2,249	372	2,843	3,215	5,464
Taxes and licenses	38,728	-	150	38,878	16,227	4,953	21,180	60,058
Telephone and utilities	102,547	544	1,399	104,490	7,772	19,532	27,304	131,794
Temporary help	-	-	-	-	18,225	-	18,225	18,225
Travel	5,392	-	-	5,392	2,987	238	3,225	8,617
USMC Support	-	-	16,096	16,096	-	-	-	16,096
Website and internet	16,528	1,543	3,967	22,038	874	874	1,748	23,786
<b>Total</b>	<b>\$ 8,426,666</b>	<b>\$ 303,177</b>	<b>\$ 465,564</b>	<b>\$ 9,195,407</b>	<b>\$ 2,478,103</b>	<b>\$ 992,541</b>	<b>\$ 3,470,644</b>	<b>\$ 12,666,051</b>

See accompanying notes to the consolidated financial statements.

Marine Corps Heritage Foundation  
and Affiliate

Consolidated Statement of Cash Flows

December 31, 2018

**Cash flows from operating activities**

Change in net assets	\$ (1,965,657)
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation	5,362,592
Receipt of donated stock	(332,878)
Change in fair value of investments	268,648
Change in pledges allowance and discount	(270,584)
Loss on disposal of fixed assets	304
Changes in operating assets and liabilities:	
Pledges receivable	6,955,797
Accounts receivable	5,320
Deposits	9,189
Prepaid expenses	(136,557)
Retirement plan assets	(9,003)
Accounts payable and accrued expenses	(357,803)
Retirement plan liability	9,003
Construction retention payable	<u>(20,338)</u>
Net cash provided by operating activities	9,518,033

**Cash flows from investing activities**

Purchases of investments	(10,249,632)
Proceeds from sales of investments	398,703
Purchases of fixed assets	<u>(12,758)</u>
Net cash used in investing activities	(9,863,687)

**Cash flows from financing activities**

Payments on notes payable	<u>(6,861,809)</u>
Net cash used in financing activities	<u>(6,861,809)</u>

**Net change in cash and cash equivalents**

Cash and cash equivalents, beginning of year	<u>9,874,145</u>
<b>Cash and cash equivalents, end of year</b>	<u><u>\$ 2,666,682</u></u>

**Supplemental disclosures of cash flow information**

Cash paid in the year for loan interest	<u><u>\$ 370,188</u></u>
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*See accompanying notes to the consolidated financial statements.*

Marine Corps Heritage Foundation  
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Notes to Consolidated Financial Statements

Year ended December 31, 2018

**Note A - Organization and Summary of Significant Accounting Policies**

The Marine Corps Heritage Foundation (the Foundation) was established to preserve and promulgate the history, traditions and culture of the United States Marine Corps and educate all Americans in its virtues. The Foundation is registered as a non-profit organization in the Commonwealth of Virginia. In 2001, the Foundation commenced raising funds to build the Heritage Center and National Museum of the Marine Corps (the Museum) located in Triangle, Virginia. Ground was broken on Phase I construction in the spring of 2004 and the Museum opened in November 2006. Phase I of the Museum depicts USMC history from inception in 1775 through the Vietnam War.

In 2011, the Foundation initiated a second capital campaign to complete the Museum. Phase II construction was completed in 2017 and included the opening of a Combat Art Gallery, a giant screen theater, administrative office spaces, a children's activity area, and educational classrooms. The Marine Corps is currently working on exhibits for the new galleries that will honor the service of all Marines from the end of the Vietnam War to the current day. The new historical galleries, a Medal of Honor gallery, and a Sports gallery/Hall of Fame are expected to open in phases during the next few years. The cumulative value of the Heritage Center, including the Museum, is reported on the consolidated statement of financial position in assets and net assets without donor restrictions.

The Foundation provides internships and fellowships for Marine Corps historical projects, sponsors award competitions, and provides program support to the History Division of Marine Corps University and the Museum.

The consolidated financial statements include the assets, liabilities and activities of the Heritage Center LLC (the LLC). The LLC was incorporated in Virginia on June 5, 2006 as a single member LLC, with the Foundation as the member. The LLC's operating agreement with the Foundation authorizes the LLC to operate revenue-producing units in the Museum, which include the Museum Store, restaurants, event space rentals, a laser rifle range and the giant screen theater. In February 2015, the LLC outsourced its retail operations to a third party vendor. The LLC may distribute funds that were generated at the Museum to the Foundation to support the continued development of the Heritage Center and other Foundation programs. The LLC distributed to the Foundation \$215,000 in 2018, which is eliminated upon consolidation.

Marine Corps Heritage Foundation  
and Affiliate

Notes to Consolidated Financial Statements (Continued)

**Note A - Organization and Summary of Significant Accounting Policies (Continued)**

The following is a summary of significant accounting policies followed in the preparation of these consolidated financial statements:

*Principles of Consolidation*

The consolidated financial statements include the accounts of the Foundation and the LLC (collectively referred to as the Foundation). Significant intercompany accounts and transactions have been eliminated in consolidation.

*Basis of Accounting*

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), promulgated by the Financial Accounting Standards Board Accounting Standards Codification (ASC or the guidance).

*Use of Estimates*

Preparation of consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and those differences could be material.

*Subsequent Events*

The Foundation has performed an evaluation of subsequent events through April 22, 2019, which is the date the consolidated financial statements were available to be issued and has considered any relevant matters in the preparation of the consolidated financial statements and notes.

*Income Taxes*

The Foundation is exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Code and is not considered a private foundation. The Foundation is required to pay federal and state income taxes only on unrelated business income. The LLC is a disregarded entity, and is consolidated into the Foundation for tax reporting purposes. Management has concluded that the Foundation has maintained its tax exempt status and that there are no uncertain tax positions as of December 31, 2018.

Marine Corps Heritage Foundation  
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Notes to Consolidated Financial Statements (Continued)

**Note A - Organization and Summary of Significant Accounting Policies (Continued)**

*Cash and Cash Equivalents*

The Foundation considers cash and cash equivalents to include only demand deposits and savings accounts. Certificates of deposit and other short-term, highly liquid investments purchased for its portfolio are treated as investments rather than cash equivalents. The Federal Deposit Insurance Corporation (FDIC) insures amounts on deposit with each financial institution up to limits prescribed by law. The Foundation may hold funds with financial institutions in excess of the FDIC insured amounts; however, the Foundation has not experienced any losses in such accounts and management believes it is not exposed to any significant credit risk on cash and cash equivalents.

*Investments and Fair Value Measurement*

The Foundation records investment purchases at cost, or if donated, at fair value on the date of donation. Subsequent to the initial recording, investments are adjusted to fair values in the consolidated statement of financial position. Net investment return (or loss) is reported on the consolidated statement of activities and consists of interest and dividends, less external investment expenses. The change in fair value of investments, also reported on the consolidated statement of activities, includes gains and losses realized upon sales and unrealized resulting from fluctuations in market values of investments.

In accordance with GAAP, the Foundation prioritizes the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets and liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The levels of the hierarchy are as follows:

Level 1 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities traded in active markets that the Foundation has the ability to access.

Level 2 – Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the assets or liabilities for substantially the entire period and market-corroborated inputs.

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

*Risks and Uncertainties*

The Foundation invests in various securities. These securities are exposed to a variety of risks, such as interest rates, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amount reported in the consolidated financial statements.

Marine Corps Heritage Foundation  
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Notes to Consolidated Financial Statements (Continued)

**Note A - Organization and Summary of Significant Accounting Policies (Continued)**

*Fixed Assets*

Furniture and equipment are recorded at cost, less accumulated depreciation. Depreciation expense is computed using the straight-line method over the estimated life of 3-10 years. Expenditures for maintenance and repairs are expensed as incurred; betterments which increase the value or materially extend the life of the related assets are capitalized.

*Heritage Center*

The Heritage Center consists of the National Museum of the Marine Corps, Memorial Chapel, Semper Fidelis Memorial Park, Heritage Center Parkway with an overlook, and the Playground. The 2001 National Defense Authorization Act stipulates that the Heritage Center is to be transferred to the Department of the Navy once all financial obligations have been met which is currently estimated to be 2022.

These assets are depreciated on a straight-line basis over their estimated useful lives of 20 to 30 years. The Foundation capitalizes costs in accordance with the Foundation's established threshold, while expensing amounts incurred for routine repairs and maintenance.

The carrying value of the Heritage Center is periodically evaluated and adjusted for any perceived impairments in value. The amount of write-downs, if required, is charged to expense in the period the impairment is identified. Circumstances that could have a significant adverse effect on the value of the Heritage Center include a deficit in contributions necessary to maintain the property. During the year ended December 31, 2018, there were no impairments recognized.

*Construction in Progress*

Phase II costs associated with USMC post-Vietnam historical exhibit galleries, a Medal of Honor gallery, and a Sports Gallery/Hall of Fame have been capitalized and are included as construction in progress on the consolidated statement of financial position. Depreciation on the construction in progress balance will begin when the assets are available for their intended use, and when the assets are in the location and condition necessary to operate in the manner intended by the Foundation.

Marine Corps Heritage Foundation  
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Notes to Consolidated Financial Statements (Continued)

**Note A - Organization and Summary of Significant Accounting Policies (Continued)**

*Collections*

The Foundation's collections are made up of monuments located in Semper Fidelis Memorial Park and are held for public exhibition. Each of the collection items is cataloged, preserved, and cared for, and activities verifying their existence and assessing their condition are performed continuously. These collection items are considered to be a permanent collection, and the Foundation has no intention of selling these items. The contributed collections are not recognized as assets on the statement of financial position, and are valued at approximately three million dollars as of December 31, 2018. Management has evaluated their collection items to determine if any impairment adjustments are necessary, and has concluded that no impairments need to be recognized for the year ended December 31, 2018.

*Net Assets*

Net assets, revenues, gains, and losses are classified based on the existence or absence of donor imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

Net Assets Without Donor Restrictions - Net assets available for use in general operations and not subject to donor, or certain grantor, restrictions.

Net Assets With Donor Restrictions - Net assets subject to donor, or grantor, imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires. That is, when the stipulated time has elapsed, when the stipulated purpose has been fulfilled, or both.

*Functional Allocation of Expenses*

The costs of program and supporting services activities have been summarized on a functional basis in the consolidated statement of activities. The consolidated statement of functional expenses presents the natural classification detail of expenses by function. The financial statements report certain categories of expenses that are attributed to more than one program or supporting function. Therefore, expenses require allocation on a reasonable basis that is consistently applied. Expenses that can be identified with a specific program or supporting activity are allocated directly according to their natural expenditure classification. Advertising and direct marketing costs are allocated based on a joint costs allocation, as the costs of producing these mailings is not directly attributable to any single function. Other expenses such as salaries, taxes, benefits, depreciation not related to the Museum and Heritage Center, professional services, office expenses, information technology, insurance, and others are allocated on the basis of estimates of time and effort.

Marine Corps Heritage Foundation  
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Notes to Consolidated Financial Statements (Continued)

**Note A - Organization and Summary of Significant Accounting Policies (Continued)**

*Contributions*

Contributions and pledges are recorded when the donor makes a contribution or promise to give to the Foundation that is, in substance, unconditional. Foundation-owned life insurance policies are recorded as contributions when received and are carried at their cash surrender value.

*Pledges Receivable*

Pledges receivable that are expected to be collected within one year are reported net of any estimated uncollectible amounts. Pledges receivable that are due beyond one year are carried at the estimated present value of the future receipts based on their perceived collectability and aged outstanding balance and have been discounted using rates which range from .17% to 2.51%.

*Allowance for Uncollectible Pledges*

The Foundation has established an allowance for uncollectible pledges. Although variability is inherent in such estimates, management believes that the allowance provided in the consolidated financial statements is adequate, but largely dependent on economic conditions. When all collection efforts have been exhausted, uncollectible pledged receivables are written off as bad debt expense.

*Notes Payable*

Fair value approximates carrying value, due to the interest rate pricing on notes payable. See Note I for information on the notes payable.

*Reclassifications*

During 2018, the Foundation reclassified \$483,990 from net assets without donor restrictions to net assets with donor restrictions, based on the clarification of a donor's pledge agreement. This reclassification is included in the consolidated statement of activities, and had no effect on the total consolidated change in net assets or total consolidated net assets.

*Change in Accounting Principle*

On August 18, 2016, the Financial Accounting Standards Board (FASB) issued ASU 2016-14 *Not for Profit Entities (topic 958) Presentation of Financial Statements of Not-for-Profit-Entities*. The amendments in this update are designed to improve the net asset classification requirements and the information presented in financial statements and notes about a not-for-profit entity's liquidity, financial performance and cash flows. The amendments in the ASU are effective for annual periods beginning after December 15, 2017. Management adopted the provisions of this ASU as of, and for the year ended December 31, 2018.

Marine Corps Heritage Foundation  
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Notes to Consolidated Financial Statements (Continued)

**Note A - Organization and Summary of Significant Accounting Policies (Continued)**

*Change in Accounting Principle (continued)*

In accordance with the standard, the “placed in service” approach should be used to report expirations of restrictions on gifts of long-lived assets and cash or other assets used to acquire or construct long-lived assets, absent explicit donor stipulations. Given this, the cumulative value of the Heritage Center was reclassified from net assets with donor restrictions to net assets without donor restrictions in the amount of \$74,104,293, effective January 1, 2018.

The adoption of the ASU did not have an effect on the total net assets reported in the consolidated financial statements. However, wording used in financial statement descriptions has been updated, net asset classifications have been renamed and footnote disclosures including disclosures about liquidity and availability of resources have been enhanced.

*Recent Accounting Pronouncements*

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (topic 606). The core principle of ASU 2014-09 is to recognize revenue when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity is expected to be entitled for those goods or services. The amendments in the ASU are effective for annual periods beginning after December 15, 2018 using either of two methods: (1) retrospective to each prior reporting period presented with the option to elect certain practical expedients as defined with the ASU; or (2) retrospective with the cumulative effect of initial adoption recognized at the date of initial application. Management has not yet selected a transition method and is currently evaluating the effects that the ASU will have on the consolidated financial statements.

In June 2018, the FASB issued ASU 2018-08, Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made, (topic 958). The ASU clarifies when the transfer of an asset or the extinguishment of a liability (the transaction) meets the definition of an exchange transaction or a contribution. When the transaction is an exchange transaction, an entity must apply Topic 606, *Revenue from Contracts with Customers* or other applicable Topics. When the transaction is a contribution, the ASU clarifies when the contribution is conditional and when revenue should be recognized. The amendments in the ASU are effective for annual periods beginning after December 15, 2018 for contributions received and effective for fiscal years beginning after December 15, 2019 for contributions made. Early adoption is permitted. The amendments should be applied on a modified prospective basis. However, retrospective application is permitted. Management is evaluating the impact the amendments in this ASU will have on the consolidated financial statements.

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Notes to Consolidated Financial Statements (Continued)

**Note B - Liquidity and Availability of Resources**

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the date of the consolidated statement of financial position are comprised of the following:

	December 31, <u>2018</u>
Cash and cash equivalents	\$ 2,574,100
Investments	6,902,439
Accounts receivable	286,748
Pledges receivable	<u>1,386,944</u>
	<u>\$ 11,150,231</u>

The Foundation is substantially supported by contributions with no donor restrictions; however, restricted gifts are occasionally received. Because a donor's restriction requires resources to be used for a particular purpose or during a specified time, the Foundation must maintain sufficient resources to meet those responsibilities to its donors. As a result, not all financial assets will be available for expenditure within one year. The Foundation's management keeps detailed records to monitor restricted contributions and tracks when they would be available for general expenditures.

As part of the Foundation's liquidity management plan, the Foundation invests cash in excess of monthly requirements in short-term investments, CDs, and money market funds. Lines of credit may also be utilized when needed to fund construction efforts at the Museum and Heritage Center. Additionally, the Foundation has accounts and pledges receivable that are due within one year. A portion of the pledges receivable balance listed on the consolidated statement of financial position serves as collateral for the Foundation's loan agreement with Navy Federal Credit Union. The pledges receivable balance in the above liquidity analysis includes amounts that will be used to repay loan principal and interest amounts within one year of the date of the consolidated statement of financial position.

The Foundation structures its financial assets to be available when operating expenditures, liabilities and other obligations become due. The Foundation has evaluated its general expenditures for the next fiscal year and has determined that certain donor restrictions are for purposes related to the regular, ongoing programs and activities of the Foundation. Therefore, certain donor restricted financial assets are considered available for general expenditure and are included in the above analysis.

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Notes to Consolidated Financial Statements (Continued)

**Note B - Liquidity and Availability of Resources (Continued)**

The endowment funds consist of donor-restricted permanent endowments which are not available for general expenditure. Income from donor-restricted endowments is restricted for specific purposes, unless the donor stipulates that income may be used for general expenditure. There are no board designated endowment funds, or any other self-imposed limits set aside by the board.

**Note C - Pledges Receivable**

Pledges receivable consist of the following in 2018:

Amounts due in:

Less than one year	\$ 1,386,944
One to five years	5,009,764
More than five years	<u>689,200</u>
Total pledges	7,085,908
Less allowance and discount	<u>(571,823)</u>
Pledges net of allowance and discount	<u><u>\$ 6,514,085</u></u>

As of December 31, 2018, approximately 9.1% of the total pledges receivable represents amounts from current Foundation Board members.

**Note D - Investments and Fair Value Measurements**

The following table is a summary of the Foundation's investments measured at fair value within the GAAP fair value hierarchy at December 31:

<u>Class of Security</u>	<u>December 31, 2018</u>	<u>Fair Value Level</u>
Mutual funds	\$ 2,162,993	Level 1
Exchange traded funds	<u>1,590,678</u>	Level 1
Total investments in hierarchy	3,753,671	
Certificates of deposit	10,799,046	
Hedge funds	<u>100,063</u>	
Total investments held at fair value	<u><u>\$ 14,652,780</u></u>	

The certificates of deposit held by the Foundation are included within the investment balance on the consolidated statement of financial position. They do not meet the definition of securities under accounting standards and thus are not subject to the fair value disclosure requirements of GAAP. The Foundation's mutual funds and exchange traded funds are valued based on quoted market prices in active markets and therefore classified as Level 1 securities in accordance with GAAP.

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Notes to Consolidated Financial Statements (Continued)

**Note D - Investments and Fair Value Measurements (Continued)**

The Foundation's alternative investments consist primarily of two hedge funds (Funds), whose values are derived from the Fund's net asset value. The Foundation may redeem some or all of its shares in the Funds as of the last business day of any calendar quarter. Written notice to redeem all or part of its capital interest must be received by the Funds at least sixty days prior to the date of redemption. Redemptions can be done in increments of \$10,000, provided that the greater of \$50,000 or twenty percent of the Foundation's initial investment remains in the Funds.

Investments in the hedge funds are typically valued, as a practical expedient, utilizing the net asset valuations provided by the underlying private investment companies and or their administrators, without adjustment, when the net asset valuations of the investments are calculated in a manner consistent with GAAP for investment companies. In accordance with GAAP, the Funds, which are measured at fair value using the net asset value per share (or equivalent) as a practical expedient, have not been classified in the fair value hierarchy.

Retirement plan assets totaling \$331,354 at December 31, 2018 consist of pooled separate accounts, which are measured at fair value using the net asset value per share (or equivalent) as a practical expedient, and have not been classified in the fair value hierarchy.

The Foundation is aware of various split-interest agreements from donors where the Foundation may be listed as the beneficiary of future benefits. The Foundation is not able to obtain sufficient information for the determination of the related assets, liabilities, revenues, and changes in the fair value of the split-interest agreements over the term of the agreements. Accordingly, these are not recognized in the consolidated financial statements for the year ended December 31, 2018.

**Note E - Fixed Assets**

Fixed assets of the Foundation consist of the following at December 31:

	December 31, 2018
Equipment and software	\$ 2,257,208
Furniture and fixtures	285,224
	2,542,432
Accumulated depreciation	(1,568,354)
Fixed assets, net	<u>\$ 974,078</u>

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Notes to Consolidated Financial Statements (Continued)

**Note F - Heritage Center**

The Heritage Center consists of the following at December 31:

	December 31, 2018
National Museum USMC	\$ 87,768,385
NMMC Theater	15,012,854
Semper Fidelis Memorial park	7,718,903
Memorial chapel	5,874,122
Heritage Center parkway overlook	2,347,504
Heritage Center parkway	1,874,592
Playground	<u>497,137</u>
	121,093,497
Accumulated depreciation	<u>(40,089,657)</u>
Heritage Center, net	<u><u>\$ 81,003,840</u></u>

**Note G - Net Assets With Donor Restrictions**

Net assets with donor restrictions are restricted for the following purposes or periods:

	December 31, 2018
Subject to expenditure for specified purpose	
Educational programs	\$ 1,000,000
Awards	8,709
Support Programs	<u>79,470</u>
	1,088,179
Endowments to be held in perpetuity	
Grants and fellowships	423,598
Educational programs	<u>100,000</u>
	523,598
Subject to endowment spending policy and appropriation:	
Grants and fellowships	<u>503,333</u>
	<u><u>\$ 2,115,110</u></u>

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Notes to Consolidated Financial Statements (Continued)

**Note G - Net Assets With Donor Restrictions (Continued)**

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purpose as follows for the year ended December 31:

	December 31, 2018
Satisfaction of purpose restrictions:	
Awards	\$ 155,871
Support programs	40,254
Grants and Fellowships	16,736
Education	1,972
	<u>\$ 214,833</u>

**Note H - Endowment**

The Foundation's endowment consists of three individual donor-restricted funds established to support grants and fellowships, and educational programs. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

*Interpretation of Relevant Law*

The Foundation has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gifts as of the date of the donor restricted endowment funds, unless there are explicit donor stipulations to the contrary. At December 31, 2018, there were no such donor stipulations. As a result of this interpretation, the Foundation retains in perpetuity (a) the original value of the initial and subsequent gift amounts donated to the endowment fund (including promises to give net of discount and allowance for uncollectible amounts) and (b) any accumulations to the endowment that are required to be maintained in perpetuity. Donor restricted amounts not retained in perpetuity are subject to appropriation for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by UPMIFA.

The Foundation considers the following factors in making a determination to appropriate or accumulate donor restricted endowment funds:

- The duration and preservation of the fund
- The purpose of the Foundation and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Foundation
- The investment policies of the Foundation

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Notes to Consolidated Financial Statements (Continued)

**Note H - Endowment (Continued)**

As of December 31, 2018, the Foundation had the following endowment net asset composition by type of fund:

With Donor Restrictions		
Original donor-restricted gift amounts required to be maintained in perpetuity:		
Grants and fellowships	\$	423,598
Educational programs		100,000
		523,598
Accumulated earnings from endowment:		
Grants and fellowships		503,333
	\$	1,026,931

From time to time, certain donor-restricted endowment funds may have fair values less than the amount required to be maintained by donors or by law (underwater endowments). The Foundation has interpreted UPMIFA to permit spending from underwater endowments in accordance with prudent measures required under law. At December 31, 2018, funds with original gift values of \$523,598 had a fair value of of \$1,026,931. There were no deficiencies in donor-restricted endowment funds as of December 31, 2018, and thus, there has been no action taken by the Foundation during 2018 concerning appropriation from underwater endowment funds.

*Investment and Spending Policies*

The Foundation practices investment and spending policies for endowment assets that attempt to provide a predictable stream of funding for programs supported by its endowment while seeking to maintain the original endowment gift. Endowment assets include donor-restricted gifts that the Foundation must hold in perpetuity. The Foundation expects its endowment funds to provide a moderate rate of return over time. The Foundation uses a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized market gains) and current income through interest and dividends. The Foundation utilizes diversified asset allocations in order to achieve its long-term investment objectives within prudent risk management constraints. The Foundation withdraws donor-restricted endowment funds annually in an amount sufficient to cover the previous year's qualifying program expenses incurred.

Changes in endowment net assets for the year ended December 31, 2018 are as follows:

With Donor Restrictions		
Endowment net assets, beginning of year	\$	1,022,456
Investment return, net		12,234
Expenditure appropriations		(7,759)
Endowment net assets December 31, 2018	\$	1,026,931

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Notes to Consolidated Financial Statements (Continued)

**Note I - Notes Payable**

The Foundation entered into a line of credit agreement with Navy Federal Credit Union on April 13, 2015, which allowed borrowing up to \$20,000,000 for use in the construction expansion of the National Museum of the Marine Corps. The line of credit was converted to a term loan totaling \$14,309,045 on April 13, 2017 and matures on May 1, 2022. Loan principal payments amounted to \$6,861,809 for the year ended December 31, 2018.

Interest accrued on the unpaid principal balance of this loan at the rate of 4.00% until April 13, 2017. After that time, interest accrued on the unpaid balance at a rate of 3.50%, which will continue to be accrued until paid in full. During the year ended December 31, 2018, total interest costs incurred amounted to \$370,188. Interest was expensed as incurred during 2018.

**Note J - Retirement Plans**

The Foundation provides a salary deferral arrangement which is qualified under Section 403(b) of the Internal Revenue Code. Employees may begin making elective contributions upon reaching age 21. The Foundation begins matching 50% of the amount deferred by participants after employees complete 90 days of service. Benefits expense for the year ended December 31, 2018 was \$86,847.

The Foundation also sponsors a deferred compensation plan under IRC Section 457(b). Eligible employees may elect to have amounts, subject to statutory limits which are annually adjusted, withheld from their compensation and contributed to funds established for the employees' benefit. Deferred compensation assets held by the Foundation under the plan for which the employees are 100% vested total \$331,354 for the year ended December 31, 2018. The consolidated statement of financial position reflects an asset and corresponding liability for this retirement plan.

**Note K - Commitments**

*Retail Operating Agreement*

The Foundation entered into a lease and operating agreement with a third party provider (Provider) to conduct museum gift shop operations beginning February 2015. The agreement is for an initial term of six years with the ability to renew for an additional five-year term.

The agreement stipulates that the Provider will pay both a fixed and variable rent. The fixed rental income, referred to as the base rent is \$3,452 per month for the right to use the premises for purposes of retail concessions. The variable rental income is based on a percentage of gross receipts of sales on a three tiered basis, excluding any sales taxes, returns and other items as designated per the contract. The three tiers are: 15% of gross receipts up to \$2,000,000; 20% of gross receipts between \$2,000,000 and \$2,500,000; and 25% of gross receipts greater than \$2,500,000. Lastly, the Provider is to make a capital investment between \$80,000 and \$100,000 for improvements to the retail premises within the initial term of the agreement and between \$50,000 and \$75,000 within the first 24 months of the renewal term.

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Notes to Consolidated Financial Statements (Continued)

**Note K - Commitments (Continued)**

The agreement contains a clause that requires the Foundation to purchase directly from the third party provider any branded inventory that is not saleable should the agreement be terminated. As of December 31, 2018, the Foundation has no intentions to terminate the agreement.

**Note L - Allocation of Joint Costs of Direct Mailings**

The Foundation produces mailings that include programmatic and administrative information, together, with a request for contributions in support of the Foundation's mission. The cost of producing these mailings is not directly attributable to any single function. In 2018, the Foundation incurred joint costs of \$2,122,411 for informational materials and activities that included fundraising appeals. Of these costs, \$360,810 were allocated to program services, \$1,294,671 and \$466,930 were allocated to fundraising and general and administrative, respectively.

**Note M - Related Party Transactions**

The consolidated statement of financial position includes \$645,296 in outstanding pledges receivable as of December 31, 2018, from members of the Foundation's Board of Directors. There was no revenue recognized from these members in 2018.

**Note N - In-Kind Support**

In-kind support received by the Foundation is recorded at fair value and is reflected in the consolidated statement of activities as in-kind support and within each of the functional expense categories benefited (general and administrative, fundraising and program). Total in-kind support consisted of the following for the year ended December 31, 2018:

Without donor restrictions:

Legal services	\$	25,269
Investment management		40,376
USMC historical research materials		<u>5,386</u>
Total without donor restrictions		71,031

With donor restrictions:

Google grant award for advertising		10,232
Awards banquet		<u>6,000</u>
Total with donor restrictions		<u>16,232</u>

Total in-kind goods and services	\$	<u><u>87,263</u></u>
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Consolidating Statement of Financial Position

	December 31, 2018			
	Foundation	Heritage Center, LLC	Reclassifications & Eliminations	Total
<b>Assets</b>				
Cash and cash equivalents	\$ 2,574,100	\$ 92,582	\$ -	\$ 2,666,682
Investments	14,652,780	-	-	14,652,780
Investment in LLC	944,435	-	(944,435)	-
Accounts receivable	279,581	62,066	-	341,647
Pledges receivable, net	6,514,085	-	-	6,514,085
Due (to) from Foundation	-	(7,167)	7,167	-
Prepaid expenses	197,477	1,058	-	198,535
Heritage Center, net	81,003,840	-	-	81,003,840
Construction in progress	23,792,558	-	-	23,792,558
Fixed assets, net	119,301	854,777	-	974,078
Cash surrender value of life insurance policies	138,104	-	-	138,104
Retirement plan assets	331,354	-	-	331,354
Total assets	<u>\$ 130,547,615</u>	<u>\$ 1,003,316</u>	<u>\$ (937,268)</u>	<u>\$ 130,613,663</u>
<b>Liabilities and net assets</b>				
Liabilities:				
Accounts payable and accrued expenses	\$ 396,607	\$ 58,881	\$ -	\$ 455,488
Due to (from) LLC	(7,167)	-	7,167	-
Notes payable	7,447,236	-	-	7,447,236
Retirement plan liabilities	331,354	-	-	331,354
Total liabilities	8,168,030	58,881	7,167	8,234,078
Net assets:				
Without donor restrictions	120,264,475	944,435	(944,435)	120,264,475
With donor restrictions	2,115,110	-	-	2,115,110
Total net assets	<u>122,379,585</u>	<u>944,435</u>	<u>(944,435)</u>	<u>122,379,585</u>
Total liabilities and net assets	<u>\$ 130,547,615</u>	<u>\$ 1,003,316</u>	<u>\$ (937,268)</u>	<u>\$ 130,613,663</u>

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Consolidating Statement of Activities

	Year ended December 31, 2018					
	Foundation: Without Donor Restrictions	Foundation: With Donor Restrictions	Foundation Total	Heritage Center, LLC	Reclassifications & Eliminations	Total
<b>Revenues, gains and other support</b>						
Contributions	\$ 9,471,478	\$ 265,385	\$ 9,736,863	\$ 25,030	\$ -	\$ 9,761,893
Museum gift shop income	-	-	-	338,451	-	338,451
Theater/rifle range revenue	-	-	-	218,797	-	218,797
Other revenue	6,851	-	6,851	175,237	-	182,088
Special events	-	-	-	184,187	-	184,187
In-kind support	71,031	16,232	87,263	-	-	87,263
Investment income, net	166,363	29,360	195,723	640	-	196,363
Net assets released from restrictions	214,833	(214,833)	-	-	-	-
Total revenue, gains, and other support	9,930,556	96,144	10,026,700	942,342	-	10,969,042
<b>Expenses</b>						
Program services:						
Museum & Heritage Center	7,497,611	-	7,497,611	929,055	-	8,426,666
Marine Corps University History Division	303,177	-	303,177	-	-	303,177
Other historical support	465,564	-	465,564	-	-	465,564
Total program services	8,266,352	-	8,266,352	929,055	-	9,195,407
Supporting services:						
Fundraising	2,478,103	-	2,478,103	-	-	2,478,103
General and administrative	992,541	-	992,541	-	-	992,541
Total supporting services	3,470,644	-	3,470,644	-	-	3,470,644
Total expenses	11,736,996	-	11,736,996	929,055	-	12,666,051
Change in net assets, before change in fair value of investments and LLC distribution	(1,806,440)	96,144	(1,710,296)	13,287	-	(1,697,009)
Change in fair value of investments	(251,550)	(17,098)	(268,648)	-	-	(268,648)
LLC net loss	(201,713)	-	(201,713)	-	201,713	-
Change in net assets before distribution	(2,259,703)	79,046	(2,180,657)	13,287	201,713	(1,965,657)
LLC distribution	215,000	-	215,000	(215,000)	-	-
Change in net assets	(2,044,703)	79,046	(1,965,657)	(201,713)	201,713	(1,965,657)
Reclassifications of net assets	(483,990)	483,990	-	-	-	-
Net assets, beginning of year	48,688,875	75,656,367	124,345,242	1,146,148	(1,146,148)	124,345,242
Adoption of ASU 2016-14	74,104,293	(74,104,293)	-	-	-	-
Net assets, end of year	<u>\$ 120,264,475</u>	<u>\$ 2,115,110</u>	<u>\$ 122,379,585</u>	<u>\$ 944,435</u>	<u>\$ (944,435)</u>	<u>\$ 122,379,585</u>