

PACIFIC BATTLESHIP CENTER

Financial Statements
December 31, 2014 and 2013
(With Independent Auditor's Report Thereon)

PACIFIC BATTLESHIP CENTER

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Independent Auditor's Report

The Board of Directors
Pacific Battleship Center
San Pedro, California

We have audited the accompanying financial statements of Pacific Battleship Center (PBC) (a not-for-profit organization), which comprise the statements of financial position as of December 31, 2014 and 2013, and the related statements of activities and cash flows for the years 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 audits. We conducted our audits 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 of 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 PBC'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 PBC's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Pacific Battleship Center as of December 31, 2014 and 2013, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Macias Gini E' O'Connell CPA

June 29, 2015
Newport Beach, California

Pacific Battleship Center
Statements of Financial Position
December 31, 2014 and 2013

Assets	2014	2013
Cash	\$ 564,467	\$ 484,742
Accounts receivable	47,014	62,753
Contributions receivable	767,500	1,007,000
Engineering/machine shop materials	50,518	50,708
Deposits and prepaid insurance	69,411	64,391
Property and equipment, net	<u>4,724,517</u>	<u>4,760,786</u>
Total assets	<u><u>\$ 6,223,427</u></u>	<u><u>\$ 6,430,380</u></u>
Liabilities and Net Assets		
Liabilities:		
Accounts payable	\$ 259,928	\$ 80,185
Accrued and other liabilities	227,682	170,385
Line of credit	80,000	-
Capital lease obligations	32,088	118,832
Loan and notes payable	<u>1,365,590</u>	<u>1,533,243</u>
Total liabilities	<u>1,965,288</u>	<u>1,902,645</u>
Net Assets:		
Unrestricted	3,301,673	3,491,649
Temporarily restricted	<u>956,466</u>	<u>1,036,086</u>
Total net assets	<u>4,258,139</u>	<u>4,527,735</u>
Total liabilities and net assets	<u><u>\$ 6,223,427</u></u>	<u><u>\$ 6,430,380</u></u>

See accompanying notes to financial statements.

Pacific Battleship Center
Statement of Activities
Year ended December 31, 2014

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Total</u>
Revenues and other support:			
Admissions	\$ 2,068,203	\$ -	\$ 2,068,203
Contributions	193,359	363,476	556,835
Donated goods and services	272,083	-	272,083
Commissions	331,374	-	331,374
Other income	144,133	-	144,133
Total revenues	<u>3,009,152</u>	<u>363,476</u>	<u>3,372,628</u>
Net assets released from restriction	443,096	(443,096)	-
Total revenues and other support	<u>3,452,248</u>	<u>(79,620)</u>	<u>3,372,628</u>
Expenses:			
Program services (including \$152,434 of donated services)	2,266,171	-	2,266,171
General and administrative	699,548	-	699,548
Fundraising	161,475	-	161,475
Subtotal expenses	<u>3,127,194</u>	<u>-</u>	<u>3,127,194</u>
Change in net assets, before depreciation	325,054	(79,620)	245,434
Depreciation	(515,030)	-	(515,030)
Change in net assets	(189,976)	(79,620)	(269,596)
Net assets, beginning of year	<u>3,491,649</u>	<u>1,036,086</u>	<u>4,527,735</u>
Net assets, end of year	<u>\$ 3,301,673</u>	<u>\$ 956,466</u>	<u>\$ 4,258,139</u>

See accompanying notes to financial statements.

Pacific Battleship Center
Statement of Activities
Year ended December 31, 2013

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Total</u>
Revenues and other support:			
Admissions	\$ 2,812,376	\$ -	\$ 2,812,376
Contributions	574,663	65,100	639,763
Donated goods and services	610,804	-	610,804
Commissions	421,074	-	421,074
Other income	262,484	-	262,484
Total revenues	4,681,401	65,100	4,746,501
Net assets released from restriction	529,014	(529,014)	-
Total revenues and other support	5,210,415	(463,914)	4,746,501
Expenses:			
Program services (including \$93,265 of donated services)	2,810,009	-	2,810,009
General and administrative	497,486	-	497,486
Fundraising	196,830	-	196,830
Subtotal expenses	3,504,325	-	3,504,325
Change in net assets, before depreciation	1,706,090	(463,914)	1,242,176
Depreciation	(480,660)	-	(480,660)
Change in net assets	1,225,430	(463,914)	761,516
Net assets, beginning of year	2,266,219	1,500,000	3,766,219
Net assets, end of year	<u>\$ 3,491,649</u>	<u>\$ 1,036,086</u>	<u>\$ 4,527,735</u>

See accompanying notes to financial statements.

Pacific Battleship Center
Statements of Cash Flows
Years ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Cash flows provided by operating activities:		
Change in net assets	\$ (269,596)	\$ 761,516
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	515,030	480,660
Forgiveness of pre-opening vendor payables	-	(259,223)
Contributed property and equipment	(119,649)	(517,539)
Change in assets and liabilities:		
Accounts receivable	15,739	18,189
Contributions receivable	239,500	493,000
Engineering/machine shop materials	190	178,269
Deposits and prepaid insurance	(5,020)	(56,057)
Accounts payable	101,366	(405,311)
Accrued and other liabilities	57,297	83,286
Cash provided by operating activities	<u>534,857</u>	<u>776,790</u>
Cash flows from investing activities:		
Purchases of property and equipment	<u>(280,735)</u>	<u>(147,275)</u>
Cash used in investing activities	<u>(280,735)</u>	<u>(147,275)</u>
Cash flows from financing activities:		
Proceeds from issuance of line of credit	80,000	-
Principal repayments on notes payable	(167,653)	(79,870)
Payments on capital lease obligations	<u>(86,744)</u>	<u>(187,804)</u>
Cash used in financing activities	<u>(174,397)</u>	<u>(267,674)</u>
Net increase in cash and cash equivalents	79,725	361,841
Cash, beginning of year	<u>484,742</u>	<u>122,901</u>
Cash, end of year	<u><u>564,467</u></u>	<u><u>484,742</u></u>
<u>Non-cash investing and financing activities:</u>		
Additions to fixed assets in accounts payable	\$ 78,377	\$ -
Conversion of pre-opening vendor payable to note payable	-	(728,279)
Supplemental Disclosure of Cash Flow Information:		
Cash paid during the year for interest	\$ 44,575	\$ -

See accompanying notes to financial statements.

PACIFIC BATTLESHIP CENTER

Notes to Financial Statements

December 31, 2014 and 2013

(1) Organization

The Pacific Battleship Center (PBC or Organization) is a California not-for-profit corporation, with a mission to:

- celebrate the American spirit through the preservation and interpretation of the Battleship USS Iowa,
- educate the public on the accomplishments and sacrifices of American patriots, and
- engage guests in unique and exciting ways that bring the ship to life by connecting the past with the future.

The PBC accomplishes this through the operation of a museum of naval history aboard the former Battleship USS Iowa (BB-61), which is moored in the Port of Los Angeles. Following ship restoration and pre-opening preparation, the ship was opened to the public in July 2012.

The PBC leases from the City of Los Angeles, through its Board of Harbor Commissioners, the pier where the USS Iowa is moored. In accordance with accounting principles generally accepted in the United States of America, the fair value of the use of the pier in excess of the amounts paid is to be reflected on the Organization's financial statements. The fair value of the lease may be in excess of the amounts paid under the agreement. However, since no objective basis is available to measure the related value, no amounts have been reflected in the financial statements for the use of the premises.

The United States Navy has allowed PBC to use the USS Iowa as a maritime museum. In accordance with accounting principles generally accepted in the United States of America, the fair value of the use of the USS Iowa is to be reflected on the PBC's financial statements. However, since no objective basis is available to measure the related value, no amounts have been recorded in the financial statements for the use of the ship.

(2) Summary of Significant Accounting Policies

(a) Basis of presentation

The financial statements are prepared on the accrual basis of accounting in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 958 *Presentation of Financial Statements – Not-for-Profit Entities*. The assets, liabilities, and net assets of the PBC are reported within categories as follows:

Unrestricted net assets – Net assets not subject to donor imposed stipulations.

Temporarily restricted net assets – Net assets subject to donor imposed stipulations that will be met by actions of the PBC and/or the passage of time. When a donor stipulated time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restriction.

PACIFIC BATTLESHIP CENTER
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

Permanently restricted net assets – Net assets subject to donor imposed stipulations requiring that they be maintained permanently by the PBC. The income from these assets is available for either general operations or specific programs as specified by the donor. The PBC did not have any permanently restricted net assets as of December 31, 2014 or 2013.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets (i.e., the donor stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

(b) Cash

The PBC considers all highly liquid instruments purchased with an original maturity of three months or less to be cash and cash equivalents. The PBC maintains its cash in one financial institution. The accounts maintained in the institution are guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. The PBC's cash balance exceeded FDIC limits by \$362,700 at December 31, 2014. The PBC has not experienced any losses on these accounts and does not believe it is exposed to any significant risk.

(c) Contributions receivable

Unconditional promises to give are recorded as contributions receivable. The PBC discounts contributions that are expected to be collected after one year at a rate commensurate with the risk involved. Amortization of the discount is recorded as additional contribution revenue.

(d) Engineering/machine shop materials

When the PBC took possession of the USS Iowa, it contained excess quantities of various metals, such as aluminum, brass and steel. It is anticipated these materials will be consumed in the repair and maintenance of the ship. The fair value is estimated based on current retail prices, and has been recorded as engineering/machine shop materials in the accompanying financial statements.

In addition, the ship included wooden decking, the majority of which consisted of teak wood. However, unlike the metals, this wood is not in excess of the ship's needs, and has not been recorded in the accompanying financial statements.

PACIFIC BATTLESHIP CENTER
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

(e) *Deposits and prepaid insurance*

The PBC has entered into a financing arrangement for annual insurance premiums. After down payments paid during 2014 and 2013, the PBC has an obligation to pay \$46,126 and \$45,800 as of December 31, 2014 and 2013, respectively, and is recorded as accrued and other liabilities in the accompanying financial statements. The financed asset amounts as of December 31, 2014 and 2013 of \$57,390 and \$55,747, respectively, is included in deposits and prepaid insurance in the accompanying financial statements, and will be amortized over the next year.

(f) *Property and equipment*

Property and equipment are carried at cost at date of purchase or fair value at date of donation, net of accumulated depreciation.

Depreciation is provided using the straight-line method over the estimated useful lives of the assets. Ship restoration and improvements and furniture and equipment are depreciated over 10 years. The costs of normal maintenance and repairs and minor replacements are charged to expense when incurred.

(g) *Fair value of financial instruments*

The carrying amounts of cash, contribution receivable, accounts payable and accrued and other liabilities at December 31, 2014 and 2013, approximate fair value because of the short term maturity of these financial instruments.

(h) *Commissions*

The PBC generates commission revenue from the operation of its gift shop and its photo booth, both of which are operated by third parties in 2013. In 2014, the photo booth services were brought in-house. In addition, the PBC also generates smaller amounts of commission revenue from event catering, food concessions, soft drink machines and ATM machines.

(i) *Tax exempt status*

The PBC is tax exempt under Section 501(c)(3) of the Internal Revenue Code and Section 23701d of the Revenue and Taxation Code of the State of California and, generally, is subject to state and federal income taxes on any net income that is derived from a trade or business, regularly carried on, and not in furtherance of the purpose for which the PBC was granted exemption. No income tax provision has been recorded as net income, from unrelated trade or business because, in the opinion of management, it is not material to the financial statements taken as a whole.

PACIFIC BATTLESHIP CENTER
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

(j) Uncertainty in income taxes

The PBC has evaluated the financial statement impact of tax positions taken or expected to be taken in its tax returns. The PBC has reviewed its positions for all open tax years and has determined that no provision for income taxes is required. The PBC is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. The PBC believes it is no longer subject to income tax examinations for years prior to 2009.

(k) Donated goods and services

In 2014 and 2013, the PBC received donated goods and services of \$272,083 and \$610,804, respectively, which are reflected in the accompanying statement of activities at their estimated fair values at the date of receipt as donated goods and services revenue. Contributions of services are recognized if the services create or enhance nonfinancial assets or require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. Donated goods and services received for the years ended December 31, 2014 and 2013 are as follows:

	<u>2014</u>	<u>2013</u>
Capitalized donated services for sewer installation (see Note 3)	\$ -	\$ 254,625
Capitalized equipment	119,649	262,914
Donated program services	<u>152,434</u>	<u>93,265</u>
Total donated goods and services	<u>\$ 272,083</u>	<u>\$ 610,804</u>

The PBC also has community volunteers that provide their services through oversight and hands-on participation in the PBC's activities. Such contributed services have not been recognized in the accompanying financial statements as they do not require specialized skills.

(l) Advertising

The PBC uses advertising to promote its programs among the audiences it serves. All advertising costs are expensed as incurred. Total advertising costs for the years ended December 31, 2014 and 2013 were \$180,451 and \$105,896, respectively.

PACIFIC BATTLESHIP CENTER
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

(m) Functional allocation of expenses

The costs for providing various program services, general administrative services, and fundraising expenses, have been summarized on a functional basis, excluding depreciation, in the statements of activities. Program related expenses are tracked on a time entry system and reviewed and allocated regularly, and those costs not directly associated with program services are allocated to general administration expenses. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

(n) Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(o) Reclassifications

Certain 2013 information has been reclassified to conform with 2014 presentation.

(3) Property and equipment

Property and equipment are summarized as follows at December 31, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Furniture and equipment	\$ 2,010,343	\$ 1,541,964
Sewer installation	254,625	254,625
Ship restoration and improvement	<u>3,675,681</u>	<u>3,665,281</u>
Subtotal capital assets	5,940,649	5,461,870
Accumulated depreciation	<u>(1,216,132)</u>	<u>(701,084)</u>
Total property and equipment, net	<u>\$ 4,724,517</u>	<u>\$ 4,760,786</u>

Depreciation expense was \$515,030 and \$480,660 for the years ended December 31, 2014 and 2013, respectively. During 2013, the PBC installed a land-based, pier-side sewer system, but it was not placed in service until December 2014, and therefore depreciation was not recorded for the year ended December 31, 2013. Additional construction was needed before the Overnight Program could commence and the sewer placed into service. This included work on-board the ship to link the sewer system to the pier-side system, and installation of fire sprinkler and fire safety systems.

PACIFIC BATTLESHIP CENTER
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

(4) Contributions receivable

Contributions receivable at December 31, 2014 and 2013, respectively, are expected to be received as follows:

	<u>2014</u>	<u>2013</u>
Within one year	\$ 267,500	\$ 257,000
Within one to five years	500,000	750,000
Total contributions receivable	<u>\$ 767,500</u>	<u>\$ 1,007,000</u>

The amounts due from one donor represent 98% and 99% of the contributions receivable at December 31, 2014 and 2013, respectively.

(5) Capital lease obligations

Following is a summary of equipment held under capital lease at December 31, 2014 and 2013, respectively:

	<u>2014</u>	<u>2013</u>
Ticketing booth	\$ 32,088	\$ 61,369
400KW Caterpillar generator	-	48,618
Forklift	-	8,845
	<u>\$ 32,088</u>	<u>\$ 118,832</u>

Future minimum lease payments under capital lease obligations as of December 31, 2014, are as follows:

<u>Year ending December 31,</u>	
2015	\$ 30,101
2016	<u>2,880</u>
Total future minimum lease payments	32,981
Less amount representing interest	<u>(893)</u>
Present value of future minimum lease payments	<u>\$ 32,088</u>

PACIFIC BATTLESHIP CENTER
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

(6) Commitments

(a) The PBC leases the pier where the USS Iowa is moored from the City of Los Angeles, through its Board of Harbor Commissioners. The PBC leases the pier under an agreement that requires PBC to pay monthly rent based on the greater of a) a fixed-minimum monthly rental, or b) an amount equal to a percentage of admission, commission and other income arising from any business, use or operation occurring on the premises. The lease contains two 5-year renewal options after the original lease period expires. The PBC also leases office equipment under operating leases with varying expirations.

Minimum future rental payments under the non-cancellable operating leases are as follows:

<u>Years Ending December 31,</u>	<u>Amount</u>
2015	\$ 100,000
2016	100,000
2017	100,000
2018	100,000
2019	100,000
Thereafter	300,000
	\$ 800,000

Rent expense was approximately \$88,000 and \$69,000 for the years ended December 31, 2014 and 2013, respectively.

(b) In 2013, the PBC entered into a contractual agreement with a former employee to provide consulting services to the PBC until August 31, 2017. Management believes that the contract includes substantial risk of forfeiture and therefore only payments made in 2014 and 2013 are reflected as expenses in the accompanying financial statements.

(7) Line of credit

During 2014, the PBC obtained a \$250,000 revolving line of credit from Farmers & Merchants Bank to help finance its working capital and short-term capital needs. The unsecured line of credit had a balance of \$80,000 at December 31, 2014 and was repaid on June 19, 2015. Interest was payable monthly on outstanding balances at the interest rate of 7.5%.

(8) Loan and notes payable

As of December 31, 2012, the PBC had approximately \$1.208 million of accounts payable representing pre-opening amounts, i.e., amounts arising from activities prior to the opening of the USS Iowa to the public. During 2013, the PBC negotiated the settlement of these amounts with various vendors, which resulted in \$728,279 converted to long-term notes payable and \$259,223 of debt forgiveness, the latter is represented as a contribution in 2013 in the accompanying financial statements.

PACIFIC BATTLESHIP CENTER
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

At December 31, 2014 and 2013, respectively, loan and notes payable consist of the following:

	2014	2013
Non-interest bearing loan due to related party payable upon demand.	\$ 500,000	\$ 500,000
Note due to related party with annual interest rate of 4%, with outstanding principal due in January 2016. The PBC recorded \$12,000 and \$15,208 of forgiven interest as a contribution in 2014 and 2013, respectively, in the accompanying statement of activities.	300,000	300,000
Note bearing interest rate of 4.0% annually, due upon demand.	50,000	50,000
Notes payable as settlement for pre-opening payables, with annual interest rate of 4%, payable monthly with outstanding principal and interest due in 2016.	81,812	132,046
Notes payable as settlement for pre-opening payables, with annual imputed interest rate of 4%, payable monthly with outstanding principal and interest due in 2017.	40,796	56,588
Notes payable as settlement for pre-opening payables, with annual interest rate of 4%, payable monthly with outstanding principal and interest due in 2018.	254,672	317,204
Note payable as settlement for pre-opening payables, with annual imputed interest rate of 4%, payable monthly with outstanding principal and interest due in 2019.	138,310	177,405
Total loan and notes payable	\$ 1,365,590	\$ 1,533,243

Future principal payments due at December 31 are as follows:

Years Ending December 31,	Amount
2015	\$ 1,000,442
2016	138,855
2017	102,537
2018	75,100
2019	48,656
	\$ 1,365,590

PACIFIC BATTLESHIP CENTER
Notes to Financial Statements (Continued)
December 31, 2014 and 2013

(9) Functional allocation of expenses

For the years ended December 31, 2014 and 2013, expenses by functional basis (inclusive of depreciation) are as follows:

	<u>2014</u>	<u>2013</u>
Program services	\$ 2,781,201	\$ 3,290,669
General and administrative	699,548	497,486
Fundraising	<u>161,475</u>	<u>196,830</u>
Total expenses by functional basis	<u>\$ 3,642,224</u>	<u>\$ 3,984,985</u>

(10) Subsequent events

The PBC has evaluated subsequent events from the date of the statement of financial position through June 29, 2015, which is the date the financial statements were available to be issued.