

School of Arts and Culture at MHP

Financial Statements

June 30, 2017
(With Comparative Totals for 2016)



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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
School of Arts and Culture at MHP
San Jose, California

We have audited the accompanying financial statements of School of Arts and Culture at MHP (a California nonprofit corporation) (the "School"), which comprise the statement of financial position as of June 30, 2017, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America (the "U.S."); 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 U.S. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of School of Arts and Culture at MHP as of June 30, 2017, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the U.S.

Report on Summarized Comparative Information

We have previously audited School of Arts and Culture at MHP's 2016 financial statements, and our report dated November 30, 2016 expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2016, is consistent, in all material respects, with the audited financial statements from which it has been derived.

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

Armanino^{LLP}
San Jose, California

January 8, 2018

School of Arts and Culture at MHP
Statement of Financial Position
June 30, 2017
(With Comparative Totals for 2016)

	2017	2016
ASSETS		
Current assets		
Cash and cash equivalents	\$ 426,012	\$ 431,497
Cash - Agency fund for scholarships	22,445	21,595
Accounts receivable	53,859	13,715
Grants receivable	372,083	357,400
Pledges receivable	300	-
Donated rent receivable, current portion (Note 5)	528,388	516,901
Prepaid expenses and deposits	27,616	25,604
Total current assets	1,430,703	1,366,712
Property and equipment, net	71,621	72,243
Other assets		
Grants receivable, net of current portion	-	60,000
Donated rent receivable, net of current portion (Note 5)	6,647,658	7,176,045
Total other assets	6,647,658	7,236,045
Total assets	<u>\$ 8,149,982</u>	<u>\$ 8,675,000</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable and accrued liabilities	\$ 207,499	\$ 216,982
Agency fund for scholarships payable	22,445	21,595
Deferred revenue	123,855	120,022
Total current liabilities	353,799	358,599
Net assets		
Unrestricted	364,591	52,688
Temporarily restricted	7,431,592	8,263,713
Total net assets	7,796,183	8,316,401
Total liabilities and net assets	<u>\$ 8,149,982</u>	<u>\$ 8,675,000</u>

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

School of Arts and Culture at MHP
Statement of Activities
For the Year Ended June 30, 2017
(With Comparative Totals for 2016)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>2017 Total</u>	<u>2016 Total</u>
Support and revenue				
Support				
Grants and contributions	\$ 708,062	\$ 605,617	\$ 1,313,679	\$ 1,280,724
Donated rent present value discount amortization (Note 5)	-	164,055	164,055	339,309
Contributions in-kind (excluding donated rent)	<u>-</u>	<u>-</u>	<u>-</u>	<u>492</u>
Total support	<u>708,062</u>	<u>769,672</u>	<u>1,477,734</u>	<u>1,620,525</u>
Revenue				
Rental income	646,549	-	646,549	585,695
Tuition and fees	99,331	-	99,331	177,583
Other revenue	26,315	-	26,315	9,863
Interest income	411	-	411	828
Total revenue	<u>772,606</u>	<u>-</u>	<u>772,606</u>	<u>773,969</u>
Total support and revenue	1,480,668	769,672	2,250,340	2,394,494
Net assets released from restriction	<u>1,601,793</u>	<u>(1,601,793)</u>	<u>-</u>	<u>-</u>
Total support and revenue and net assets released from restriction	<u>3,082,461</u>	<u>(832,121)</u>	<u>2,250,340</u>	<u>2,394,494</u>
Expenses				
Program services				
Arts education program	679,576	-	679,576	728,325
Events - community access and engagement and market rental program	760,201	-	760,201	675,038
Multicultural arts leadership institute	113,876	-	113,876	109,457
Facility	576,340	-	576,340	526,122
Mayferia	199,616	-	199,616	-
Total program services	<u>2,329,609</u>	<u>-</u>	<u>2,329,609</u>	<u>2,038,942</u>
Support services				
Management and general	305,002	-	305,002	320,008
Fundraising	135,947	-	135,947	116,160
Total support services	<u>440,949</u>	<u>-</u>	<u>440,949</u>	<u>436,168</u>
Total functional expenses	<u>2,770,558</u>	<u>-</u>	<u>2,770,558</u>	<u>2,475,110</u>
Change in net assets (Note 3)	311,903	(832,121)	(520,218)	(80,616)
Net assets, beginning of year	<u>52,688</u>	<u>8,263,713</u>	<u>8,316,401</u>	<u>8,397,017</u>
Net assets, end of year	<u>\$ 364,591</u>	<u>\$ 7,431,592</u>	<u>\$ 7,796,183</u>	<u>\$ 8,316,401</u>

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

School of Arts and Culture at MHP
Statement of Functional Expenses
For the Year Ended June 30, 2017
(With Comparative Totals for 2016)

	Program services					Support services				2017 Total	2016 Total
	Arts education program	Events - community access and engagement and market rental program	Multicultural arts leadership institute	Facility	Mayferia	Total program services	Management and general	Fundraising	Total support services		
Personnel expenses											
Salaries and wages	\$ 145,281	\$ 83,878	\$ 40,989	\$ 39,248	\$ 40,202	\$ 349,598	\$ 64,787	\$ 39,170	\$ 103,957	\$ 453,555	\$ 370,090
Employee benefits	20,477	7,836	4,429	3,247	4,788	40,777	5,344	2,987	8,331	49,108	34,009
Payroll taxes	11,274	6,435	3,193	3,165	3,143	27,210	7,733	3,030	10,763	37,973	31,527
Total personnel expenses	177,032	98,149	48,611	45,660	48,133	417,585	77,864	45,187	123,051	540,636	435,626
Donated rent	278,647	154,986	20,429	204,151	-	658,213	20,427	2,315	22,742	680,955	680,956
Outside services	130,936	246,109	7,549	74,201	73,079	531,874	29,135	58,690	87,825	619,699	555,388
Repairs and maintenance	-	-	-	206,474	-	206,474	-	-	-	206,474	173,525
Event rental expense	1,622	190,097	600	3,126	5,285	200,730	5,273	-	5,273	206,003	183,025
Utilities	62,227	35,910	17,557	16,800	17,207	149,701	27,734	16,780	44,514	194,215	174,332
Professional fees	2,243	-	-	-	12,500	14,743	78,040	10,280	88,320	103,063	82,543
Marketing and recruiting expense	12,670	23,688	55	-	27,374	63,787	1,712	1,275	2,987	66,774	29,781
Supplies, including in-kind	5,069	4,006	1,483	20,037	8,707	39,302	9,333	-	9,333	48,635	50,661
Travel	805	3,197	10,366	-	4,408	18,776	500	581	1,081	19,857	3,500
Bank charges	-	-	-	-	-	-	18,245	100	18,345	18,345	11,088
Insurance	-	-	-	-	-	-	15,726	-	15,726	15,726	19,287
Depreciation	6,270	3,487	460	4,593	-	14,810	460	52	512	15,322	12,851
Conferences, conventions and meetings	289	-	6,243	127	-	6,659	3,839	261	4,100	10,759	9,967
Telephone	4	-	-	-	-	4	8,698	8	8,706	8,710	6,328
Dues and subscriptions	692	346	80	733	132	1,983	2,857	364	3,221	5,204	5,487
Training	485	-	243	-	2,032	2,760	-	-	-	2,760	565
Other operating expenses	5	-	-	-	-	5	2,649	54	2,703	2,708	18,944
Printing and publication	426	226	-	-	-	652	2,007	-	2,007	2,659	6,502
Taxes and licenses	-	-	-	438	759	1,197	170	-	170	1,367	438
Postage and shipping	154	-	-	-	-	154	333	-	333	487	12,316
Grants	-	-	200	-	-	200	-	-	-	200	1,200
Scholarships	-	-	-	-	-	-	-	-	-	-	800
	<u>\$ 679,576</u>	<u>\$ 760,201</u>	<u>\$ 113,876</u>	<u>\$ 576,340</u>	<u>\$ 199,616</u>	<u>\$ 2,329,609</u>	<u>\$ 305,002</u>	<u>\$ 135,947</u>	<u>\$ 440,949</u>	<u>\$ 2,770,558</u>	<u>\$ 2,475,110</u>
Percentage of total	<u>25 %</u>	<u>27 %</u>	<u>4 %</u>	<u>21 %</u>	<u>7 %</u>	<u>84 %</u>	<u>11 %</u>	<u>5 %</u>	<u>16 %</u>	<u>100 %</u>	

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

School of Arts and Culture at MHP
Statement of Cash Flows
For the Year Ended June 30, 2017
(With Comparative Totals for 2016)

	2017	2016
Cash flows from operating activities		
Change in net assets	\$ (520,218)	\$ (80,616)
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation expense	15,322	12,851
Donated rent expense	680,955	680,956
Donated rent present value discount amortization	(164,055)	(339,309)
Changes in operating assets and liabilities		
Accounts receivable	(40,144)	18,347
Grants receivable	45,017	(120,207)
Prepaid expenses and deposits	(2,012)	2,246
Accounts payable and accrued liabilities	(9,484)	45,233
Agency fund for scholarships payable	850	21,595
Deferred revenue	3,833	69,074
Net cash provided by operating activities	10,064	310,170
Cash flows from investing activities		
Purchase of property and equipment	(14,699)	(4,903)
Net cash used in investing activities	(14,699)	(4,903)
Net increase (decrease) in cash, cash equivalents and Agency fund	(4,635)	305,267
Cash, cash equivalents and Agency fund, beginning of year	453,092	147,825
Cash, cash equivalents and Agency fund, end of year	\$ 448,457	\$ 453,092
Cash, cash equivalents and Agency fund consisted of the following:		
Cash and cash equivalents	\$ 426,012	\$ 431,497
Cash - Agency fund for scholarships	22,445	21,595
	\$ 448,457	\$ 453,092

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

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

1. NATURE OF OPERATIONS

Guided by a twenty-month community planning process designed to re-imagine Mexican Heritage Plaza's future, a new vision for a School of Arts and Culture at MHP (the "School") was created, embraced by the community and adopted by the City of San Jose in Spring 2011. The School was formally launched in July 2011 with a vision to create a vibrant place of learning, culture and community that nurtures the soul and brings joy, skill building and a sense of belonging to children, families and all who participate. The goal of the School is to narrow the opportunity gap in arts education and learning, nurture the joy, creativity and well-being of our children and unleash the talent of our next generation of students, leaders, artists and consumers of culture. The School is leveraging a \$35 million cultural facility by providing unique and culturally relevant educational offerings of value to the children and families in our community while also creating a "community container" for arts programming with a network of multicultural arts partners. In January 2014, the School of Arts and Culture at MHP was named as the permanent operator of the Mexican Heritage Plaza, and entered into a long-term agreement with the City of San Jose to operate the facility (see Notes 5 and 7).

2. PROGRAM SERVICES

Arts Education Program

The School provides a "multi-cultural and inter-cultural venue" for community events and programs that embrace all cultures, while exploring the artistic traditions, cultural history, and contemporary creative expression of Mexican and Latin American arts. School of Arts and Culture at MHP believes that the arts are powerful vehicles for human development and social transformation - by creating nurturing communities for children, especially those at risk. The School works to create a deep alignment in social and artistic goals. Its task is not to integrate the goals of social transformation and artistic excellence - but to, in the words of its colleagues in the El Sistema movement "reimagine them as one goal." Performance and exhibition is emphasized with the goal of working together toward a communal and joyful experience of creating art together - not as competitive pressure to see who is best.

The School is proud to offer children and the community an inspiring space of professional caliber for performance and exhibition as a vehicle to make their learning visible. Afterschool programs span ten weeks; summer day camps provide a full day of arts curriculum and healthy meals. All sessions culminate in a student performance and exhibition open to the community. Classes include hip hop, breakdance, folklórico, capoeira, Brazilian dance, mariachi for both vocal and instrumental, paper maché, Mexican mural painting, self-portraiture drawing, painting, sculpture, tlacuilo drawing, classical guitar, Aztec dance and drumming, and theater. In addition to the classes offered on-site at the Mexican Heritage Plaza, the School works with local schools to provide arts learning and arts enrichment experiences for students.

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

2. PROGRAM SERVICES (continued)

Events - Community Access and Engagement

School of Arts and Culture at MHP wishes to create as many opportunities as possible for the community to visit, use, perform, and learn at the Mexican Heritage Plaza (the "Plaza"). Like the School of Arts and Culture at MHP, the Plaza was created through extensive community processes. The School continues to honor the Plaza's work and history by ensuring a practice of open communication exists and that multiple entry points are developed over time.

The School's Community Access policy is defined primarily by the spirit of the Guiding Principles for Community Access and Engagement:

- Create welcoming, inclusive and affordable community gatherings and cultural offerings in partnership with artists, arts organizations and community focused nonprofits that capitalize on the strengths of this unique facility and location in the Eastside of San José.
- Develop partnerships with a network of artists, arts and community organizations that will leverage existing relationships and capacity while advancing and growing collective impact.
- Build community confidence, enthusiasm and trust over time through consistent communication, responsiveness and a reliable menu of opportunities.
- Develop a broad mix in programming with a focus on Mexican culture while activating opportunities for social integration with the broader multicultural artistic community present in San José.
- Facilitate multiple points of entry for community members, partner organizations as well as private clients.
- Create a relationship of reciprocity with organizations and the community through "mission compatible" activation of spaces.
- Embrace grassroots participation as critical to the success of School of Arts and Culture at MHP's vision, and provide opportunities for community feedback.

Events - Market Rental Program

School of Arts and Culture at MHP is located in a beautiful multi-use venue in a historically significant location and neighborhood. The site is the same place where civil rights activist Cesar Chavez organized the first grape boycott with the farmworker movement. The house he lived in is located a quarter of a mile away from the School.

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

2. PROGRAM SERVICES (continued)

Events - Market Rental Program (continued)

The business plan written by the MHP Steering Committee in 2011 identifies rental income from the facility as an important component of the long term sustainability of School of Arts and Culture at MHP. The School has partnered with a for profit company, Giant Creative Services, to ensure a careful, creative and attentive approach to market rate rentals. This close partnership with the School staff has successfully increased the usage of the facility by a number of arts organizations and private events in a manner never before seen under previous operators. The School's Market Rental Program generates revenue that then directly supports the school program.

Multicultural Arts Leadership Institute (MALI)

The Multicultural Arts Leadership Institute (MALI) is a professional development opportunity for leaders of color in the arts, culture and entertainment sectors. Currently, so many people of color serve their community through the arts but often work in isolation and without much support. The MALI program was created by people of color, with people of color distinctly in mind. It was piloted under the auspices of 1stACT Silicon Valley from 2008 to 2011 and formally became a stand-alone program operated by School of Arts and Culture at MHP in July 2011. The mission of MALI aligns directly with the School of Arts and Culture at MHP's intention to strengthen the multicultural arts community and cultivate new audiences and cross-cultural experiences.

MALI's presence at School of Arts and Culture at MHP provides a network of 115 graduates who are strong multicultural leaders who can be leveraged to advance the vision of the School. The School provides a home for MALI.

Facility

The School of Arts and Culture at MHP operates the Mexican Heritage Plaza, which is owned by the City of San Jose. The School leverages the \$35 million facility to offer its programs, including quality arts education courses to the community through its Arts Education Program; an arts leadership program for people of color (i.e. the Multicultural Arts Leadership Institute); and community events through its Community Access and Engagement and Market Rental programs. In this way, the long underutilized facility is activated and transformed into a vibrant hub of community activity.

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

2. PROGRAM SERVICES (continued)

Mayferia

During the year ended June 30, 2017, the School of Arts and Culture at MHP launched a special project initiative called Mayferia. This project celebrates the talent, history, and beauty of the Mayfair community. The School will continue to leverage its connections and role in the community as an anchor agency and convener to recruit community members to participate in the process of initiating, developing, planning and implementing the elements of the project. Mayferia activities bring these rich, multi-faceted cultural activities to an area characterized by gang violence, poverty, blight, a lack of resources. Also, with a predominantly Latino population, Mayferia helps residents to develop and enhance a sense of belonging and pride in their heritage and neighborhood, gaining a broader perspective of the challenges faced by the Mayfair neighborhood and a new perspective on the possibilities for change. Current funding for Mayferia will take the project through the year ending June 30, 2019.

3. CHANGE IN NET ASSETS

During the years ended June 30, 2017 and 2016, the School experienced a decrease in net assets of \$520,218 and \$80,616, respectively. A significant amount of the decrease can be attributed to "Donated rent" expense.

Changes in net assets for the fiscal year ended June 30, 2017 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Change in net assets	\$ 311,903	\$ (832,121)	\$ (520,218)
Add back:			
Donated rent expense	680,955	-	680,955
Less:			
Release from time restriction (Note 8)	(680,955)	680,955	-
Donated rent present value discount amortization	<u>-</u>	<u>(164,055)</u>	<u>(164,055)</u>
Change in net assets, excluding donated rent expense	<u>\$ 311,903</u>	<u>\$ (315,221)</u>	<u>\$ (3,318)</u>

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

3. CHANGE IN NET ASSETS (continued)

Changes in net assets for the fiscal year ended June 30, 2016 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Change in net assets	\$ 11,697	\$ (92,313)	\$ (80,616)
Add back:			
Donated rent expense	680,956	-	680,956
Less:			
Release from time restriction (Note 8)	(680,956)	680,956	-
Donated rent present value discount amortization	<u>-</u>	<u>(339,309)</u>	<u>(339,309)</u>
Change in net assets, excluding donated rent expense	<u>\$ 11,697</u>	<u>\$ 249,334</u>	<u>\$ 261,031</u>

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting and financial statement presentation

The financial statements of School of Arts and Culture at MHP have been prepared on the accrual basis of accounting.

In accordance with accounting principles generally accepted in the United States of America, the School is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

- *Unrestricted net assets* - include those assets over which the Board of Directors has discretionary control in carrying out the operations of the School. Under this category, the School maintains an operating fund, property and equipment fund plus any net assets designated by the Board for specific purposes.
- *Temporarily restricted net assets* - include those assets which are subject to donor restriction and for which the applicable restriction was not met as of the year end of the current reporting period.
- *Permanently restricted net assets* - include those assets which are subject to a non-expiring donor restriction, such as endowments. There are currently no permanently restricted net assets.

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Summarized financial information

The financial statements include certain prior-year summarized comparative information in total but not by net asset class or functional expense categories. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the School's financial statements for the year ended June 30, 2016, from which the summarized information was derived.

Cash and cash equivalents

Cash and cash equivalents include highly liquid investments and investments with a maturity of three months or less, and exclude donor restricted receipts and amounts designated for long-term purposes. The School maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The School has not experienced any losses in such accounts. Management believes it is not exposed to any significant risk on cash accounts.

Fair value measurements

Fair value is defined as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."

A hierarchy has been established to prioritize the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest ranking to fair values determined using unadjusted quoted prices in active markets for identical assets (Level 1) and the lowest ranking to fair values determined using methodologies and models with unobservable inputs (Level 3). Observable inputs are those that market participants would use in pricing the asset based on market data obtained from sources independent of the School. Unobservable inputs reflect the School's assumption about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The fair value hierarchy is categorized into three levels based on the inputs as follows:

- *Level 1* - Values are unadjusted quoted prices for identical assets and liabilities in active markets accessible at the measurement date.
- *Level 2* - Inputs include quoted prices for similar assets or liabilities in active markets, quoted prices from those willing to trade in markets that are not active, or other inputs that are observable or can be corroborated by market data for the term of the instrument. Such inputs include market interest rates and volatilities, spreads and yield curves.

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurements (continued)

- *Level 3* - Certain inputs are unobservable (supported by little or no market activity) and significant to the fair value measurement. Unobservable inputs reflect the School's best estimate of what hypothetical market participants would use to determine a transaction price for the asset or liability at the reporting date.

Accounts, grants and pledges receivable

The School considers all accounts, grants and pledges receivable to be fully collectible; accordingly, no allowance for doubtful accounts is considered necessary.

Promises to give

Unconditional promises to give, less an allowance for uncollectible amounts, are recognized as support in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Promises are recorded at net realizable value if expected to be collected in one year and at fair value if expected to be collected in more than one year. The School considers all unconditional promises to give to be fully collectible; accordingly, no allowance for doubtful accounts is considered necessary. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

Property and equipment

Property and equipment are recorded at cost or estimated fair value for donated items. Equipment purchases over \$1,000 are capitalized. The cost of repairs and maintenance which do not improve or extend the lives of the respective assets are expensed currently. Depreciation is computed on the straight-line method based on the estimated useful lives of the assets, which is 5 to 14 years. Depreciation is charged to the activity benefiting from the use of the property or equipment.

Accrued vacation

Accrued vacation represents vacation earned, but not taken as of June 30, 2017 and 2016. The accrued vacation balance as of June 30, 2017 and 2016 was \$36,040 and \$33,504, respectively.

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Agency fund for scholarships

The School entered into an agreement in August 2015 with Mi Pueblo, LLC (Mi Pueblo). Under this agreement, Mi Pueblo appointed the School as an agent. This agreement was established to provide scholarship funds to college bound, graduating high school seniors. These funds are under the control of Mi Pueblo and cannot be awarded to a student without the approval of Mi Pueblo. Scholarships were awarded during the fiscal years ending June 30, 2017 and 2016 totaling \$4,000 and \$125,000, respectively. The cash and related liability for the agency fund for scholarships totaled \$22,445 and \$21,595 as of June 30, 2017 and 2016, respectively.

Revenue recognition

The School recognizes support and revenue on the accrual basis of accounting. Revenue from grants which have been classified as "exchange transactions" and program fees are recognized as revenue in the period in which the service is provided.

Contributions

Contributions are recognized when the donor makes a pledge to give that is, in substance, an unconditional promise. Contributions are recorded as unrestricted, temporarily restricted, or permanently restricted depending on the nature of donor restrictions. Restricted contributions are reported as increases in restricted net assets. When the restriction is met the amount is shown as a reclassification of restricted net assets to unrestricted net assets.

Contributions in-kind

Donated equipment and other donated goods are recorded at their estimated fair value as of the date of the donation. Donated space is recorded at the estimated fair value of comparable property as of the date of the donation. Contributed services, which require a specialized skill and which the School would have paid for if not donated, are recorded at the estimated fair value at the time the services are rendered.

Functional expense allocations

The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of activities and in the statement of functional expenses. Accordingly, certain costs have been allocated among the programs and support services benefited. Indirect expense allocations are based on square footage and/or the number of full time equivalent staff members in each activity.

School of Arts and Culture at MHP
Notes to Financial Statements
June 30, 2017
(With Comparative Totals for 2016)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax status

School of Arts and Culture at MHP is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code and state income taxes under Section 23701d of the California Revenue Taxation Code. Accordingly, no provision for income taxes has been made in the accompanying statements. In addition, the School qualifies for the charitable contribution deduction under Section 170(b)(1)(A) of the Internal Revenue Code and has been classified as an organization that is not a private foundation under Section 509(a)(1) of the Internal Revenue Code.

Uncertainty in income taxes

Generally accepted accounting principles provide accounting and disclosure guidance about positions taken by an organization in its tax returns that might be uncertain. Management has considered its tax positions and believes that all of the positions taken by the School in its federal and state exempt organization tax returns are more likely than not to be sustained upon examination.

The School's federal returns could be subject to examination by federal taxing authorities, generally for 3 years after they are filed. The School's state returns could be subject to examination by state taxing authorities, generally for 4 years after they are filed.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of support, revenue and expenses during the period. Accordingly, actual results could differ from those estimates.

Advertising

The School's policy is to expense advertising costs as the costs are incurred. Advertising expense for the years ended June 30, 2017 and 2016 was \$68,894 and \$35,310, respectively.

Subsequent events

Management of the School has evaluated events and transactions subsequent to June 30, 2017 for potential recognition or disclosure in the financial statements. The School did not have subsequent events that required recognition or disclosure in the financial statements for the year ended June 30, 2017. Subsequent events have been evaluated through the date the financial statements became available to be issued, January 8, 2018.

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5. DONATED RENT RECEIVABLE

In January 2014, the School of Arts and Culture at MHP entered into a fifteen year agreement, effective July 1, 2014, with the City of San Jose to act as the permanent operator of the Mexican Heritage Plaza. Under this agreement the School operates the Plaza for no rent and both parties may elect to extend the term of the agreement for 2 terms of ten years each (see Note 7).

As management has determined that it is unlikely that either party would terminate the agreement, during the initial fifteen year term, the School recognized the benefit of the fair value of the rent received through this agreement as donated rent receivable and temporarily restricted support. The School has established the fair market value of the rent under the agreement at \$680,954 per year. The annual rent expense is included in the statement of activities beginning with the year ended June 30, 2015. The net present value of the future contribution benefit has been computed at a discount rate of 2.2% based upon prevailing rates when the agreement was entered into and is recorded as donated rent receivable on the statement of financial position.

Donated rent receivable is expected to be received as follows:

<u>Year ending June 30,</u>		
2018	\$	528,388
2019		540,131
2020		552,134
2021		564,404
2022		576,947
Thereafter		<u>4,414,042</u>
		7,176,046
Current portion		<u>(528,388)</u>
	<u>\$</u>	<u>6,647,658</u>

6. PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	<u>2017</u>	<u>2016</u>
Theater equipment	\$ 58,385	\$ 44,717
Leasehold improvements	48,375	48,375
Office equipment	<u>8,586</u>	<u>7,555</u>
	115,346	100,647
Accumulated depreciation	<u>(43,725)</u>	<u>(28,404)</u>
	<u>\$ 71,621</u>	<u>\$ 72,243</u>

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6. PROPERTY AND EQUIPMENT (continued)

Depreciation expense for the years ended June 30, 2017 and 2016 was \$15,322 and \$12,851, respectively.

7. MEXICAN HERITAGE PLAZA OPERATOR AND USE AGREEMENT

In January 2014, School of Arts and Culture at MHP entered into a new fifteen year agreement with the City, effective July 1, 2014 to act as the permanent operator of the Mexican Heritage Plaza. Following the expiration in June 30, 2029, both parties may elect to extend the term of the agreement for 2 terms of ten years each (see Note 5).

Under the new agreement, the quarterly operations payments to the School will be structured to match earned and contributed income raised by the School. The match will be limited to \$450,000 per year in years one to five and \$425,000 per year in years six through termination. Other terms of the match remain unchanged from the previous agreement.

Under the new agreement, annual appropriations for Capital Repairs and Capital Replacements of \$50,000 per year are earmarked for the Plaza for years one to five and \$100,000 in years six through termination. Included in this \$100,000 is \$25,000 representing a reallocation from the reduction in the operation payments and is contingent upon a City match of \$25,000.

8. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following:

	<u>2017</u>	<u>2016</u>
Purpose restrictions		
Mayferia	\$ 166,668	\$ 126,247
K-12 education and summer camps	50,000	183,210
Other programs	22,651	24,500
Fiscal sponsorship	16,227	34,042
Multicultural Arts Leadership Institute	-	45,280
	<u>255,546</u>	<u>413,279</u>
Time restrictions		
Donated rent for future periods	7,176,046	7,692,946
General support for future periods	-	157,488
	<u>7,176,046</u>	<u>7,850,434</u>
	<u>\$ 7,431,592</u>	<u>\$ 8,263,713</u>

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8. TEMPORARILY RESTRICTED NET ASSETS (continued)

Temporarily restricted net assets released from restriction during the year were as follows:

	2017	2016
Purpose restrictions		
Other programs	\$ 223,355	\$ 6,555
Mayferia	209,580	153
K-12 education and summer camps	198,710	104,824
Multicultural Arts Leadership Institute	71,530	30,195
Fiscal sponsorship	60,175	27,289
	763,350	169,016
Time restrictions		
Donated rent for future periods	680,955	680,956
General operating	157,488	177,512
	\$ 1,601,793	\$ 1,027,484

9. CONFLICT OF INTEREST POLICY

Included among the School's Board of Directors and Officers are volunteers from the community who provide valuable assistance to the School in the development of policies and programs and in the evaluation of business transactions. The School has adopted a conflict of interest policy whereby Board members are disqualified from participation in the final decisions regarding any action affecting their related company or agency.

10. COMMITMENTS AND CONTINGENCIES

Grants and contracts awarded to School of Arts and Culture at MHP are subject to the funding agencies' criteria, contract terms and regulations under which expenditures may be charged and are subject to audit under such terms, regulations and criteria. Occasionally, such audits may determine that certain costs incurred in connection with the grants do not comply with the established criteria that govern them. In such cases, the School could be held responsible for repayments to the funding agency for the costs or be subject to a reduction of future funding in the amount of the costs.

Management does not anticipate any material questioned costs for the contracts and grants administered during the period. The School would be responsible for the absorption of any over-expenditure of its restricted grants which cannot be covered by additional grant funds or contributions from other sources.

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11. CONCENTRATIONS

During the years ended June 30, 2017 and 2016, the School received 42% and 38% of its total support and revenue (including in-kind) directly from the City of San Jose. A reduction in awards of grants from the City could materially impact the services the School provides. In addition, the School of Arts and Culture at MHP maintains that it is unlikely that the City of San Jose would be able to rent the entire facility to any single tenant given the unique nature of the space and the community directive to maintain arts and cultural programming at the site.