PACIFIC BATTLESHIP CENTER

Financial Statements

December 31, 2013 and 2012

(With Independent Auditor's Report Thereon)

MGO Certified Public Accountants.

PACIFIC BATTLESHIP CENTER

Table of Contents

MGO Certified Public Accountants.

Newport Beach
4675 MacArthur Court, Suite 600
Newport Beach, CA 92660
949.221.0025

Sacramento

Walnut Creek

Oakland

LA/Century City

San Diego

Seattle

Independent Auditor's Report

The Board of Directors
Pacific Battleship Center:

We have audited the accompanying financial statements of Pacific Battleship Center (PBC) (a nonprofit organization), which comprise the statements of financial position as of December 31, 2013 and 2012, 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, 2013 and 2012, 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 & O'Connell LLP

June 27, 2014
Newport Beach, California

Pacific Battleship Center

Statements of Financial Position

December 31, 2013 and 2012

Assets		**2013**	**2012**
Cash	$	484,742	122,901
Accounts receivable		62,753	80,942
Contributions receivable		1,007,000	1,500,000
Engineering/machine shop materials		50,708	228,977
Deposits and prepaid insurance		64,391	8,334
Property and equipment, net		4,760,786	4,576,632
Total assets	$	6,430,380	6,517,786
Liabilities and Net Assets			
Liabilities:			
Accounts payable	$	80,185	1,472,998
Accrued and other liabilities		170,385	87,099
Capital lease obligations		118,832	306,636
Loan and notes payable		1,533,243	884,834
Total liabilities		1,902,645	2,751,567
Net Assets:			
Unrestricted		3,491,649	2,266,219
Temporarily restricted		1,036,086	1,500,000
Total net assets		4,527,735	3,766,219
Total liabilities and net assets	$	6,430,380	6,517,786

See accompanying notes to financial statements.

Pacific Battleship Center

Statement of Activities

Year ended December 31, 2013

	Unrestricted	Temporarily restricted	Total
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	$ 3,491,649	1,036,086	4,527,735

See accompanying notes to financial statements.

Pacific Battleship Center
Statement of Activities
Year ended December 31, 2012

		Unrestricted	Temporarily restricted	Total
Revenues and other support:				
Admissions	$	2,333,877	-	2,333,877
Contributions		3,926,704	1,500,000	5,426,704
Commissions		233,616	-	233,616
Other income		210,685	-	210,685
Total revenues and other support		6,704,882	1,500,000	8,204,882
Expenses:				
Program services		3,028,956	-	3,028,956
General and administrative		396,227	-	396,227
Fundraising		571,332	-	571,332
Subtotal expenses		3,996,515	-	3,996,515
Change in net assets, before depreciation		2,708,367	1,500,000	4,208,367
Depreciation		(220,424)	-	(220,424)
Change in net assets		2,487,943	1,500,000	3,987,943
Net assets, beginning of year		(221,724)	-	(221,724)
Net assets, end of year	$	2,266,219	1,500,000	3,766,219

See accompanying notes to financial statements.

Pacific Battleship Center

Statements of Cash Flows

Years ended December 31, 2013 and 2012

	2013	2012
Cash flows provided by operating activities:		
Change in net assets	$ 761,516	3,987,943
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	480,660	220,424
Forgiveness of pre-opening vendor payables	(259,223)	-
Contributed property and equipment	(517,539)	-
Change in assets and liabilities:		
Accounts receivable	18,189	(80,942)
Contributions receivable	493,000	(1,500,000)
Engineering/machine shop materials	178,269	(1,065)
Deposits and prepaid insurance	(56,057)	(8,334)
Accounts payable	(405,311)	1,343,302
Accrued and other liabilities	83,286	80,868
Cash provided by operating activities	776,790	4,042,196
Cash flows from investing activities:		
Purchases of property and equipment	(147,275)	(4,508,466)
Cash used in investing activities	(147,275)	(4,508,466)
Cash flows from financing activities:		
Proceeds from issuance of notes payable	-	550,000
Principal repayments on notes payable	(79,870)	-
Payments on capital lease obligations	(187,804)	(78,147)
Cash (used in) provided by financing activities	(267,674)	471,853
Net increase in cash and cash equivalents	361,841	5,583
Cash, beginning of year	122,901	117,318
Cash, end of year	$ 484,742	122,901
Non-cash financing activities:		
Conversion of pre-opening vendor payable to note payable	(728,279)	

See accompanying notes to financial statements.

(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,
- to educate the public on the accomplishments and sacrifices of American patriots, and
- to 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 City of Los Angeles, through its Board of Harbor Commissioners, owns the pier where the USS Iowa is moored. 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. 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.

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, 2013 or 2012.

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 two financial institutions. Beginning January 1, 2013, the accounts maintained in the institutions are guaranteed by the Federal Deposit Insurance Corporation (“FDIC”) up to $250,000. Previously, until December 31, 2012, the accounts were guaranteed by FDIC up to $250,000 for interest bearing accounts and unlimited for non-interest bearing accounts. At December 31, 2013, the PBC was $211,400 in excess of the FDIC insurance limits. At December 31, 2012, the PBC was not in excess of the FDIC insurance limits.

(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.

(Continued)

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.

(e) Deposits and Prepaid Insurance

The PBC has entered into a financing arrangement for annual insurance premiums. After the down payment of $10,506 paid during 2013, the PBC has an obligation to pay $45,800 in 2014 and is reflected as accrued and other liabilities in the accompanying financial statements. The financed asset amount of $55,747 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.

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. Depreciation commenced in July 2012, when the ship opened to the public. 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, 2013 and 2012, 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 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.

(Continued)

(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.

(k) Donated goods and services

In 2013, the PBC received donated goods and services of $610,804, 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 year ended December 31, 2013 are as follows:

Capitalized donated services for sewer installation (see Note 3)	$	254,625
Capitalized equipment		262,914
Donated program services		93,265
Total donated goods and services	$	610,804

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) 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.

(m) 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.

(n) Reclassifications

Certain prior year amounts have been reclassified to conform with the current year presentation.

(3) Property and equipment

Property and equipment are summarized as follows at December 31, 2013 and 2012:

	2013	2012
Furniture and equipment	$ 1,541,964	$ 1,158,490
Sewer installation	254,625	-
Ship restoration and improvement	3,665,281	3,638,566
Subtotal capital assets	5,461,870	4,797,056
Accumulated depreciation	(701,084)	(220,424)
Total property and equipment, net	$ 4,760,786	$ 4,576,632

Depreciation expense was $480,660 and $220,424 for the years ended December 31, 2013 and 2012, respectively. During 2013, the PBC began the project of installing sewer access. The project is in process and therefore no depreciation expense has been recorded for 2013. The installation is expected to be completed by October 2014.

(4) Contributions receivable

Contributions receivable at December 31, 2013 and 2012, respectively, are expected to be received as follows:

	2013	2012
Within one year	$ 257,000	$ 500,000
Within one to five years	750,000	1,000,000
Total contributions receivable	$ 1,007,000	$ 1,500,000

The amounts due from one donor represent 99% and 100% of the contributions receivable at December 31, 2013 and 2012, respectively.

(5) Capital lease obligations

Following is a summary of equipment held under capital lease at December 31, 2013 and 2012, respectively:

		2013		**2012**
400KW Caterpillar generator	$	48,618	$	106,925
230KW Caterpillar generator		-		75,000
Ticketing booth		61,369		90,648
Forklift		8,845		34,063
	$	118,832	$	306,636

Future minimum lease payments under capital lease obligations as of December 31, 2013, are as follows:

Year ending December 31,		
2014	$	90,786
2015		29,280
2016		29,280
Total future minimum lease payments		149,346
Less amount representing interest		(30,514)
Present value of future minimum lease payments	$	118,832

(6) Commitments

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 2013 are reflected as expenses on the accompanying financial statements.

(7) 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 note payable and $259,223 of debt forgiveness, the latter is represented as contribution in the accompanying financial statements.

(Continued)

At December 31, 2013 and 2012, respectively, loan and notes payable consist of the following:

	2013	2012
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 $15,208 of forgiven interest as a contribution in 2013 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
Note bearing interest rate of 10.0% annually, due March 31, 2014.	-	25,000
Non-interest bearing note due to related party payable upon demand.	-	9,834
Notes payable as settlement for pre-opening payables, with annual interest rate of 4%, payable monthly with outstanding principal and interest due in 2016.	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.	233,993	-
Notes payable as settlement for pre-opening payables, with annual interest rate of 4%, payable monthly with outstanding principal and interest due in 2018.	317,204	-
Total loan and notes payable	$ 1,533,243	$ 884,834

Future principal payments due at December 31 are as follows:

Years Ending June 30,	**Amount**
2014	$ 741,906
2015	178,575
2016	463,729
2017	96,320
2018	52,713
	$ 1,533,243

(Continued)

(8) Functional allocation of expenses

For the years ended December 31, 2013 and 2012, expenses by functional basis (inclusive of depreciation) are as follows:

	2013	2012
Program services	$ 3,290,669	$ 3,249,380
General and administrative	497,486	396,227
Fundraising	196,830	571,332
Total expenses by functional basis	$ 3,984,985	$ 4,216,939

(9) Subsequent events

The PBC has evaluated events and transactions occurring subsequent to the statement of financial position date of December 31, 2013, for items that should potentially be recognized or disclosed in these financial statements. The evaluation was conducted through June 27, 2014, the date the financial statements were available to be issued.

On April 25, 2014, the PBC received a cash donation of $250,000 in support of the PBC's new Overnight Program. The Overnight Program, which is expected to open in September 2014, will provide children the opportunity to spend the night onboard the ship, while also providing PBC with an additional, ongoing revenue stream.