

# Pacific Resources for Education and Learning

## Notes to Financial Statements

### September 30, 2009 and 2008

#### 1. Organization and Operations

Pacific Resources for Education and Learning ("PREL") is a not-for-profit corporation established in January 1990. PREL's mission is *Building Capacity Through Education*. PREL's primary operating area includes the State of Hawaii; a U.S. commonwealth, the Commonwealth of the Northern Mariana Islands; two U.S. territories, American Samoa and Guam; and three freely associated states, the Republic of the Marshall Islands, the Republic of Palau, and the Federated States of Micronesia (Chuuk, Kosrae, Pohnpei, and Yap). PREL's main office is located in Honolulu, Hawaii. In 2005, the Twenty-Third Legislature of the State of Hawaii recognized PREL as an Educational Service Agency.

PREL is a tax-exempt organization for Federal and State income tax purposes, under Internal Revenue Code Section 501(c)(3).

#### 2. Summary of Significant Accounting Policies

##### Financial Statement Presentation

The financial statements of PREL are presented on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America established for not-for-profit organizations.

In March 2008, PREL's Board of Directors approved a change to PREL's fiscal year end from November 30 to September 30. This change aligns PREL's fiscal year end more closely to the seasonal nature of its business. Accordingly, PREL is presenting audited financial statements for the ten months ended September 30, 2008.

PREL classifies net assets, revenues, gains and other support and expenses based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of PREL and changes therein are classified and reported as follows:

- **Unrestricted net assets** – Net assets not subject to donor-imposed stipulations or received with restrictions that were satisfied in the same period.
- **Temporarily restricted net assets** – Net assets subject to donor-imposed stipulations that may or will be met either by actions of PREL and/or the passage of time. See Note 10 for information regarding PREL's temporarily restricted net assets.
- **Permanently restricted net assets** – Net assets subject to donor-imposed stipulations that must be maintained permanently by PREL. There were no permanently restricted net assets at September 30, 2009 and 2008.

##### Use of Estimates in Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles 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.

##### Fair Value Measurements

PREL measures the fair value of assets and liabilities as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants at the measurement date. The fair value hierarchy distinguishes between independent observable inputs and unobservable inputs used to measure fair value as follows:

*Level 1:* Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

*Level 2:* Inputs other than quoted market prices included within Level 1 that are observable for an asset or liability, either directly or indirectly.

*Level 3:* Unobservable inputs for an asset or liability reflecting the reporting entity's own assumptions. Level 3 inputs should be used to measure fair value to the extent that observable Level 1 or 2 inputs are not available.

##### Cash and Equivalents

Cash and equivalents include unrestricted currency on hand and demand deposits.

##### Investments

Cash, money funds, and short-term bonds in brokerage accounts are classified as investments and are recorded at fair value.

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### September 30, 2009 and 2008

#### **Receivables**

Grants and contract receivables represent reimbursable grants and contracts outstanding at year end. Management analyzes the collectibility of these receivables and establishes an allowance for doubtful accounts when the receivable is deemed uncollectible. At September 30, 2009 and 2008, PREL's grants and contract receivables were primarily from the Federal government. Management has determined that the grants and contract receivables are fully collectible; therefore, no allowance for uncollectible grants and contract receivables is considered necessary as of September 30, 2009 and 2008.

#### **Property and Equipment**

Property and equipment are stated at cost or fair value on the date of receipt for donated assets, and depreciated using the straight-line method over the estimated useful lives of the assets. Donated furniture and fixtures located on leased property are depreciated over the lease term. Gains or losses on asset retirement or disposition are reflected in the statement of activities.

Capital equipment purchased with Federal grant or contract proceeds is expensed as the Federal government retains an interest in and control over the equipment. At the conclusion of the grant period, the equipment may be utilized by other federal programs or may be purchased from the Federal government.

#### **Deferred Revenue**

Deferred revenue represents amounts advanced from a licensee relative to a software product that was developed by PREL and licensed to the licensee. Amounts advanced are for future royalty fees, which will be earned by PREL once the licensee begins to earn revenues from the sale or license of the product, as defined in the license agreement.

#### **Revenue Recognition**

A substantial percentage of PREL's revenue is derived from federal cost reimbursable grants and contracts, and fixed price contracts. Revenue is deemed earned and recorded when expenditures are incurred in compliance with specific contract or grant restrictions. This method approximates the percentage-of-completion method of accounting for fixed price contracts. Losses on fixed priced contracts, if any, are recognized at the time a loss on a contract becomes known. Amounts received but not yet earned from contracts are recorded as advance funding on contracts in the statements of financial position.

Federal grant and contract amounts presented in the statements of activities consist of grants and contracts awarded to PREL from the Federal government or other organizations that require compliance with federal grant and contract restrictions.

#### **Contributed Services**

Educators, schools and others participate in educational programs and research offered by PREL under various contracts and grants. The value of their contributions is not reflected in the financial statements since these services do not meet the criteria for recognition as contributed services.

#### **Concentrations of Risk**

Substantially all of PREL's Federal support is received from the U.S. Department of Education. This support is subject to annual appropriation.

Expenditures under PREL's Federal programs are subject to final audits that could result in adjustments. Management believes that liabilities, if any, resulting from such audits will not have a material effect on the financial statements.

Credit is granted to customers, substantially all of whom are governmental agencies in the region served by PREL.

Cash balances are maintained with one financial institution in the State of Hawaii. At times, cash balances are in excess of available depository insurance limits, however, PREL does not believe that this concentration of credit risk represents a material risk of loss with respect to its financial position. Additionally, effective October 14, 2008, the financial institution participated in the Federal Deposit Insurance Corporation's Transaction Account Guarantee Program, which fully guarantees noninterest bearing transaction accounts through June 30, 2010.

Investments in money funds and U.S. government and municipal obligations held in brokerage accounts are subject to credit and/or market risk.

#### **Subsequent Events**

PREL has reviewed all events that have occurred from October 1, 2009 through the date of the financial statement issuance for proper accounting and disclosure in the financial statements.

# Pacific Resources for Education and Learning

## Notes to Financial Statements

### September 30, 2009 and 2008

#### 3. Investments

Investments at September 30, 2009 and 2008 were comprised of the following:

|                             | <b>2009</b>       | <b>2008</b>       |
|-----------------------------|-------------------|-------------------|
| Municipal obligations       | \$ 100,000        | \$ -              |
| U.S. government obligations | -                 | 500,000           |
| Money funds                 | 243,719           | 28,258            |
|                             | <u>\$ 343,719</u> | <u>\$ 528,258</u> |

Fair value of investments based on Level 2 inputs (significant other observable inputs) and measured on a recurring basis was \$343,719 and \$528,258 at September 30, 2009 and 2008, respectively. Valuation techniques utilized to determine fair value are consistently applied.

#### 4. Unbilled Contract Receivables

Unbilled contract receivables were \$823,472 and \$557,890 at September 30, 2009 and 2008, respectively.

#### 5. Property and Equipment

Property and equipment at September 30, 2009 and 2008 was comprised of the following:

|                                   | <b>2009</b>      | <b>2008</b>       |
|-----------------------------------|------------------|-------------------|
| Furniture, fixtures and equipment | \$ 507,547       | \$ 578,877        |
| Leasehold improvements            | 248,530          | 248,530           |
|                                   | <u>756,077</u>   | <u>827,407</u>    |
| Less: accumulated depreciation    | 666,707          | 713,488           |
|                                   | <u>\$ 89,370</u> | <u>\$ 113,919</u> |

Depreciation expense amounted to \$44,586 and \$46,741 for the year ended September 30, 2009 and the ten months ended September 30, 2008, respectively.

#### 6. Line of Credit

PREL has a revolving line of credit with a bank, which renews annually unless either party terminates the line of credit. The revolving line of credit was \$150,000 as of September 30, 2009 and 2008. Terms of the credit agreement state that future drawings, if any, will be subject to the bank's base rate plus 2.25% at September 30, 2009 and 2008. The line is collateralized by all of PREL's unrestricted assets. There were no drawings at September 30, 2009 and 2008.

#### 7. Lease Commitments

PREL entered into a non-cancelable operating lease for its office space in Honolulu that expires on December 26, 2012. The lease provides for fixed minimum rent payments and PREL's share of building operating expenses with an option to extend. PREL also has a non-cancelable operating lease expiring on June 30, 2010 for office space in Guam.

The future minimum annual rental commitments are as follows:

| <b>Years ending</b> |                     |
|---------------------|---------------------|
| 2010                | \$ 468,000          |
| 2011                | 458,000             |
| 2012                | 458,000             |
| 2013                | 114,000             |
|                     | <u>\$ 1,498,000</u> |

# Pacific Resources for Education and Learning

## Notes to Financial Statements

### September 30, 2009 and 2008

Total lease rent expense for all operating leases approximated \$479,000 and \$410,000 for the year ended September 30, 2009 and the ten months ended September 30, 2008, respectively.

#### Other Commitments

At September 30, 2009, PREL had approximately \$1,269,000 in commitments outstanding for research consultants and technical expertise services for programs run by PREL.

#### 8. Retirement Plan

PREL has a defined contribution retirement plan covering substantially all regular full-time employees. PREL contributions of 12.5% of eligible employee compensation begin after an employee has completed six months of service. Contributions are paid to a third party fund sponsor and are fully vested when paid. PREL's contributions to the plan amounted to approximately \$584,000 and \$565,000 for the year ended September 30, 2009 and the ten months ended September 30, 2008, respectively.

#### 9. Related Parties

PREL is governed by a board of directors consisting of individuals representing the constituency in the region that PREL serves. Much of PREL's grant and contract activity is incurred in support of programs that benefit local government, educational agencies and local communities where the directors have assumed positions of leadership. PREL also has receivables and accounts payable with these organizations.

#### 10. Pacific Teacher Scholarship Fund

In 2004, PREL established the Pacific Teacher Scholarship Fund with the purpose to increase the number of qualified teachers in the U.S.-affiliated Pacific. The scholarship is available to eligible college students from the U.S.-affiliated Pacific pursuing teacher certification. Contributions received are recorded as temporarily restricted. When scholarships are awarded, the funds are released from restriction.

PREL's Board of Directors designated \$14,774 for the Scholarship Fund in 2004. The composition of funds available at September 30, 2009 and 2008 is as follows:

|                        | 2009              | 2008             |
|------------------------|-------------------|------------------|
| Temporarily restricted | \$ 95,371         | \$ 78,912        |
| Unrestricted           | 14,774            | 14,774           |
|                        | <u>\$ 110,145</u> | <u>\$ 93,686</u> |

#### 11. Uniform Prudent Management of Institutional Funds Act

In 2006, the Uniform Law Commission approved the Uniform Prudent Management of Institutional Funds Act ("UPMIFA"), which provides guidance and authority to charitable organizations concerning the management and investment of funds held by those organizations, and imposes additional duties on those who manage and invest charitable funds. In June 2009, the State of Hawaii enacted a version of UPMIFA, effective for funds existing on, or established after, July 1, 2009.

In 2008, the Financial Accounting Standards Board issued guidance on the accounting and disclosures for endowment funds subject to UPMIFA. PREL's adoption of this pronouncement in 2009 did not have an impact on its financial statements as PREL did not maintain any donor-restricted or Board designated endowment funds at September 30, 2009. Accordingly, PREL did not maintain formal investment or spending policies associated with donor-restricted or Board designated endowment funds.