

**THE REASON FOUNDATION
COMPARATIVE FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITORS' REPORT
SEPTEMBER 30, 2013 AND 2012**

**THE REASON FOUNDATION
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SEPTEMBER 30, 2013 AND 2012**

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CERTIFIED PUBLIC ACCOUNTANTS
&
BUSINESS CONSULTANTS

January 29, 2014

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
The Reason Foundation
Los Angeles, California

Report on the Financial Statements

We have audited the accompanying financial statements of The Reason Foundation (a nonprofit foundation), which comprise the statement of financial position as of September 30, 2013, 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; 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 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 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 The Reason Foundation as of September 30, 2013, 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 United States of America.

Report on Summarize Comparative Information

We have previously audited The Reason Foundation's 2012 financial statements, and our report dated February 4, 2013, 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 September 30, 2012, is consistent, in all material respects, with the audited financial statements from which it has been derived.

NSBN LLP

NSBN LLP
Beverly Hills, California

THE REASON FOUNDATION
 STATEMENTS OF FINANCIAL POSITION
 SEPTEMBER 30, 2013
 WITH COMPARATIVE TOTALS AT SEPTEMBER 30, 2012

	2013	2012
CURRENT ASSETS		
Cash and cash equivalents (Note 2, 5, 15)	\$ 906,190	\$ 577,227
Accounts receivable, net (Note 2)	97,638	79,069
Pledges receivable, net (Note 2)	302,002	305,350
Investments (Note 2, 6)	2,877,416	3,670,890
TOTAL CURRENT ASSETS	4,183,246	4,632,536
PROPERTY AND EQUIPMENT (Note 2)		
Land	1,908,473	1,908,473
Buildings and improvements	987,972	527,874
Furniture and equipment	1,131,330	994,707
Leasehold improvements	23,725	21,725
Total	4,051,500	3,452,779
Less: accumulated depreciation	(1,002,516)	(914,762)
NET PROPERTY AND EQUIPMENT	3,048,984	2,538,017
OTHER ASSETS		
Deposits	41,412	181,934
TOTAL ASSETS	\$ 7,273,642	\$ 7,352,487
CURRENT LIABILITIES		
Accounts payable	\$ 137,027	\$ 152,164
Accrued expenses	721,679	774,403
Deferred revenue	-	1,050
Unearned subscriptions, current portion (Note 8)	278,524	282,976
Mortgage payable, current portion (Note 10)	112,238	102,553
TOTAL CURRENT LIABILITIES	1,249,468	1,313,146
LONG TERM LIABILITIES		
Unearned subscriptions, less current portion (Note 8)	94,575	80,668
Mortgage payable, less current portion (Note 10)	757,279	1,080,670
TOTAL LIABILITIES	2,101,322	2,474,484
NET ASSETS		
Unrestricted	4,831,175	4,778,375
Temporarily restricted (Note 12)	296,866	55,349
Permanently restricted (Note 12)	44,279	44,279
TOTAL NET ASSETS	5,172,320	4,878,003
TOTAL LIABILITIES AND NET ASSETS	\$ 7,273,642	\$ 7,352,487

See accompanying independent auditors' report.
 The notes are an integral part of these financial statements.

THE REASON FOUNDATION
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED SEPTEMBER 30, 2013
WITH COMPARATIVE TOTALS FOR THE YEAR ENDED SEPTEMBER 30, 2012

	2013			2012	
	Unrestricted Fund	Temporarily Restricted Fund	Permanently Restricted Fund	Total Funds	Total Funds
REVENUE AND SUPPORT					
Contributions	\$ 7,739,197	\$ 283,461	\$ -	\$ 8,022,658	\$ 8,063,133
Magazine	889,048	-	-	889,048	890,741
Special events	331,021	-	-	331,021	238,126
Net investment income and other income	228,368	-	-	228,368	392,282
Released from restriction (Note 13)	41,944	(41,944)	-	-	-
TOTAL REVENUE AND SUPPORT	9,229,578	241,517	-	9,471,095	9,584,282
EXPENSES					
Program services					
Foundation	311,533	-	-	311,533	418,318
Reason- Rupe	507,769	-	-	507,769	339,414
Reason-TV	1,571,437	-	-	1,571,437	1,368,694
Magazine	2,921,384	-	-	2,921,384	2,961,200
Research	2,356,409	-	-	2,356,409	2,229,354
Total program services	7,668,532	-	-	7,668,532	7,316,980
Supporting services					
Management and general	277,800	-	-	277,800	532,254
Fundraising	1,002,703	-	-	1,002,703	935,628
Total supporting services	1,280,503	-	-	1,280,503	1,467,882
Total expenses before special events	8,949,035	-	-	8,949,035	8,784,862
Special events expenses	227,743	-	-	227,743	174,354
TOTAL EXPENSES	9,176,778	-	-	9,176,778	8,959,216
CHANGE IN NET ASSETS	52,800	241,517	-	294,317	625,066
NET ASSETS AT BEGINNING OF YEAR	4,778,375	55,349	44,279	4,878,003	4,252,937
NET ASSETS AT END OF YEAR	\$ 4,831,175	\$ 296,866	\$ 44,279	\$ 5,172,320	\$ 4,878,003

See accompanying independent auditors' report.
The notes are an integral part of these financial statements.

THE REASON FOUNDATION
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED SEPTEMBER 30, 2013
WITH COMPARATIVE TOTALS FOR THE YEAR ENDED SEPTEMBER 30, 2012

	2013										2012	
	Program Services					Supporting Services					Total Expenses	Total Expenses
	Foundation	Reason-Rupe	Reason-TV	Magazine	Research	Total Program Services	Administration	Development	Total Expenses	Total Expenses		
Books and periodicals	\$ 528	\$ -	\$ 595	\$ 2,897	\$ 3,249	\$ 7,561	\$ 365	\$ 1,901	\$ 9,827	\$ 41,107		
Commissions	-	-	-	48,710	-	48,710	-	-	48,710	34,600		
Contract services	1,597	232,751	186,786	338,605	289,154	1,048,893	12,355	16,841	1,078,089	1,292,235		
Dues and subscriptions	9,308	1,884	3,686	9,891	68,143	92,912	1,709	11,479	106,100	66,565		
Insurance	2,596	2,915	16,397	27,745	27,605	77,258	3,778	12,433	93,469	78,769		
Manufacturing and distribution	-	-	648	527,321	531	528,500	-	139	528,639	526,071		
Media tracking and placement services	13,334	-	-	-	-	13,334	-	-	13,334	16,475		
Miscellaneous	3,174	-	23,813	6,095	13,103	46,185	2,690	3,971	52,846	106,141		
On-line services	8,308	2,236	14,520	51,245	29,512	105,822	2,224	6,926	114,972	95,538		
Postage and shipping	508	374	10,447	38,667	18,832	66,828	(486)	66,046	132,388	84,259		
Printed material	90	-	4,910	37,041	26,050	68,091	130	45,699	113,920	56,128		
Professional fees	895	1,753	7,993	11,608	13,074	35,323	1,553	5,114	41,990	19,114		
Promotion and advertising	91	110	1,040	201,485	9,997	212,723	158	18,506	231,387	247,875		
Occupancy costs	7,295	17,588	56,297	86,633	85,820	253,633	11,757	37,150	302,540	383,758		
Salaries, benefits, and taxes	227,967	223,178	1,047,061	1,422,912	1,458,575	4,379,593	226,467	588,412	5,194,472	4,734,453		
Supplies	14,463	2,619	59,086	31,873	73,475	181,516	7,578	44,694	233,788	136,446		
Telephone	3,371	966	12,820	14,329	17,230	48,716	1,545	6,109	56,370	49,195		
Travel and entertainment	15,920	17,351	107,908	41,404	196,963	379,546	2,589	126,305	508,440	543,384		
Unfulfilled pledges	-	-	-	-	-	-	-	-	-	250,000		
Total expenses before depreciation	309,346	504,016	1,554,008	2,896,461	2,331,313	7,595,144	274,412	991,725	8,861,281	8,762,113		
Depreciation	2,187	3,753	17,429	24,923	25,096	73,388	3,388	10,978	87,754	22,749		
Total Expenses	\$ 311,533	\$ 507,769	\$ 1,571,437	\$ 2,921,384	\$ 2,356,409	\$ 7,668,532	\$ 277,800	\$ 1,002,703	\$ 8,949,035	\$ 8,784,862		

See accompanying independent auditors' report.
The notes are an integral part of these financial statements.

THE REASON FOUNDATION
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012

CASH FLOWS FROM OPERATING ACTIVITIES	2013	2012
Change in net assets	\$ 294,317	\$ 625,066
Adjustments to reconcile net assets to net cash provided by operating activities:		
Depreciation	87,754	22,749
Net unrealized (gains) on investments	(221,860)	(390,961)
Donated investment	-	(1,772)
(Increase) decrease in assets:		
Accounts receivable, net	(18,569)	(11,311)
Pledges receivable, net	3,348	171,540
Deposits	140,522	(57,490)
Increase (decrease) in liabilities:		
Accounts payable	(15,137)	34,448
Accrued expenses	(52,724)	227,492
Deferred revenue	(1,050)	(7,950)
Unearned subscriptions	9,455	(55,115)
NET CASH PROVIDED BY OPERATING ACTIVITIES	226,056	556,696
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of property and equipment	(598,721)	(1,329,307)
Purchases of investments	(985,000)	(2,000,000)
Proceeds from sales of investments	2,000,334	2,150,000
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	416,613	(1,179,307)
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments of long term debt	(313,706)	(16,777)
NET CASH (USED IN) FINANCING ACTIVITIES	(313,706)	(16,777)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	328,963	(639,388)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	577,227	1,216,615
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 906,190	\$ 577,227
SUPPLEMENTAL CASH FLOW INFORMATION		
CASH PAID DURING THE YEAR:		
Income taxes paid	\$ -	\$ -
Interest paid	\$ 39,651	\$ 3,827
NON CASH INVESTING AND FINANCING TRANSACTION:		
Debt incurred on acquisition of real property	\$ -	\$ 1,200,000

See accompanying independent auditors' report.
The notes are an integral part of these financial statements.

**THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013**

Note 1 ORGANIZATION

The Reason Foundation (Foundation) was organized for the purpose of educating Americans in the basic principles of the classical liberal/libertarian political philosophy. Toward this end, the Foundation provides research and publications which apply free-market principles to public policy issues. The Foundation's activities include the monthly publication of Reason magazine and the publication of various studies on public policy issues.

Note 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation-

The financial statements of The Reason Foundation have been prepared on the accrual basis of accounting in accordance with the basis of Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) Numbers 958-605 and 958-205. These financial statements reflect all significant receivables, payables, and other liabilities. The Foundation reports 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.

Summarized Comparative Financial Information-

The financial statements include certain prior-year summarized comparative information in total, but not by net asset category. 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 Foundation's financial statements for the year ended September 30, 2012 from which the summarized information was derived.

Cash and Cash Equivalents-

For the purposes of the financial statement, the Foundation considers all highly liquid debt instruments purchased with a maturity date of three months or less to be cash equivalents.

Investments-

Investments in equity securities with readily determinable fair market values and all investments in debt securities are measured at fair value in the statement of financial position. Realized and unrealized gains and losses, interest and dividends on investments are reflected in the statement of activities as unrestricted unless these activities are restricted by donor or by law.

THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013

Note 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT.)

Contributions-

The Foundation has also adopted FASB ASC Number 958-605 and 958-720, "Accounting for Contributions Received and Contributions Made." In accordance with FASB ASC 958-605 and 958-720, contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. When a restriction expires (that is, when a stipulated time restriction ends or 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 restrictions.

Subsequent Events -

Date of Management's Review - Subsequent events have been evaluated through January 29, 2014, the date that these financial statements were available to be issued.

Property and Equipment-

Property, equipment, building, and building equipment are recorded at historical cost and are being depreciated using the straight-line method over the estimated useful life of the assets. The following lives have been assigned:

Furniture and equipment	3 years
Leasehold improvements	5 years
Building improvements	7 years
Building	39 years

Expenditures for maintenance, repairs, and renewals of minor items are charged to expense as incurred. Major renewals and improvements are capitalized. Upon disposition, the cost and related accumulated depreciation are removed from the accounts and the resulting gain or loss is reflected in operations for the year. It is the Foundation's policy to expense items under \$1,000.

Tax Status-

The Foundation is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code, and is exempt from California franchise taxes under Section 23701(d) of the State Revenue and Taxation Code. In addition, the Foundation has been determined by the Internal Revenue Service not to be a private foundation within the meaning of Section 509(a)(1) of the code.

THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013

Note 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT.)

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, disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting year. Actual results could differ from those estimates.

Advertising-

Advertising costs are charged to operations when incurred and are included in functional expenses.

Accounts and Pledges Receivable-

Accounts receivable at September 30, 2013 consist of individually small amounts from a large number of entities, and include advertising sales, list rentals, and magazine subscriptions. Management of the Foundation has assessed the credit risk associated with these accounts receivable and has established an allowance for doubtful accounts to reduce the net carrying value of the receivables to net realizable value. For the year ended September 30, 2013, the allowance for doubtful accounts was \$8,927.

Pledges receivable at September 30, 2013 are due from organizations, corporations, and individuals well-known to the Foundation, with a favorable past payment history. Management of the Foundation has assessed the credit risk associated with these pledges receivable and has determined that an allowance for potential uncollectible amounts is not necessary.

Note 3 FUND ACCOUNTING

The financial statements of the Foundation are reported in self-balancing fund groups as follows:

Unrestricted Fund-

The unrestricted fund is part of the net assets of the Foundation that are not subject to donor-imposed stipulations. The only limits on unrestricted net assets are broad limits resulting from the nature of the Foundation and the purposes specified in its articles of incorporation or bylaws and, perhaps, limits resulting from contractual agreements.

THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013

Note 3 FUND ACCOUNTING (CONT.)

Temporarily Restricted Fund-

The temporarily restricted fund is part of the net assets of the Foundation resulting from contributions and other inflows of assets whose use by the Foundation is limited by donor imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Foundation pursuant to those stipulations. The majority of contributions with restrictions are stipulated to be used as funds for educating Americans in the basic principles of the classical liberal/libertarian political philosophy. The use and nature of these contributions can result in a continually increasing balance in temporarily restricted net assets.

Permanently Restricted Fund-

The permanently restricted fund is used to record resources received that are permanently restricted as to use by the donor or grantor.

Note 4 FUNCTIONAL ALLOCATION OF EXPENSES

In accordance with FASB ASC Number 958-720-45 the costs of providing the program and the supporting services 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 between the program and the supporting services in reasonable ratios determined by management.

Note 5 CASH AND CASH EQUIVALENTS

The cash balance includes money market funds that earn interest at a rate which fluctuates according to prime and are carried at cost which approximates market. The cash balance is comprised of the following:

Checking and savings	\$	801,917
Money market funds		104,273
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Total cash and cash equivalents	\$	<u>906,190</u>

THE REASON FOUNDATION
 NOTES TO FINANCIAL STATEMENTS
 SEPTEMBER 30, 2013

Note 6 INVESTMENTS

The Foundation's investments are reported at fair value in the accompanying statements of financial position for September 30, 2013.

	<u>Fair Value Measurements Using:</u>
	Quoted Prices in Active Markets for Identical Assets (Level 1)
Mutual funds	
Common Stock	\$ 1,369,246
Bond funds	1,508,170
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Total investments	\$ 2,877,416
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FASB ASC Number 820-10 defines fair value, establishes a framework for measuring fair value, and expands disclosure about fair value measurements. This standard provides a consistent definition of fair value which focuses on an exit price between market participants in an orderly transaction, prioritizes the use of market based information over entity specific information and establishes a three level hierarchy for fair value measurements based on the transparency of information used in the valuation of an asset or liability as of the measurement date.

Fair values determined by Level 1 inputs utilize quoted prices in active markets for identical assets. Fair values determined by level 2 inputs utilize data points that are observable such as quoted prices, interest rates and yield curves. Fair values determined by level 3 inputs are unobservable data points for the asset and include situations where there is little, if any, market activity for the asset. There were no level 2 or 3 inputs as of September 30, 2013.

Note 7 MAILING LISTS

The Foundation has developed a mailing list of its subscribers during the course of its operations. For the year ended September 30, 2013, rentals of this list to certain list brokers generated revenue of \$16,311.

THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013

Note 8 UNEARNED SUBSCRIPTIONS

Deferred revenue from prepaid magazine subscriptions is recognized as revenue over the term of the subscriptions. At September 30, 2013, the unearned portion of subscription revenue was as follows:

Unearned subscriptions	\$	373,099
Less: current portion		<u>(278,524)</u>
Long-term portion	\$	<u>94,575</u>

The long-term portion of the unearned subscriptions expires principally through the year ending September 30, 2015.

Note 9 LINE OF CREDIT

The Foundation maintains a \$200,000 line of credit with a bank, collateralized by index, inventory, and chattel paper, accounts, equipment and general intangibles, which expires July 27, 2014. Interest accrues at the Index rate plus 3.9%. There was no outstanding balance at September 30, 2013.

Note 10 MORTGAGE PAYABLE

The Foundation has a mortgage note payable in the amount of \$1,200,000. This note is secured by real property. This note is subject to an interest rate per anum of 3.73%. The monthly payment is \$12,030 including interest. This note matures on July 27, 2022. In conjunction with the note, the foundation has agreed to a number of the lender's covenants. As of September 30, 2013, the company is not aware of any violations of the covenants.

At September 30, 2013	\$	869,517
Less: current portion		<u>(112,238)</u>
Long-term portion	\$	<u>757,279</u>

THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013

Note 10 MORTGAGE PAYABLE (CONT.)

Maturities of long term debt as of September 30, 2013 for the succeeding years are as follows:

<u>Years ended September 30,</u>		
2014	\$	112,238
2015		115,530
2016		118,947
2017		122,494
2018		126,175
Thereafter		<u>274,133</u>
	\$	<u><u>869,517</u></u>

Note 11 COMMITMENTS

The Foundation leases office space in Washington, District of Columbia, expiring April 30, 2023. The Foundation has an automobile lease expiring September 9, 2014. Future minimum annual rental payments under these lease agreements are as follows:

<u>Year Ending September 30,</u>	<u>Washington Office</u>	<u>Automobile</u>	<u>Total</u>
2014	\$ 178,945	\$ 5,005	\$ 183,950
2015	183,420	-	183,420
2016	188,012	-	188,012
2017	192,718	-	192,718
2018	197,524	-	197,524
Thereafter	<u>969,764</u>	-	<u>969,764</u>
Totals	<u>\$ 1,910,383</u>	<u>\$ 5,005</u>	<u>\$ 1,915,388</u>

Rental expense for the year ended September 30, 2013, amounted to \$302,540.

THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013

Note 12 RESTRICTED NET ASSETS

The restricted net assets are available for the various programs for the following purposes:

Temporarily Restricted Funds:

Magazine	\$ 82,530
Donor restricted funds	<u>214,336</u>
Total	<u>\$ 296,866</u>

Permanently Restricted Fund:

Donor restricted investments in perpetuity, income is expendable to support general operations.	<u>\$ 44,279</u>
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Note 13 NET ASSETS RELEASED FROM RESTRICTION

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrences of other events specified by donors.

Purpose/ Time Restrictions Accomplished:

Magazine	<u>\$ 41,944</u>
Total	<u>\$ 41,944</u>

Note 14 TAX-SHELTERED RETIREMENT PLAN

Any full time employee of the Foundation may set up a tax-sheltered retirement plan in accordance with Section 403(b) of the Internal Revenue Code. The Foundation assists the employee in setting up the plan and will arrange for the contributions to be made through payroll deductions. The Foundation does not make contributions to such plans.

THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013

Note 15 CONCENTRATION OF CREDIT RISK

Financial instruments which potentially subject the Foundation to concentrations of credit risk consist of cash and cash equivalents, investments, accounts receivable and pledges receivable. The Foundation places its cash and money market funds principally with a high credit quality financial institution where the funds are guaranteed by the Federal Deposit Insurance Corporation (FDIC). At times, such cash and money market fund balances may be in excess of the FDIC insurance limits. Management of the Foundation regularly reviews the financial stability of its cash and money market fund depository and deems the risk of loss due to these concentrations to be minimal. Management of the Foundation has assessed the credit risk associated with the investments held at September 30, 2013, and has determined that an allowance for potential losses due to credit risk in the investment portfolio is not necessary. At September 30, 2013, all accounts exceeded the FDIC limits.

Note 16 ACCOUNTING FOR UNCERTAINTY IN INCOME TAXES

The Foundation is exempt from taxation under Internal Revenue Code Section 501 (c) (3) and California Revenue and Taxation Code Section 23701(d). The Foundation is subject to a 2% (1% if certain criteria are met) federal excise tax on net investment income.

As required by FASB ASC Number 740-10, "Accounting for Uncertainty in Income Taxes," the Foundation recognizes the effect of income tax positions only if those positions are more likely than not (>50%) of being sustained. Management of the Foundation does not believe the financial statements include any uncertain tax positions. The Foundation's returns are subject to examination by federal and state taxing authorities, generally for three and four years, respectively, after they are filed.

Note 17 DONOR DESIGNATED ENDOWMENT

The Foundation's endowment consists of a fund established to create a permanent endowment. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

THE REASON FOUNDATION
NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2013

Note 17 DONOR DESIGNATED ENDOWMENT (CONT.)

The Board of Trustees of the Foundation has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

The investment committee has recommended the following investment policy which includes the endowment fund. This policy was adopted by the full Board of Trustees. Net assets are to be invested 70% in fixed income and 30% in equities. The spending policy is to allow distribution of an amount equal to 5% of the fair market value of the endowment fund. In any year in which the endowment experiences a net investment loss, no distributions will be made.

Endowment Net Asset Composition by Type of Fund as of September 30, 2013 is as follows:

	Permanently Restricted
Donor-restricted endowment funds	\$ 44,279
Total funds	\$ <u>44,279</u>

Changes in endowment net assets as of September 30, 2013 are as follows:

	Permanently Restricted
Endowment net assets, beginning of year	\$ 44,279
Contributions	-
Investment income	-
Net appreciation (depreciation)	-
Amounts appropriated for expenditure	-
Endowment net assets, end of year	\$ <u>44,279</u>