MIND RESEARCH INSTITUTE

FINANCIAL STATEMENTS

DECEMBER 31, 2013 AND 2012

TABLE OF CONTENTS

Guzman & Gray

Certified Public Accountants

4510 East Pacific Coast Highway, Suite 270
Long Beach, California 90804
(562) 498-0997 Fax: (562) 597-7359

Mark Gray, C.P.A.
Patrick S. Guzman, C.P.A.

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
of MIND Research Institute

We have audited the accompanying financial statements of MIND Research Institute (a nonprofit organization), which comprise the financial position as of December 31, 2013, and the related statements of activities and changes in net assets, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements. The prior year summarized comparative information has been derived from the Organization's financial statements for the year ended December 31, 2012 and in our report dated April 16, 2013 we expressed an unmodified opinion on those 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.

Auditors' 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 audits 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 auditors' 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 Organization'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 Organization'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.

Auditors' Responsibility (Continued)

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 MIND Research Institute as of December 31, 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.

Guzman & Gray

GUZMAN & GRAY
Long Beach, CA
April 15, 2014

MIND RESEARCH INSTITUTE
STATEMENT OF FINANCIAL POSITION

DECEMBER 31, 2013 AND 2012

ASSETS

	December 31, 2013	December 31, 2012
CURRENT ASSETS		
Cash and cash equivalents	$ 1,538,962	$ 1,918,867
Marketable securities		8,298
Accounts receivable	2,052,826	628,288
Pledges receivable	326,893	1,241,130
Prepaid expenses	205,100	135,921
Total Current Assets	4,123,781	3,932,504
FIXED ASSETS		
Equipment, furniture, and leasehold improvements	4,036,683	2,706,115
Less: accumulated depreciation	(1,503,224)	(1,098,829)
Total Fixed Assets, net	2,533,459	1,607,286
OTHER ASSETS		
Pledges receivable, noncurrent	328,013	343,844
Deposit	62,029	80,544
Intangible assets, net	501,552	389,967
Total Other Assets	891,594	814,355
TOTAL ASSETS	7,548,834	6,354,145

LIABILITIES AND NET ASSETS

	2013	2012
CURRENT LIABILITIES		
Accounts payable	507,895	593,958
Accrued expenses	837,689	359,432
Deferred revenue, current	404,884	243,002
Deferred rent, current	22,404	
Note payable, current	5,904	
Total Current Liabilities	1,778,776	1,196,392
NONCURRENT LIABILITIES		
Deferred revenue, net of current	163,003	326,006
Deferred rent, net of current	767,911	677,250
Note payable, net of current	45,551	
Total Noncurrent Liabilities	976,465	1,003,256
NET ASSETS		
Unrestricted	4,107,438	3,540,136
Temporarily restricted	686,155	614,361
Total Net Assets	4,793,593	4,154,497
TOTAL LIABILITIES AND NET ASSETS	$ 7,548,834	$ 6,354,145

See independent auditors' report and notes to the financial statements

MIND RESEARCH INSTITUTE
STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

FOR THE YEAR ENDED DECEMBER 31, 2013
WITH COMPARATIVE TOTALS FOR THE YEAR ENDED DECEMBER 31, 2012

	Unrestricted	Temporarily Restricted	December 31, 2013	December 31, 2012
REVENUE AND SUPPORT				
Gross school sales	$ 20,066,926	$	$ 20,066,926	$ 15,899,090
Less contributions and sponsorships	(1,192,078)		(1,192,078)	(1,280,900)
Total Nonsponsored School Sales	18,874,848		18,874,848	14,618,190
Contributions	3,437,190	372,312	3,809,502	4,789,153
Special events, net	538,687		538,687	453,316
In-kind revenues	1,074,462		1,074,462	19,056
Total Development and Fundraising	5,050,339	372,312	5,422,651	5,261,525
Gain (loss) on sale of securities	232		232	(72)
Total Other Support	232		232	(72)
Net Assets Released from restrictions	300,518	(300,518)		
TOTAL REVENUE AND SUPPORT	24,225,937	71,794	24,297,731	19,879,643
EXPENSES				
Program	20,391,330		20,391,330	16,276,528
Management	1,267,883		1,267,883	607,089
Fundraising	1,999,422		1,999,422	2,017,519
TOTAL EXPENSES	23,658,635		23,658,635	18,901,136
CHANGE IN NET ASSETS	567,302	71,794	639,096	978,507
BEGINNING NET ASSETS	3,540,136	614,361	4,154,497	3,175,990
ENDING NET ASSETS	$ 4,107,438	$ 686,155	$ 4,793,593	$ 4,154,497

MIND RESEARCH INSTITUTE

STATEMENT OF FUNCTIONAL EXPENSES

FOR THE YEAR ENDED DECEMBER 31, 2013

WITH COMPARATIVE TOTALS FOR THE YEAR ENDED DECEMBER 31, 2012

	Program					December 31,	
	Education	Research	Total	Management	Fundraising	2013	2012
WAGES AND BENEFITS							
Salaries	$ 12,785,810	$ 249,983	$ 13,035,793	$ 976,204	$ 1,280,441	$ 15,292,438	$ 11,666,584
Benefits	954,743	24,181	978,924	38,103	105,020	1,122,047	919,200
Payroll taxes	923,666	18,141	941,807	60,600	97,375	1,099,782	803,701
Total Wages and Benefits	14,664,219	292,305	14,956,524	1,074,907	1,482,836	17,514,267	13,389,485
OTHER EXPENSES							
Travel, meals, & entertainment	1,373,806	35,391	1,409,197	27,135	71,249	1,507,581	1,396,734
Outside services	917,661	124,009	1,041,670	15,553	111,736	1,168,959	1,201,188
Rent	814,860	14,743	829,603	37,594	63,870	931,067	741,665
Depreciation & amortization	462,437	9,485	471,922	20,030	41,043	532,995	358,713
Conferences & meetings	360,597	262	360,859	3,117	17,061	381,037	409,112
Telecommunications	306,429	584	307,013	4,847	5,858	317,718	306,692
Accounting & legal	153,147	1,533	154,680	64,875	16,598	236,153	112,918
Printing & publishing	166,879	82	166,961	2,109	30,058	199,128	145,650
ERP system	159,998	3,285	163,283	6,597	13,246	183,126	
Subscriptions	124,794	11	124,805	724	18,862	144,391	76,831
Public relations & advertising	141,480		141,480			141,480	350,139
Special event awards dinner					83,798	83,798	94,756
Postage & shipping	67,050	254	67,304	2,367	3,879	73,550	53,526
Bank fees	34,117	470	34,587	1,690	22,713	58,990	34,377
Interest expense	50,064	1,054	51,118	2,214	4,514	57,844	43,328
Business insurance	24,656	476	25,132	1,047	2,294	28,473	15,560
Payroll processing fees	11,832	239	12,071	515	1,061	13,647	11,358
Dues & memberships					6,094	6,094	21,962
Software maintenance	2,945		2,945			2,945	
Licenses & permits	311	4	315	812	29	1,156	3,903
Other	68,907	954	69,861	1,750	2,623	74,236	133,239
Total Other Expenses	5,241,970	192,836	5,434,806	192,976	516,586	6,144,368	5,511,651
TOTAL EXPENSES	$ 19,906,189	$ 485,141	$ 20,391,330	$ 1,267,883	$ 1,999,422	$ 23,658,635	$ 18,901,136

See independent auditors' report and notes to financial statements

MIND RESEARCH INSTITUTE
STATEMENT OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

	December 31, 2013	December 31, 2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in Net Assets	$ 639,096	$ 978,507
Adjustments to reconcile changes in net assets to net cash provided from operating activities		
Depreciation and amortization	532,995	358,713
Loss (gain) on sale of marketable securities	(232)	72
Donation of marketable securities		(8,298)
Donation of equipment	(1,055,406)	
Loss on disposal of equipment	41,019	
(Increase) decrease in assets:		
Accounts receivable	(1,424,538)	267,632
Pledge receivables	930,068	(622,241)
Prepaid expenses	(69,179)	(50,191)
Inventory		73,140
Deposits	18,515	(57,170)
Increase (decrease) in liabilities:		
Accounts payable	(86,063)	221,287
Accrued expenses	478,257	222,087
Deferred revenues	(1,121)	501,742
Deferred rent	113,065	677,250
Net Cash From Operating Activities	116,476	2,562,530
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale of marketable securities	8,530	12,366
Purchase of fixed assets	(421,410)	(1,059,335)
Acquisition of intangible assets	(134,956)	(37,210)
Net Cash From Investing Activities	(547,836)	(1,084,179)
CASH FLOWS FROM FINANCING ACTIVITIES		
Issuance of note payable	51,455	
Net Cash From Investing Activities	51,455	
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(379,905)	1,478,351
BEGINNING CASH AND CASH EQUIVALENTS	1,918,867	440,516
ENDING CASH AND CASH EQUIVALENTS	$ 1,538,962	$ 1,918,867
SUPPLEMENTARY INFORMATION		
Interest paid	$ 57,844	$ 43,328
Income taxes paid	NONE	NONE

See independent auditors' report and notes to financial statements

NOTE 1 – ORGANIZATION

The MIND Research Institute (The “Institute”) is a nonprofit tax exempt organization which was incorporated in April 1998. It enables elementary and primary students to reach their full academic and career potential through developing and deploying math instructional software and systems. A non-profit organization, MIND also conducts basic neuroscientific, mathematics, and education research to improve math education and advance scientific understanding.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The financial statements of the Organization have been prepared on the accrual basis.

Basis of Presentation

The Organization reports information regarding their 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 – Net assets that are not subject to donor imposed restrictions and that may be expendable for any purpose in performing the primary objectives of the Organization.
>
> Temporarily restricted net assets – Net assets subject to donor-imposed stipulations that can be fulfilled by actions of the Organization pursuant to those stipulations or that expire by the passage of time. Temporarily restricted resources whose restrictions are met in the same reporting period are recorded as unrestricted.
>
> Permanently restricted net assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the Organization.

Accounting 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. Actual results could differ from those estimates.

Cash and Cash Equivalents

For the purpose of the statement of cash flows, the Organization considers cash on hand and cash in other depository institutions with an original maturity of three months or less to be cash equivalents.

Marketable Securities

Marketable securities are stated at fair market value. Contributed securities are recorded at their market value on the date of donation. Net realized and unrealized gains and losses are reflected in the statement of activities.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accounts Receivable
Accounts receivable consist of sales of educational programs. No allowance for bad debts has been provided as management believes all accounts are collectible.

Pledges Receivable
Unconditional promises to give are recognized in the period received and when collectability is reasonably assured. Conditional promises to give are recognized only when the conditions on which they depend are substantially met and the promises become unconditional. Pledges to be received in more than one year are discounted to net present value based on the Wall Street Journal prime rate.

No allowance for uncollectable amounts has been established as management believes the all receivables to be fully collectible.

Textbook Inventory
Inventory consists of educational materials. Inventory is valued at the lower of cost or market. Sale of inventory is recorded on the first-in-first-out method. The Organization assesses inventory for damaged or obsolete materials. During 2012, the Organization determined the inventory was obsolete and expensed remaining balance. As of December 31, 2013 and 2012, there was no inventory.

Equipment, Furniture, and Leasehold Improvements
Equipment, furniture, and leasehold improvements are carried at cost or, if donated, at the approximate fair value at the date of donation. Depreciation is provided on the straight-line method over estimated useful lives. Additions and improvements that increase the capacity or lengthen the useful lives of the assets are capitalized. Repairs and maintenance are expensed as incurred.

Intangible Assets
Patent and trademark application costs are capitalized. When a patent is approved, it is amortized on the straight-line method over estimated useful live.

Revenue and Support
Revenue primarily consists of contributions and sales of educational materials. Contributions are recognized when the donor makes a promise to give that is, in substance, unconditional. All contributions are considered to be unrestricted unless specifically restricted by the donor. Sales are recognized after the product has been delivered to the customer and training has been provided or upon license renewal.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Donated Services and Goods

The Organization recognizes the contribution of services if the services received require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. Contributed services that do not meet the criteria shall not be recognized.

Donated goods are recorded as contributions at their estimated fair value at the date of donation. Such donations are reported as increases in unrestricted net assets unless the donor has restricted the donated goods to a specific purpose.

Functional Allocation of Expenses

The costs of providing the various programs and activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Computer Software Development Costs

All computer software development costs are considered research and development activities and are expensed as incurred.

Income Tax Status

The Organization is exempt from income taxes under Internal Revenue Code Section 501(c)(3) and California Revenue Code Section 23701(d). The Organization is classified by the Internal Revenue Service as an entity that is not a private foundation within the meaning of Section 509(a) and qualifies for deductible contributions as provided in Section 170(c)(2). Income for certain activities not directly related the Organization's tax-exempt purpose is subject to unrelated business income taxation.

The Organization evaluates uncertain tax positions whereby the effect of the uncertainty would be recorded if the tax positions will more likely than not be sustained upon examination. As of December 31, 2013, management does not believe the Organization has any uncertain tax positions requiring accrual or disclosure. The Organization is subject to potential income tax audits on open tax years by any taxing jurisdiction in which it operates. The statute of limitations for federal and California state purposes is generally three and four years, respectively.

Reclassifications

Certain reclassifications have been made to the 2012 financial statements to conform to the 2013 presentation.

Reporting of Subsequent Events

In preparing these financial statements, the Organization has evaluated events and transactions for potential recognition or disclosure through April 15, 2014, the date the financial statements were available to issue.

NOTE 3 – FAIR VALUE MEASUREMENTS

Generally accepted accounting principles establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. The fair value hierarchy is as follows:

Level 1: Quoted prices in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to level 1 inputs.

Level 2: Observable prices that are based on inputs not quoted on active markets, but corroborated by market data.

Level 3: Inputs that are unobservable and based on the Organization's assumptions, estimates, and internally developed inputs. The fair value hierarchy gives lowest priority to level 3 inputs.

The level in the fair value hierarchy within which a fair measurement in its entirety falls is based on the lowest level input that is significant to the fair measurement in its entirety.

Fair values measured on a recurring basis
The carrying values of marketable securities as of December 31, 2013 are as follows:

	Fair Value Measurements at December 31, 2013			
	Level 1	Level 2	Level 3	Total
Pledges receivable, net	$	$ 654,906	$	$ 654,906

The carrying values of marketable securities as of December 31, 2012 are as follows:

	Fair Value Measurements at December 31, 2012			
	Level 1	Level 2	Level 3	Total
Equity securities	$ 8,298	$	$	$ 8,298
Pledges receivable, net		1,584,974		1,584,974
	$ 8,298	$ 1,584,974	$	$ 1,593,272

The carrying value of cash and cash equivalents are reasonable estimates of fair value due to their short term nature and are not presented in the tables presented above.

NOTE 4 – PLEDGE RECEIVABLES

Pledges receivable as of December 31 are as follows:

	December 31,	
	2013	2012
Receivable in less than one year	$ 326,893	$ 1,241,130
Receivable in one to five years	367,500	390,010
	694,393	1,631,140
Less present value discounts	(39,487)	(46,166)
	654,906	1,584,974
Less current portion	(326,893)	(1,241,130)
Noncurrent portion	$ 328,013	$ 343,844

NOTE 5 – EQUIPMENT, FURNITURE, AND LEASEHOLD IMPROVEMENTS

A summary of equipment, furniture, and leasehold improvements as of December 31 is as follows:

	December 31,	
	2013	2012
Equipment	$ 2,741,436	$ 1,657,006
Furniture	351,346	286,415
Leasehold improvements	943,901	762,694
	4,036,683	2,706,115
Less: accumulated depreciation	(1,503,224)	(1,098,829)
	$ 2,533,459	$ 1,607,286

For the years ended December 31, 2013 and 2012, depreciation expense recognized was $509,623 and $335,341, respectively.

NOTE 6 – INTANGIBLE ASSETS

A summary of intangible assets as of December 31 is as follows:

	December 31, 2013	December 31, 2012
Patent costs	$ 597,854	$ 462,897
Less: accumulated depreciation	(96,302)	(72,930)
	$ 501,552	$ 389,967

For the years ended December 31, 2013 and 2012, amortization expense recognized was $23,372 and $23,372, respectively.

NOTE 7 – DEFERRED REVENUE

Deferred revenue represents sales of educational materials collected but not yet earned. As of December 31, 2013 and 2012, deferred revenue balances were $567,887 and $569,008, respectively.

NOTE 8 – NOTE PAYABLE

During January 2013, the Organization acquired a note payable to finance tenant improvements to its office facility. The note is secured by the Organization's assets and matures in December 2020. The note bears an interest rate of 7 percent. As of December 31, 2013, the outstanding balance is $51,455. For the year ended December 31, 2013, the Organization incurred interest expense and fees of $3,813.

NOTE 9 – LINE OF CREDIT

During March 2013, the Organization renewed its line of credit with a financial institution for up to $3,700,000. The line of credit is secured by the Organization's assets and matures in May 2014. The line of credit bears a variable interest rate based on the Wall Street Journal prime rate plus one percent. As of December 31, 2013, the line of credit interest rate was 5.75 percent. The line of credit requires minimum monthly payments on interest incurred and requires payment of all outstanding balances upon maturity. As of December 31, 2013 and 2012, there was no outstanding balance. For the years ended December 31, 2013 and 2012, the Organization incurred interest expense and fees of $57,844 and $43,328, respectively.

NOTE 10 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following for the years ended December 31:

	December 31, 2013	December 31, 2012
Time restricted	$ 526,155	$ 614,361
Purpose restricted	160,000	
	$ 686,155	$ 614,361

Net assets were released from donor restrictions either by incurring expenses, which satisfied the restricted purposes or by the occurrences of other events specified by donors during the years ended December 31, 2013 and 2012.

NOTE 11 – SPECIAL EVENTS

The Institute conducts special events in order to raise funds to support operations and various programs. Revenues and donor benefit expenses relating to special events for the years ended December 31, 2013 and 2012 are as follows:

	December 31, 2013	December 31, 2012
Revenues	$ 594,111	$ 506,096
Less direct donor benefits	(55,424)	(52,780)
	$ 538,687	$ 453,316

NOTE 12 – IN-KIND GOODS AND SERVICES

Many individuals volunteer their time and perform a variety of tasks that assist the Institute. For the years ended December 31, 2013 and 2012, no amounts have been recognized in the statement of activities as they have not met the criteria described in Note 2.

The Institute receives donated materials, equipment, and storage space. For the years ended December 31, 2013 and 2012, the Institute recognized in-kind revenues of $1,074,462 and $19,506, respectively.

NOTE 13 – RELATED PARTY TRANSACTIONS

For the years ended December 31, 2013 and 2012, the Institute received contributions from members of the Institute's board of directors or business or charitable entities related to them totaling $483,160 and $484,525, respectively.

The Institute was provided with inventory storage space by an entity owned by a member of the Institute's board of directors. For the years ended December 31, 2013 and 2012, the Institute recognized in-kind rent of $19,056 and $19,056, respectively.

NOTE 14 – INTEREST IN SUBSIDIARY CORPORATION

The Institute holds a 98% investment interest in a corporation named MIND Education, Inc. For the years ended December 31, 2013 and 2012, the corporation had no activity.

NOTE 15 – LEASE COMMITMENT

During September 2012, the Institute entered into a lease agreement for office space located in Irvine, California beginning in January 2013. The term of the lease extends through December 2020 and requires minimum monthly rent payments of $50,056. The lease includes certain tenant improvements and rent abatement during the lease period. As of December 31, 2013 and 2012, the Institute recorded deferred rent of $790,315 and $677,250, respectively. For the years ended December 31, 2013 and 2012, rent expense was $738,585 and $406,171, respectively.

The Institute also leases a storage facility and office equipment with maturities ranging from August 2013 to December 2018.

Future minimum lease payments for the years ending December 31 are as follows:

Year Ended December 31,	
2014	$ 760,056
2015	790,308
2016	801,793
2017	812,868
2018 and after	2,357,192
	$ 5,522,217

NOTE 16 – CONCENTRATION OF CREDIT RISK

For the years ended December 31, 2013 and 2012, the Institute received 22 percent and 26 percent of its revenue from development and fundraising. Management anticipates continued support from its contributors in the future to be a substantial portion of the Institutes' revenue.

Cash deposits in financial institutions may exceed federally insured limits at times during the year. As of December 31, 2013, the cash and cash equivalents held at financial institutions in excess of the FDIC insurance amount of $250,000 was $890,997. As of December 31, 2012, the cash and cash equivalents held at financial institutions did not exceed the FDIC insurance amount of $250,000. Cash deposited in financial institutions differs from cash presented in the statement of financial position due to timing differences.