

**Houston Zoo, Inc.**

Financial Statements  
and Independent Auditors' Report  
for the years ended December 31, 2017 and 2016

**Independent Auditors' Report**

To the Board of Directors of  
Houston Zoo, Inc.:

We have audited the accompanying financial statements of Houston Zoo, Inc., which comprise the statements of financial position as of December 31, 2017 and 2016 and the related statements of activities and of 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.

**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 our audits 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 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 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 Houston Zoo, Inc. as of December 31, 2017 and 2016 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.

*Blazek & Vetterling*

May 21, 2018



## Houston Zoo, Inc.

### Statement of Activities for the year ended December 31, 2017

	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>PERMANENTLY RESTRICTED</u>	<u>TOTAL</u>
<b>REVENUE:</b>				
Contributions	\$ 3,511,345	\$ 21,739,280	\$ 4,000	\$ 25,254,625
Membership contributions	7,235,871			7,235,871
Special events	932,901	690,508		1,623,409
Cost of benefits provided to donors	(227,288)	(149,126)		(376,414)
City management fee <i>(Note 2)</i>	9,837,416			9,837,416
Admission fees	14,600,067			14,600,067
Concession contract income	3,735,310			3,735,310
Guest program fees	7,484,121			7,484,121
Educational program fees	1,052,942			1,052,942
Investment return, net <i>(Note 5)</i>	865,147	852,553	4,095	1,721,795
Other income	<u>502,802</u>			<u>502,802</u>
Total revenue	49,530,634	23,133,215	8,095	72,671,944
<b>Net assets released from restrictions:</b>				
Capital expenditures	3,201,329	(3,201,329)		
Program expenses	1,533,269	(1,533,269)		
Expiration of time restrictions	<u>742,591</u>	<u>(742,591)</u>		
Total	<u>55,007,823</u>	<u>17,656,026</u>	<u>8,095</u>	<u>72,671,944</u>
<b>EXPENSES:</b>				
<b>Zoo programs:</b>				
Exhibition facility operations	19,836,655			19,836,655
Depreciation	8,320,648			8,320,648
Education and conservation programs	5,411,740			5,411,740
Admissions and guest relations	4,255,783			4,255,783
Guest program events	<u>2,650,840</u>			<u>2,650,840</u>
Total zoo programs	40,475,666			40,475,666
Advertising and marketing costs	2,361,915			2,361,915
Membership development	1,765,010			1,765,010
Management and general	2,142,799			2,142,799
Fundraising	<u>2,050,798</u>			<u>2,050,798</u>
Total expenses	<u>48,796,188</u>			<u>48,796,188</u>
<b>CHANGES IN NET ASSETS</b>	6,211,635	17,656,026	8,095	23,875,756
Net assets, beginning of year	<u>128,877,100</u>	<u>12,052,050</u>	<u>3,518,004</u>	<u>144,447,154</u>
Net assets, end of year	<u>\$ 135,088,735</u>	<u>\$ 29,708,076</u>	<u>\$ 3,526,099</u>	<u>\$ 168,322,910</u>

*See accompanying notes to financial statements.*

## Houston Zoo, Inc.

### Statement of Activities for the year ended December 31, 2016

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	<u>UNRESTRICTED</u>	<u>TEMPORARILY RESTRICTED</u>	<u>PERMANENTLY RESTRICTED</u>	<u>TOTAL</u>
REVENUE:				
Contributions	\$ 3,449,600	\$ 4,499,823	\$ 4,000	\$ 7,953,423
Membership contributions	7,293,169			7,293,169
Special events	1,097,772	1,111,306		2,209,078
Cost of benefits provided to donors	(271,135)	(151,296)		(422,431)
City management fee (Note 2)	9,634,482			9,634,482
Admission fees	15,474,111			15,474,111
Concession contract income	3,435,767			3,435,767
Guest program fees	7,731,662			7,731,662
Educational program fees	805,090			805,090
Investment return, net (Note 5)	303,983	309,483	1,486	614,952
Other income	<u>831,752</u>			<u>831,752</u>
Total revenue	49,786,253	5,769,316	5,486	55,561,055
Net assets released from restrictions:				
Program expenses	1,459,170	(1,459,170)		
Expiration of time restrictions	<u>811,984</u>	<u>(811,984)</u>		
Total	<u>52,057,407</u>	<u>3,498,162</u>	<u>5,486</u>	<u>55,561,055</u>
EXPENSES:				
Zoo programs:				
Exhibition facility operations	19,939,038			19,939,038
Depreciation	7,432,171			7,432,171
Education and conservation programs	5,285,954			5,285,954
Admissions and guest relations	4,777,388			4,777,388
Guest program events	<u>2,581,570</u>			<u>2,581,570</u>
Total zoo programs	40,016,121			40,016,121
Advertising and marketing costs	2,160,056			2,160,056
Membership development	2,071,867			2,071,867
Management and general	2,524,379			2,524,379
Fundraising	<u>1,824,924</u>			<u>1,824,924</u>
Total expenses	<u>48,597,347</u>			<u>48,597,347</u>
CHANGES IN NET ASSETS	3,460,060	3,498,162	5,486	6,963,708
Net assets, beginning of year	<u>125,417,040</u>	<u>8,553,888</u>	<u>3,512,518</u>	<u>137,483,446</u>
Net assets, end of year	<u>\$ 128,877,100</u>	<u>\$ 12,052,050</u>	<u>\$ 3,518,004</u>	<u>\$ 144,447,154</u>

*See accompanying notes to financial statements.*

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## Houston Zoo, Inc.

### Statements of Cash Flows for the years ended December 31, 2017 and 2016

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	<u>2017</u>	<u>2016</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Changes in net assets	\$ 23,875,756	\$ 6,963,708
Adjustments to reconcile changes in net assets to net cash provided by operating activities:		
Depreciation	8,320,648	7,432,171
Net realized and unrealized gain on investments	(1,278,583)	(61,503)
Contributions restricted for capital acquisitions	(20,422,458)	(2,872,053)
Contributions to permanent endowment funds	(4,000)	(4,000)
Changes in operating assets and liabilities:		
Concessionaire and other receivables	(13,504)	33,773
Accounts receivable from the City of Houston	(2,500,000)	
Prepaid expenses and other assets	136,104	(72,503)
Operating pledges receivable	723,041	(353,854)
Accounts payable	230,276	318,605
Accrued salaries and benefit costs	66,119	215,030
Funds held for others	(717,764)	740,184
Deferred revenue	<u>284,020</u>	<u>(199,917)</u>
Net cash provided by operating activities	<u>8,699,655</u>	<u>12,139,641</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(14,324,976)	(13,484,370)
Purchases of investments	(11,810,107)	(27,426,614)
Proceeds from sale of investments	10,802,215	26,076,336
Net change in money market mutual funds held as investments	<u>550,886</u>	<u>(218,693)</u>
Net cash used by investing activities	<u>(14,781,982)</u>	<u>(15,053,341)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Repayment of note payable		(559,000)
Proceeds from contributions restricted for capital acquisitions	7,635,550	3,475,065
Proceeds from contributions received for permanent endowment funds	<u>4,000</u>	<u>4,000</u>
Net cash provided by financing activities	<u>7,639,550</u>	<u>2,920,065</u>
<b>NET CHANGE IN CASH</b>	1,557,223	6,365
Cash, beginning of year ( <i>Note 3</i> )	<u>22,467,971</u>	<u>22,461,606</u>
Cash, end of year ( <i>Note 3</i> )	<u>\$ 24,025,194</u>	<u>\$ 22,467,971</u>
<i>Supplemental disclosure of cash flow information:</i>		
Interest paid		\$1,448
Contribution of marketable securities	\$1,331,050	\$391,990

*See accompanying notes to financial statements.*

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## Houston Zoo, Inc.

Notes to Financial Statements for the years ended December 31, 2017 and 2016

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### NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization – Approximately 90 years ago, the City of Houston (the City) created a zoo program and facility to benefit the citizens of Houston and surrounding areas. In 2002, the zoo was privatized by order of the City and operates as Houston Zoo, Inc. (the Houston Zoo).

The Houston Zoo is a conservation, education, and recreation organization dedicated to the reproduction, protection, and exhibition of animals in their habitats. The Houston Zoo provides a fun, unique and inspirational experience fostering appreciation, knowledge and care for the natural world.

Federal income tax status – The Houston Zoo is exempt from federal income tax under §501(c)(3) of the Internal Revenue Code and is classified as a public charity under §509(a)(2).

Cash – Bank deposits exceed the federally insured limit per depositor per institution.

Pledges receivable that are expected to be collected within one year are reported at net realizable value. Pledges receivable that are expected to be collected in future years are discounted to estimate the present value of future cash flows.

Allowance for uncollectible accounts – An allowance for accounts receivable or pledges receivable is provided when it is believed accounts may not be collected in full. The Houston Zoo's policy is to write off receivables against the allowance when management determines the receivable will not be collected. The amount of bad debt expense or loss on pledges recognized each period and the resulting adequacy of the allowance at the end of each period are determined using a combination of historical loss experience and analysis of individual balances each period. Management's estimates regarding the collectability of the balances could change in the near term resulting in a change in the carrying value of these receivables.

Investments are reported at fair value. Investment return is reported in the statement of activities as an increase in unrestricted net assets unless the use is limited by donor-imposed restrictions. Investment return whose use is restricted by the donor is reported as an increase in temporarily or permanently restricted net assets.

Property and equipment are reported at cost, if purchased, or at fair value at the date of gift, if donated. The Houston Zoo capitalizes property and equipment that has a cost or fair value of \$5,000 or greater and an estimated useful life of more than one year. The Houston Zoo recognizes depreciation using the straight-line method over the estimated useful lives of the assets, ranging from 3 to 25 years.

Animal and horticultural collections – In accordance with industry practice, the Houston Zoo does not capitalize animal and horticultural collections; acquisitions are reported as expenditures in the period of acquisition. The Houston Zoo is responsible for the health and welfare of its animal and horticultural collections. The Houston Zoo maintains records of its collections and any exchanges with other organizations. Under the direction of the Board of Directors, the President, and the curatorial staff, collections continue to be cared for, used, and expanded. In 2017 and 2016, the Houston Zoo expended approximately \$25,000 and \$91,000, respectively, to expand its collections.

In an ongoing commitment to enhance worldwide reproduction and conservation of animals, the Houston Zoo exchanges animals with other organizations. Consistent with industry practice, the Houston Zoo does not record any liability for such exchange arrangements as generally these arrangements are without monetary consideration.

Funds held for others – The Houston Zoo holds funds for several organizations. Funds held for others are included in the Houston Zoo’s assets limited as to use and as a liability of the Houston Zoo.

Net asset classification – Contributions, investment return, and related net assets are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Unrestricted net assets* include those net assets whose use is not restricted by donor-imposed stipulations, even though their use may be limited in other respects, such as by contract or board designation.
- *Temporarily restricted net assets* include contributions and investment return restricted by the donor for specific purposes or time periods. When a purpose restriction is accomplished or a time restriction ends, temporarily restricted net assets are released to unrestricted net assets.
- *Permanently restricted net assets* include contributions and investment return that donors have restricted to investment in perpetuity. Investment return may be used to fund activities and programs as stipulated by the donors.

Contributions are recognized at fair value when a commitment is received from the donor. Contributions received with donor stipulations that limit their use are classified as restricted support. Conditional contributions are recognized as revenue when the conditions are substantially met. The Houston Zoo recognizes gifts of property and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are classified as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Houston Zoo reports expirations of donor restrictions when the assets are placed in service.

Donated materials, use of facilities and services – Donated materials and use of facilities are recognized at fair value as unrestricted contributions when an unconditional commitment is received from the donor. The related expense is recognized as the item is used. Contributions of services are recognized when services received (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation.

During 2017, approximately 1,600 volunteers contributed approximately 75,000 hours in connection with programs. During 2016, approximately 1,400 volunteers contributed approximately 75,000 hours in connection with programs. No amount has been recorded in the financial statements because the services did not meet the criteria for recognition under generally accepted accounting principles.

Special events revenue is recognized when the event occurs. Amounts received in advance of the event represent conditional contributions and are reported in the statement of financial position as deferred revenue. Direct donor benefit costs represent the cost of goods and services provided to attendees of special events.



Fees for services – Revenue from admissions, concessions, educational program fees and guest program fees services such as food vendors and stroller rentals are recognized when the related services are provided. Fees for services collected in advance are reported as deferred revenue until earned.

Grants made are recognized as expense at fair value when the Houston Zoo approves an unconditional commitment to a grant recipient. Commitments made but not yet funded are recorded as grants payable and are discounted, if material, to estimate the present value of future cash flows.

Advertising costs are expensed as incurred. Advertising expense of approximately \$1,146,000 was recognized in 2017 and \$1,200,000 was recognized in 2016.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts reported as revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

Reclassifications – Certain reclassifications have been made to the prior year financial statements to conform with the current presentation.

Recent financial accounting pronouncements – In fiscal year 2017, the Houston Zoo adopted Accounting Standards Update (ASU) 2016-18: *Statement of Cash Flows – Restricted Cash*, which requires the statement of cash flows to explain the change in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Prior to adoption, restricted cash and cash equivalents were excluded from beginning and ending cash and cash equivalents in the statement of cash flows. The statement of cash flows for the year ended 2016 was restated to reflect retrospective adoption. This change had no impact on net assets or changes in net assets.

In August 2016, the Financial Accounting Standards Board issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The amendments in this ASU are aimed at providing more useful information to users of not-for-profit financial statements. Under this ASU, net assets will be presented in two classes: *net assets with donor restrictions* and *net assets without donor restrictions* and underwater endowments will be grouped with *net assets with donor restrictions*. New or enhanced disclosures will be required about the nature and composition of net assets, and the liquidity and availability of resources for general operating expenditures within one year of the balance sheet date. Expenses will be required to be presented by both nature and function, and investment return will be presented net of external and direct internal investment expenses. Absent explicit donor stipulations, restrictions on long-lived assets will expire when assets are placed in service. The Houston Zoo is required to adopt this ASU for fiscal year 2018. Adoption of this ASU will impact the presentation and disclosures of the financial statements.

## **NOTE 2 – ZOO OPERATIONS AGREEMENT**

In 2002, the City entered a 50-year lease for the land, buildings and improvements of the zoo premises with the Houston Zoo Development Corporation (HZDC). HZDC is a Texas local government corporation created by the City for the sole purpose of leasing the zoo premises. Concurrently, HZDC entered into a 50-year operating agreement with the Houston Zoo to operate, maintain, manage, and develop the zoo premises. Under the operating agreement with HZDC, the Houston Zoo receives an annual management fee that will be increased each year based on the Consumer Price Index. The

management fee is subject to annual appropriation and budget approval by the City. The operating agreement can be terminated by the Houston Zoo if the annual appropriation is not approved by the City. The Houston Zoo recognized a management fee from the City of \$9,837,416 in 2017 and \$9,634,482 in 2016. At December 31, 2017, \$2.5 million is due from the City related to the operating agreement. The receivable of \$2.5 million is expected to be collected in fiscal year 2018.

### NOTE 3 – CASH

Cash and restricted or designated cash consists of the following:

	<u>2017</u>	<u>2016</u>
Restricted or designated cash:		
Board-designated for strategic operating and capital initiatives (2017-2022)	\$ 11,520,597	\$ 14,980,409
Board-designated reserve funds held in cash	313,437	309,636
Donor-restricted for Centennial Campaign	6,101,653	
Donor-restricted for other projects	4,834,540	4,928,138
Donor-restricted for capital projects	250,000	1,076,329
Funds held for others	<u>166,125</u>	<u>883,889</u>
Total restricted or designated cash	23,186,352	22,178,401
Other cash	<u>838,842</u>	<u>289,570</u>
Total cash	<u>\$ 24,025,194</u>	<u>\$ 22,467,971</u>

### NOTE 4 – PLEDGES RECEIVABLE

Pledges receivable are as follows:

	<u>2017</u>	<u>2016</u>
Pledges receivable	\$ 18,528,356	\$ 6,201,646
Discount to net present value at 0.36% to 1.98%	<u>(302,675)</u>	<u>(39,832)</u>
Pledges receivable, net	18,225,681	6,161,814
Operating pledges receivable	<u>(1,553,925)</u>	<u>(2,276,966)</u>
Pledges receivable for capital acquisitions, net	<u>\$ 16,671,756</u>	<u>\$ 3,884,848</u>

Pledges receivable at December 31, 2017 are expected to be collected as follows:

Receivable in less than one year	\$ 10,848,832
Receivable in one to five years	7,529,524
Receivable in more than five years	<u>150,000</u>
Total pledges receivable	<u>\$ 18,528,356</u>

At December 31, 2017, approximately 41% of pledges receivable were due from two donors. At December 31, 2016, approximately 65% of pledges receivable were due from two donors.

## NOTE 5 – INVESTMENTS

Investments consist of the following:

	<u>2017</u>	<u>2016</u>
Equity mutual funds	\$ 8,268,533	\$ 7,164,731
Corporate bonds and notes	5,019,437	5,723,019
Fixed-income mutual funds	2,710,980	2,588,636
U. S. Treasury and agency securities	1,729,366	711,229
Money market mutual funds	1,657,916	2,208,802
Exchange-traded funds	<u>745,774</u>	<u>                    </u>
Total investments	<u>\$ 20,132,006</u>	<u>\$ 18,396,417</u>

Investments at December 31, 2017 and 2016 are held for the endowment and board-designated operating reserves.

Investments are exposed to various risks such as interest rate, market, and credit risks. Because of these risks, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position and statement of activities.

Investment return includes earnings on cash and consists of the following:

	<u>2017</u>	<u>2016</u>
Interest and dividends	\$ 536,064	\$ 603,974
Unrealized gain (loss) on investments	1,132,739	(808,040)
Realized gain on investments	145,844	869,543
Investment management fees	<u>(92,852)</u>	<u>(50,525)</u>
Investment return, net	<u>\$ 1,721,795</u>	<u>\$ 614,952</u>

## NOTE 6 – FAIR VALUE MEASUREMENTS

Generally accepted accounting principles require that certain assets and liabilities be reported at fair value and establish a hierarchy that prioritizes inputs used to measure fair value. Fair value is 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. The three levels of the fair value hierarchy are as follows:

- *Level 1* – Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date.
- *Level 2* – Inputs are other than quoted prices included in Level 1, which are either directly observable or can be derived from or corroborated by observable market data at the reporting date.
- *Level 3* – Inputs are not observable and are based on the reporting entity's assumptions about the inputs market participants would use in pricing the asset or liability.

Assets measured at fair value at December 31, 2017 are as follows:

	<u>LEVEL 1</u>	<u>LEVEL 2</u>	<u>LEVEL 3</u>	<u>TOTAL</u>
Investments:				
Equity mutual funds:				
Developed international	\$ 3,252,602			\$ 3,252,602
Domestic large-cap growth	2,278,539			2,278,539
Domestic large-cap value	1,747,958			1,747,958
Commodity	659,212			659,212
Domestic small-cap	239,255			239,255
Real estate	90,967			90,967
Corporate bonds and notes:				
A-rated		\$ 2,236,439		2,236,439
BAA-rated		2,065,450		2,065,450
Other ratings		717,548		717,548
Fixed-income mutual funds:				
High yield bond	777,429			777,429
Inflation protected	664,650			664,650
Corporate bond	483,810			483,810
Government bond	415,063			415,063
Asset-backed securities	370,028			370,028
U. S. Treasury and agency securities		1,729,366		1,729,366
Money market mutual funds	1,657,916			1,657,916
Short-term exchange-traded funds	<u>745,774</u>			<u>745,774</u>
Total assets measured at fair value	<u>\$ 13,383,203</u>	<u>\$ 6,748,803</u>	<u>\$ 0</u>	<u>\$ 20,132,006</u>

Assets measured at fair value at December 31, 2016 are as follows:

	<u>LEVEL 1</u>	<u>LEVEL 2</u>	<u>LEVEL 3</u>	<u>TOTAL</u>
Investments:				
Equity mutual funds:				
Developed international	\$ 2,830,750			\$ 2,830,750
Domestic large-cap growth	1,944,503			1,944,503
Domestic large-cap value	1,521,478			1,521,478
Commodity	575,800			575,800
Domestic small-cap	207,034			207,034
Real estate	85,166			85,166
Corporate bonds and notes:				
A-rated		\$ 2,713,630		2,713,630
BAA-rated		2,589,006		2,589,006
Other ratings		420,383		420,383
Fixed-income mutual funds:				
High yield bond	713,433			713,433
Inflation protected	648,072			648,072
Corporate bond	458,258			458,258
Government bond	406,701			406,701
Asset-backed securities	362,172			362,172
U. S. Treasury and agency securities		711,229		711,229
Money market mutual funds	<u>2,208,802</u>			<u>2,208,802</u>
Total assets measured at fair value	<u>\$ 11,962,169</u>	<u>\$ 6,434,248</u>	<u>\$ 0</u>	<u>\$ 18,396,417</u>

Valuation methods used for assets measured at fair value are as follows:

- *Mutual funds* are valued at the net asset value of shares held at year end.
- *Corporate bonds and notes* and *U. S. Treasury and agency securities* are valued using prices obtained from independent quotation bureaus that use computerized valuation formulas to calculate fair values.
- *Exchange-traded funds* are valued at the closing price reported on the active market on which the individual securities are traded.

These valuation methods may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Houston Zoo believes its valuation methods are appropriate, the use of different methods or assumptions could result in a different fair value measurement at the reporting date.

#### NOTE 7 – PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	<u>2017</u>	<u>2016</u>
Leasehold improvements	\$ 138,272,246	\$ 124,375,018
Furniture, fixtures and equipment	12,913,073	10,837,715
Construction in progress	<u>5,233,733</u>	<u>8,401,968</u>
Total property and equipment, at cost	156,419,052	143,614,701
Accumulated depreciation	<u>(49,315,294)</u>	<u>(40,994,646)</u>
Property and equipment, net	<u>\$ 107,103,758</u>	<u>\$ 102,620,055</u>

#### NOTE 8 – UNRESTRICTED NET ASSETS

Unrestricted net assets consist of the following:

	<u>2017</u>	<u>2016</u>
Property and equipment, net	\$ 106,265,233	\$ 100,260,905
Zoo operations	3,143,237	360,057
Board-designated for strategic operating and capital initiatives (2017-2022)	11,520,597	14,980,409
Board-designated operating reserve	7,977,199	7,880,298
Board-designated endowment funds:		
Maintenance	4,160,892	3,599,928
General	<u>2,021,577</u>	<u>1,795,503</u>
Total unrestricted net assets	<u>\$ 135,088,735</u>	<u>\$ 128,877,100</u>

## NOTE 9 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes:

	BALANCE DECEMBER 31, 2016	2017		BALANCE DECEMBER 31, 2017
		CONTRIBUTIONS AND INVESTMENT RETURN	UTILIZED FOR ZOO PROGRAMS AND CAPITAL IMPROVEMENTS	
Capital improvements	\$ 600,000	\$ 20,172,458	\$ (350,000)	\$ 20,422,458
Conservation	5,612,731	1,536,475	(1,269,657)	5,879,549
John P. McGovern Children's Zoo	1,283,179	477,653	(50,000)	1,710,832
General operations in future periods	1,160,591	333,000	(742,591)	751,000
Elephant exhibit expansion	2,651,329	250,000	(2,901,329)	
Other	<u>744,220</u>	<u>363,629</u>	<u>(163,612)</u>	<u>944,237</u>
Total temporarily restricted net assets	<u>\$ 12,052,050</u>	<u>\$ 23,133,215</u>	<u>\$ (5,477,189)</u>	<u>\$ 29,708,076</u>

## NOTE 10 – ENDOWMENT FUNDS

Changes in endowment net assets are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
Endowment net assets, January 1, 2016	<u>\$ 4,106,909</u>	<u>\$ 1,634,541</u>	<u>\$ 3,512,518</u>	<u>\$ 9,253,968</u>
Investment return:				
Interest and dividends	137,188	178,723	859	316,770
Realized and unrealized gain	122,085	159,003	763	281,851
Investment management fees	<u>(20,751)</u>	<u>(28,243)</u>	<u>(136)</u>	<u>(49,130)</u>
Total investment return	<u>238,522</u>	<u>309,483</u>	<u>1,486</u>	<u>549,491</u>
Contributions/transfers	1,050,000		4,000	1,054,000
Appropriation of endowment assets for expenditure		<u>(31,704)</u>		<u>(31,704)</u>
Endowment net assets, December 31, 2016	<u>5,395,431</u>	<u>1,912,320</u>	<u>3,518,004</u>	<u>10,825,755</u>
Investment return:				
Interest and dividends	135,361	147,567	709	283,637
Realized and unrealized gain	680,865	742,257	3,565	1,426,687
Investment management fees	<u>(34,188)</u>	<u>(37,271)</u>	<u>(179)</u>	<u>(71,638)</u>
Total investment return	<u>782,038</u>	<u>852,553</u>	<u>4,095</u>	<u>1,638,686</u>
Contributions/transfers	<u>5,000</u>		<u>4,000</u>	<u>9,000</u>
Endowment net assets, December 31, 2017	<u>\$ 6,182,469</u>	<u>\$ 2,764,873</u>	<u>\$ 3,526,099</u>	<u>\$ 12,473,441</u>

Endowment net asset composition as of December 31, 2017:

	<u>UNRESTRICTED</u>	TEMPORARILY <u>RESTRICTED</u>	PERMANENTLY <u>RESTRICTED</u>	<u>TOTAL</u>
Donor-restricted endowment funds:				
Jane Block Endowment for the Children's Zoo		\$ 1,437,022	\$ 1,735,049	\$ 3,172,071
Conservation programs		521,160	633,591	1,154,751
Clark and Gordon Memorial special event endowment		385,930	548,734	934,664
Zoo Friends education exhibits		141,968	200,000	341,968
Martel Lecture Series		70,582	100,000	170,582
Fred Maier Beautification Fund		62,119	75,000	137,119
Morris Docent Education Award		41,424	50,000	91,424
Alban Heiser Conservation Award		11,481	49,270	60,751
Carter Education Internship		20,713	25,000	45,713
Other endowments		72,474	109,455	181,929
Board-designated endowment funds	<u>\$ 6,182,469</u>	_____	_____	<u>6,182,469</u>
Total endowment net assets	<u>\$ 6,182,469</u>	<u>\$ 2,764,873</u>	<u>\$ 3,526,099</u>	<u>\$ 12,473,441</u>

Endowment net asset composition as of December 31, 2016:

	<u>UNRESTRICTED</u>	TEMPORARILY <u>RESTRICTED</u>	PERMANENTLY <u>RESTRICTED</u>	<u>TOTAL</u>
Donor-restricted endowment funds:				
Jane Block Endowment for the Children's Zoo		\$ 1,009,370	\$ 1,735,049	\$ 2,744,419
Conservation programs		365,479	633,591	999,070
Clark and Gordon Memorial special event endowment		252,929	548,734	801,663
Zoo Friends education exhibits		92,669	200,000	292,669
Martel Lecture Series		47,584	100,000	147,584
Fred Maier Beautification Fund		43,633	75,000	118,633
Morris Docent Education Award		29,099	50,000	79,099
Alban Heiser Conservation Award		7,386	45,175	52,561
Carter Education Internship		14,550	25,000	39,550
Other endowments		49,621	105,455	155,076
Board-designated endowment funds	<u>\$ 5,395,431</u>	_____	_____	<u>5,395,431</u>
Total endowment net assets	<u>\$ 5,395,431</u>	<u>\$ 1,912,320</u>	<u>\$ 3,518,004</u>	<u>\$ 10,825,755</u>

The Board of Directors of the Houston Zoo has interpreted the Texas Uniform Prudent Management of Institutional Funds Act (TUPMIFA) 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 Houston Zoo classifies the original value of gifts donated to the permanent endowment as permanently restricted net assets. The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Houston Zoo in a manner consistent with the standard of prudence prescribed by TUPMIFA. In accordance with

TUPMIFA, the Houston Zoo considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the fund
- The purposes of the Houston Zoo and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Houston Zoo
- The investment policies of the Houston Zoo

### Investment Objectives

The Houston Zoo has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to enhance its real (inflation-adjusted) value over time. Endowment assets include those assets of donor-restricted funds that the Houston Zoo must hold in perpetuity or for a donor-specified period, as well as funds designated by the Board of Directors to function as endowments. Under this policy, as approved by the Board of Directors, the endowment assets are invested in a manner that is intended to produce results that are the greater of the Consumer Price Index plus 4% to 5% or a custom index, while assuming a moderate level of investment risk. The Houston Zoo expects its endowment funds, over time, to provide a real return of approximately 4% to 5% over the long term. Actual returns in any given year may vary from this amount.

Endowment funds are maintained in investment accounts which are managed by independent financial firms that follow guidance provided in an investment policy approved by the Board of Directors. To satisfy its long-term rate-of-return objectives, the Houston Zoo relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Houston Zoo targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

### Spending Policy

The Houston Zoo has a policy of appropriating for distribution each year up to 3% of its endowment fund's average fair value over the prior 12 quarters through the calendar year end preceding the fiscal year in which the distribution is planned, but may not exceed the cumulative actual earnings and appreciation of the funds. In establishing this policy, the Houston Zoo considered the long-term expected return on its endowment. The Houston Zoo's objective is to enhance the real (inflation-adjusted) value over time of the endowment assets held in perpetuity or for a specified term through new gifts and investment return.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or TUPMIFA requires the Houston Zoo to retain as a fund of perpetual duration. Deficiencies of this nature result from unfavorable market fluctuations and continued appropriation for certain programs that were deemed prudent by the Board of Directors. Such deficiencies are reported in unrestricted net assets as an aggregate deficiency of endowment funds.



**NOTE 11 – RETIREMENT PLAN**

The Houston Zoo retirement savings plan is qualified under §401(k) of the Internal Revenue Code. The plan allows eligible employees to contribute a portion of their earnings each plan year subject to certain Internal Revenue Service limitations and to defer federal income taxes on the contributions. The Houston Zoo matches 100% of the first 3% of employee contributions and matches 50% of contributions from 3% to 5%. The employee is 100% immediately vested in the employer's contributions. The Houston Zoo contributed approximately \$625,000 and \$559,000 to the plan during 2017 and 2016, respectively.

**NOTE 12 – COMMITMENTS**

As of December 31, 2017, the Houston Zoo has entered into various construction commitments totaling approximately \$21 million. The unrecognized balance of these commitments at December 31, 2017 was approximately \$17 million.

**NOTE 13 – SUBSEQUENT EVENTS**

Subsequent to December 31, 2017, the Houston Zoo received a \$50 million contribution from a foundation for the Centennial Campaign, which will be paid over eleven years.

Management has evaluated subsequent events through May 21, 2018, which is the date that the financial statements were available for issuance. As a result of this evaluation, no other events were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.

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