

TREEHOUSE

FINANCIAL REPORT

SEPTEMBER 30, 2013

C O N T E N T S

	Page
INDEPENDENT AUDITORS' REPORT	1 and 2
FINANCIAL STATEMENTS	
STATEMENT OF FINANCIAL POSITION	3
STATEMENT OF ACTIVITIES	4
STATEMENT OF FUNCTIONAL EXPENSES.....	5
STATEMENT OF CASH FLOWS	6
NOTES TO FINANCIAL STATEMENTS	7 - 17

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Treehouse
Seattle, Washington

We have audited the accompanying financial statements of Treehouse, 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; 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to 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 Treehouse 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.

Report on Summarized Comparative Information

We have previously audited Treehouse's 2012 financial statements, and our report dated January 22, 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.

Peterston Sullivan LLP.

January 7, 2014

TREEHOUSE

STATEMENT OF FINANCIAL POSITION

September 30, 2013

(With Comparative Totals for 2012)

ASSETS	2013	2012
Current Assets		
Cash and cash equivalents	\$ 1,991,268	\$ 552,320
Investments	494,009	2,247,256
Current pledges receivable, net	1,246,906	262,831
Contribution receivable for rent	179,841	180,106
Contracts receivable	56,643	72,975
Cy pres award receivable	750,000	
Inventories	196,974	225,286
Unemployment trust deposits	23,030	
Prepaid expenses	130,718	36,038
Total current assets	5,069,389	3,576,812
Long-Term Assets		
Long-term portion of receivables, less current portion		
Pledges receivable, net	1,412,540	370,006
Contribution receivable for rent, net	45,402	225,340
Furniture and equipment, net	66,924	121,538
Endowment investments	3,440,411	3,116,011
Other investments	338,511	169,669
Total long-term assets	5,303,788	4,002,564
Total assets	\$ 10,373,177	\$ 7,579,376
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts payable	\$ 63,516	\$ 38,254
Accrued salaries and related costs	265,881	194,619
Deferred revenue	45,000	
Total current liabilities	374,397	232,873
Net Assets		
Unrestricted	3,461,238	2,920,584
Temporarily restricted	3,097,131	1,309,908
Permanently restricted	3,440,411	3,116,011
Total net assets	9,998,780	7,346,503
Total liabilities and net assets	\$ 10,373,177	\$ 7,579,376

See Notes to Financial Statements

TREEHOUSE

STATEMENT OF ACTIVITIES

For the Year Ended September 30, 2013
(With Comparative Totals for 2012)

	2013			Total	2012 Total
	Unrestricted	Temporarily Restricted	Permanently Restricted		
Revenue					
Contributions and grants	\$ 4,571,796	\$ 2,237,500	\$ -	\$ 6,809,296	\$ 5,529,507
Cy pres award	750,000			750,000	
In-kind contributions	1,427,786			1,427,786	1,164,037
Contract revenue	823,771			823,771	839,835
Net assets released from restrictions	654,076	(524,996)	(129,080)		
Total revenue	8,227,429	1,712,504	(129,080)	9,810,853	7,533,379
Expenses					
Program services	6,071,047			6,071,047	5,477,660
Management and general	357,690			357,690	418,009
Fundraising	1,270,122			1,270,122	1,009,411
Total expenses	7,698,859			7,698,859	6,905,080
Changes in net assets before investment income	528,570	1,712,504	(129,080)	2,111,994	628,299
Investment income	12,084	74,719	453,480	540,283	590,712
Change in net assets	540,654	1,787,223	324,400	2,652,277	1,219,011
Net assets, beginning of year	2,920,584	1,309,908	3,116,011	7,346,503	6,127,492
Net assets, end of year	\$ 3,461,238	\$ 3,097,131	\$ 3,440,411	\$ 9,998,780	\$ 7,346,503

See Notes to Financial Statements

TREEHOUSE

STATEMENT OF FUNCTIONAL EXPENSES

For the Year Ended September 30, 2013

(With Comparative Totals for 2012)

	Program Services			Total Program Services	Support Services		Totals	
	Education Programs	Enrichment Programs			Management and General	Fundraising	2013	2012
		Wearhouse	Other					
Payroll	\$ 2,165,937	\$ 233,951	\$ 237,046	\$ 2,636,934	\$ 165,356	\$ 535,101	\$ 3,337,391	\$ 2,945,148
Wearhouse distributions		981,250		981,250			981,250	996,702
Payroll taxes and benefits	463,083	51,089	49,945	564,117	27,538	111,715	703,370	659,179
Other in-kind expenses	117,543	93,072	142,143	352,758	10,771	162,786	526,315	269,765
Occupancy	95,959	208,783	17,737	322,479	28,479	50,211	401,169	395,721
Assistance to specific individuals			339,601	339,601	385		339,986	364,425
Holiday Magic purchases			325,730	325,730			325,730	343,752
Professional services	95,272	11,281	32,120	138,673	47,275	93,208	279,156	210,768
Printing and publications	14,550	1,144	8,705	24,399	4,976	61,263	90,638	77,498
Special events						88,918	88,918	82,726
Licenses and fees	38,001	3,614	6,552	48,167	12,656	27,113	87,936	41,247
Postage and shipping	4,084	191	30,352	34,627	455	44,557	79,639	74,726
Supplies	50,503	3,254	7,431	61,188	4,736	7,087	73,011	82,460
Transportation	59,755	179	695	60,629	626	3,125	64,380	70,274
Credit card fees	165	35	16,587	16,787		38,676	55,463	57,320
Staff training	24,353	968	1,030	26,351	2,522	4,310	33,183	32,581
Meetings	8,290	706	635	9,631	2,282	11,063	22,976	23,684
Insurance	8,227	1,725	1,407	11,359	7,502	2,574	21,435	20,218
Equipment leases	12,035	1,218	1,085	14,338	4,995	1,714	21,047	14,020
Depreciation	25,357	5,474	4,464	35,295	23,809	8,170	67,274	68,420
Other	59,011	4,135	3,588	66,734	13,327	18,531	98,592	74,446
Total expenses - 2013	<u>\$ 3,242,125</u>	<u>\$ 1,602,069</u>	<u>\$ 1,226,853</u>	<u>\$ 6,071,047</u>	<u>\$ 357,690</u>	<u>\$ 1,270,122</u>	<u>\$ 7,698,859</u>	
Percent of total - 2013	<u>42%</u>	<u>21%</u>	<u>16%</u>	<u>79%</u>	<u>5%</u>	<u>16%</u>	<u>100%</u>	
Total expenses - 2012	<u>\$ 2,673,823</u>	<u>\$ 1,607,905</u>	<u>\$ 1,195,932</u>	<u>\$ 5,477,660</u>	<u>\$ 418,009</u>	<u>\$ 1,009,411</u>		<u>\$ 6,905,080</u>
Percent of total - 2012	<u>39%</u>	<u>23%</u>	<u>17%</u>	<u>79%</u>	<u>6%</u>	<u>15%</u>		<u>100%</u>

See Notes to Financial Statements

TREEHOUSE

STATEMENT OF CASH FLOWS

For the Year Ended September 30, 2013
(With Comparative Totals for 2012)

	2013	2012
Cash Flows from Operating Activities		
Change in net assets	\$ 2,652,277	\$ 1,219,011
Adjustments to reconcile change in net assets to net cash flows from operating activities		
Depreciation	67,274	68,420
Net realized and unrealized gain on investments	(449,725)	(515,277)
Interest and dividends restricted for long-term investments	(77,305)	(52,682)
Changes in allowance and discounts on receivables	25,708	20,290
Change in operating assets and liabilities		
Pledges receivable	(2,052,317)	(386,327)
Contribution receivable for rent	180,203	(405,446)
Contracts receivable	16,332	147,840
Cy pres award receivable	(750,000)	
Inventories	28,312	53,142
Unemployment trust deposits	(23,030)	
Prepaid expenses	(94,680)	(206)
Accounts payable	25,262	7,333
Accrued salaries and related costs	71,262	(20,336)
Deferred revenue	45,000	
Net cash flows from operating activities	(335,427)	135,762
Cash Flows from Investing Activities		
Purchase of investments (including reinvested income)	(693,153)	(4,322,435)
Proceeds from sale of investments	2,402,883	2,625,050
Purchase of furniture and equipment	(12,660)	(18,840)
Net cash flows from investing activities	1,697,070	(1,716,225)
Cash Flows from Financing Activity		
Interest and dividends restricted for reinvestment	77,305	52,682
Net change in cash and cash equivalents	1,438,948	(1,527,781)
Cash and cash equivalents, beginning of year	552,320	2,080,101
Cash and cash equivalents, end of year	\$ 1,991,268	\$ 552,320

See Notes to Financial Statements

NOTES TO FINANCIAL STATEMENTS

Note 1. Organization

Treehouse is a nonprofit organization addressing the essential education and enrichment needs of kids in foster care. Treehouse helps 6,000 foster kids each year through programs that help them succeed in school, fulfill key material needs, and provide important childhood experiences every child deserves. Founded in 1988, Treehouse's mission is *giving foster kids a childhood and a future*, and the organization has set an ambitious goal that foster youth in King County will graduate high school at the same rate as their peers with a plan for their future by 2017. Funding is received primarily from individuals, corporate gifts, and private foundation grants. Governmental support has traditionally been limited with the exception of an agreement with the Washington State Department of Social and Health Services ("DSHS").

Treehouse's five major programs are in two categories – Education and Enrichment.

Education Programs:

- Educational Advocacy – Treehouse Educational Advocates are co-located in DSHS Children's Administration offices throughout Washington State and work with schools, social workers, foster families, and foster youth to resolve difficult issues and remove barriers to foster kids' school success.
- Graduation Success – Foster youth face an uphill battle to graduate high school due to school transitions, lack of basic skills, and emotional upheaval. Treehouse's Graduation Success program addresses the specific education needs of youth in foster care. Treehouse education specialists partner with social workers, caregivers, teachers, school counselors and an in-school mentor to provide education planning, coaching and support to help build each youth's engagement and investment in their education and their future. Through weekly monitoring of risk indicators, personalized interventions, building problem solving and self-advocacy skills, proactively removing barriers to school success, and coordinating needed supports, Treehouse paves the way to high school graduation, hope, and opportunity. Treehouse provides Graduation Success education support services in most high schools and middle schools in King County.

Enrichment Programs:

- Wearhouse – The Wearhouse ensures that foster youth have access to the items they need to feel confident and ready to learn at school. The Wearhouse accepts donations of new and like-new clothing, toys, books, school supplies, and household goods and distributes them at no charge to eligible children residing in King County. When necessary to meet demand, Treehouse may purchase items for distribution. Due to the significance of the expenses related to the Wearhouse, the expenses have been shown separately in the Statement of Functional Expenses.
- Little Wishes/Summer Experiences – Treehouse's Little Wishes program helps pay for the important experiences that every child deserves. Treehouse provides access to extra-curricular activities like sports, clubs, music, and dance, as well as school activities helping youth gain confidence, have fun, and improve academic performance. Little Wishes also supports fun and enriching summer experiences for youth including overnight camps, day camps, leadership opportunities, summer school and other summer programs that give kids in foster care a chance to get away from it all, make new friends, and just be a kid.

- 97.3 KIRO FM Foster Child Holiday Magic - Holiday Magic is a joint holiday gift program for foster children, and is between DSHS Children's Administration, KIRO FM, and Treehouse. Children's Administration contracts with Treehouse to administer the program, raise community funds, and provide one substantial holiday gift to 4,600 foster children across Washington State. Funds are raised through a radiothon, a partnership with the employees of The Boeing Company, and direct mail and email appeals. The proceeds from the radiothon are used to purchase gifts for foster children. The contract with DSHS stipulates that any funds raised in excess of Holiday Magic gift needs will be transferred to Treehouse, and that those funds are to be utilized to benefit children currently served by DSHS.

Note 2. Summary of Significant Accounting Policies

Financial Statement Presentation

Treehouse 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. Contributions that are received are recorded as unrestricted, temporarily restricted, or permanently restricted, depending on the existence and/or nature of any donor restrictions. Temporarily restricted contributions are reclassified to unrestricted net assets when the restrictions are met. Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction is met in the year in which the support is initially recognized.

Permanently restricted contributions are reclassified to unrestricted net assets in accordance with the donors' request to release up to 5% of the average ending balances of the previous 12 quarters from restrictions annually on December 31, to fund expenditures for various programs. Permanently restricted net assets consist solely of endowment funds with donor stipulations requiring Treehouse to invest in equity securities and, as such, the difference between investment earnings or losses related to these endowments and the amounts released are presented in the financial statements as a component of permanently restricted net assets.

The financial statements include 2012 prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States. Accordingly, such information should be read in conjunction with Treehouse's financial statements for the year ended September 30, 2012, from which the summarized information was derived.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from the estimated amounts.

Fair Value Measurements

Fair value is a market-based measurement determined based on assumptions that market participants would use in pricing an asset or liability. There are three levels which prioritize the inputs used in measuring fair value as follows:

- Level 1: Observable market inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Observable market inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3: Unobservable inputs where there is little or no market data, which require the reporting entity to develop its own assumptions.

Cash and Cash Equivalents

Cash and cash equivalents include cash, money market funds, and short-term securities with an original maturity of three months or less. Money market balances held in investment accounts are included with investments in the Statement of Financial Position. Treehouse occasionally has cash and cash equivalents balances in excess of federally insured limits.

Revenue Recognition

Unconditional promises to give are recognized at fair value in the period the pledge is received. In arriving at fair value, management has discounted these contributions using an estimated present value discount rate and has established an allowance for doubtful accounts. Conditional promises to give are recognized when the conditions on which they depend are substantially met. There are no conditional promises as of September 30, 2013 or 2012. For the years ended September 30, 2013 and 2012, 29% and 10%, respectively, of contributions and grants revenue were received from one donor (and organizations related to the donor). At September 30, 2013, 71% of pledges receivable are from one donor. At September 30, 2012, 68% of pledges receivable are from two donors.

Contract revenue consists of contracts administered by local governments and is recorded as revenue when services are performed. Contracts receivable represents contracts awarded or earned, but not yet received. Substantially all contracts receivable are from one local government at September 30, 2013 and 2012.

Deferred revenue represents the proceeds from ticket sales for events. Revenue from ticket sales for events is recognized during the period the event takes place.

Cy pres awards result from the receipt of residual funds distributed by various courts from class action lawsuit recoveries. The award was distributed by the court when it determined it was not practical to distribute the award to class action members. Treehouse records Cy pres awards as revenue when it is notified that an award has been made. Treehouse does not anticipate receiving Cy pres awards in the future.

Investments

Investments in mutual funds are stated at fair value using Level 1 inputs (quoted prices on national exchanges). Certificates of deposit and money market funds are stated at cost plus accrued interest. Realized and unrealized gains and losses are included in the Statement of Activities. At September 30, 2013 and 2012, investments are as follows:

	<u>2013</u>	<u>2012</u>
Equity mutual funds		
Large cap	\$ 2,152,294	\$ 1,675,467
Mid cap	436,056	333,508
Small cap	264,415	189,665
International	347,523	280,543
Emerging markets	454,445	441,982
Fixed income mutual funds		
Intermediate-term bond funds	578,597	331,510
International bond funds	29,511	13,921
Certificates of deposit		2,246,078
Money market fund	10,090	20,262
	<u>\$ 4,272,931</u>	<u>\$ 5,532,936</u>

Investments are presented in the Statement of Financial Position as follows:

	<u>2013</u>	<u>2012</u>
Investments	\$ 494,009	\$ 2,247,256
Endowment investments	3,440,411	3,116,011
Other investments	338,511	169,669
	<u>\$ 4,272,931</u>	<u>\$ 5,532,936</u>

Investment income was composed of:

	<u>2013</u>	<u>2012</u>
Interest and dividends	\$ 90,558	\$ 75,435
Realized and unrealized gains	449,725	515,277
	<u>\$ 540,283</u>	<u>\$ 590,712</u>

Investment income reported as an increase in unrestricted net assets for the year ended September 30, 2013, amounted to \$12,084 and was generated from cash and cash equivalents and Board designated endowment funds. This amount is comprised of interest and dividends of \$127 and unrealized gains of \$11,957.

Investment income reported as an increase in temporarily restricted net assets for the year ended September 30, 2013, amounted to \$74,719. This amount is comprised of interest and dividends of \$13,126 and unrealized gains of \$61,593 generated from the Fostering Futures Endowment.

Investment income reported as an increase in permanently restricted net assets for the year ended September 30, 2013, amounted to \$453,480. This amount is composed of interest and dividends of \$77,305 and unrealized gains of \$376,175 generated from the Operations and Education Endowments.

Inventories

Inventories include new and quality used clothing and other items for children. Purchased new inventory is valued at cost. Donated new inventory and quality used clothing is valued at estimated fair value.

Unemployment Trust Deposits

Treehouse participates in a program to reduce its unemployment insurance costs. Accordingly, Treehouse has made deposits with the organization that sponsors this program (and Treehouse does not pay unemployment insurance to the State of Washington). These deposits are used to reimburse the State of Washington for unemployment benefits paid to employees who have terminated their employment with Treehouse. The goal of the program is that payments for the deposits are less than what would be paid to the State of Washington for unemployment insurance.

Furniture and Equipment

Furniture and equipment is recorded at cost, if purchased, or at estimated fair value at the date of receipt, if donated. All purchases under \$1,000 are expensed when acquired. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. Furniture and equipment consist of the following:

	2013	2012
Computer equipment	\$ 283,864	\$ 479,900
Office furniture and fixtures	293,237	411,555
Leasehold improvements	66,869	65,808
Vehicle	13,257	13,257
	<u>657,227</u>	<u>970,520</u>
Accumulated depreciation	(590,303)	(848,982)
Furniture and equipment, net	<u>\$ 66,924</u>	<u>\$ 121,538</u>

In-Kind Contributions

In-kind contributions are recorded at their estimated fair values at the date of donation. In-kind contributions recognized consist of the following:

	2013	2012
Donated new and quality used clothing	\$ 1,002,306	\$ 1,021,317
Database and software implementation	105,000	
Little Wishes discounts	82,240	48,112
Advertising and public relations	79,301	
Donor research	42,500	40,000
Summer camp discounts	41,553	34,721
Gift cards	7,000	4,020
Professional services and other	67,886	15,867
	<u>\$ 1,427,786</u>	<u>\$ 1,164,037</u>

Functional Allocation of Expenses

The costs of providing the various programs and other activities are summarized on a functional basis in the Statement of Activities. Accordingly, certain costs are allocated among the programs and supporting services benefited.

Income Taxes

Treehouse is exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Code. Treehouse's federal tax returns are open to examination for the years ended September 30, 2010 to 2013.

Reclassifications

Certain items from the September 30, 2012, financial statements have been reclassified to conform to the current presentation. These reclassifications had no impact on net assets or the change in net assets as previously reported.

Subsequent Events

Treehouse has evaluated subsequent events through the date these financial statements were available to be issued, which is the same date as the independent auditors' report. No subsequent events required recognition or disclosure in the financial statements.

Note 3. Pledges Receivable

Pledges receivable are as follows:

	<u>2013</u>	<u>2012</u>
Receivable in less than one year	\$ 1,257,592	\$ 276,117
Receivable in one to five years	1,461,344	290,502
Thereafter		100,000
	<u>2,718,936</u>	<u>666,619</u>
Less: Allowance for uncollectible pledges	<u>(10,686)</u>	<u>(13,286)</u>
	2,708,250	653,333
Less: Discounts to present value (2%)	<u>(48,804)</u>	<u>(20,496)</u>
Pledges receivable, net	<u>\$ 2,659,446</u>	<u>\$ 632,837</u>

These assets are presented in the financial statements as follows:

	<u>2013</u>	<u>2012</u>
Current pledges receivable, net	\$ 1,246,906	\$ 262,831
Long-term pledges receivable, net	<u>1,412,540</u>	<u>370,006</u>
Pledges receivable, net	<u>\$ 2,659,446</u>	<u>\$ 632,837</u>

Note 4. Restricted Net Assets

Temporarily restricted net assets consist of contributions restricted for particular purposes or time periods, and were composed of the following as of September 30:

	2013	2012
Fostering Futures Endowment earnings	\$ 244,388	\$ 169,669
Educational advocacy	500,000	
Holiday Magic		164,546
Contribution receivable for rent (restricted for time)	225,243	405,446
Contributions with payments due in future periods (restricted for time)	1,927,500	345,247
Contributions with payments due in future periods (restricted for time and Little Wishes)	200,000	225,000
	<u>\$ 3,097,131</u>	<u>\$ 1,309,908</u>

Permanently restricted net assets were composed of the following as of September 30:

	2013	2012
Education Endowment	\$ 468,349	\$ 419,007
Operations Endowment	2,565,349	2,290,291
Fostering Futures Endowment	406,713	406,713
	<u>\$ 3,440,411</u>	<u>\$ 3,116,011</u>

Note 5. Endowment Funds

Two separate endowment funds, the Education Endowment Fund and Operations Endowment Fund, were formed by two principal donors to provide a recurring base of funds to achieve the goals as requested by the donors. The donors allow an amount up to 5% of the average ending balances of the previous 12 quarters of both the Education and Operations Endowment Funds to be released from restrictions annually on December 31, without regard to the principal balance. The amount released is available to Treehouse for expenditure to fund educational programs and operational needs. Each year, the amounts released are shown as being transferred to unrestricted net assets. The donors require Treehouse to invest the endowment funds in equity securities and, as such, all other investment earnings or losses related to these endowments in excess of the amounts released are retained and presented in the financial statements as a component of permanently restricted net assets.

An endowment fund called the Fostering Futures Endowment Fund was created in 2003 in conjunction with Treehouse's Fostering Futures Campaign. Earnings from the Fostering Futures Endowment Fund are available to be used to achieve the targeted goals of Treehouse; however, the Board of Directors has resolved that no funds from the Fostering Futures Endowment Fund will be expended until the fund grows to \$1,000,000. Therefore, the earnings from the Fostering Futures Endowment Fund are board-designated. There were no transfers from this Fund in 2013 or 2012. During the year ended September 30, 2013, the Board of Directors designated funds to function as part of the Fostering Futures Endowment Fund ("quasi-endowment").

As required by accounting principles generally accepted in the United States, net assets associated with endowment funds, including quasi-endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law

The Board of Directors has interpreted the State of Washington 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 (other than the Operations and Educational Endowment Funds). As a result of this interpretation, Treehouse classifies as permanently restricted net assets (other than the Operations and Educational Endowment Funds) (a) the original value of gifts donated to the permanent endowment, plus (b) the original value of subsequent gifts to the permanent endowment. The remaining portion of donor-restricted endowment funds, representing the earnings from the Fostering Futures Fund, that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Treehouse in a manner consistent with the standard of prudence prescribed by UPMIFA. Funds designated by the Board of Directors, to be treated as Fostering Futures quasi-endowment funds, are classified as Board designated unrestricted net assets. In accordance with UPMIFA, Treehouse considers the following factors in making a determination to appropriate or accumulate donor-restricted funds:

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

Endowment Net Assets consisted of the following at:

	September 30, 2013			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ 244,388	\$ 3,440,411	\$ 3,684,799
Board-designated quasi-endowment funds	94,123			94,123
Total invested endowment net assets	<u>\$ 94,123</u>	<u>\$ 244,388</u>	<u>\$ 3,440,411</u>	<u>\$ 3,778,922</u>
	September 30, 2012			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	<u>\$ -</u>	<u>\$ 169,669</u>	<u>\$ 3,116,011</u>	<u>\$ 3,285,680</u>

Changes in Endowment Net Assets are as follows for the years ended:

	September 30, 2013			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Endowment net assets, beginning of year	\$ -	\$ 169,669	\$ 3,116,011	\$ 3,285,680
Investment return:				
Net investment income		13,126	77,305	90,431
Net realized and unrealized gain	11,957	61,593	376,175	449,725
Total investment return	11,957	74,719	453,480	540,156
Net assets appropriated and released from restrictions			(129,080)	(129,080)
Other changes and transfers	82,166			82,166
Endowment net assets, end of year	<u>\$ 94,123</u>	<u>\$ 244,388</u>	<u>\$ 3,440,411</u>	<u>\$ 3,778,922</u>

	September 30, 2012			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Endowment net assets, beginning of year	\$ -	\$ 150,381	\$ 2,671,699	\$ 2,822,080
Investment return:				
Net investment income		18,244	52,682	70,926
Net realized and unrealized gain		1,044	514,233	515,277
Total investment return		19,288	566,915	586,203
Net assets appropriated and released from restrictions			(122,603)	(122,603)
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 169,669</u>	<u>\$ 3,116,011</u>	<u>\$ 3,285,680</u>

Return Objectives and Risk Parameters

Treehouse adopted an investment policy that was approved by the Board of Directors for endowment assets that attempts to provide a predictable stream of funding to programs supported by its endowments while seeking to maintain the purchasing power of the endowment assets. In accordance with the donors' stipulations, Treehouse's investment policy states that the assets in the Operations and Education Endowments are to be invested in equity securities and performance will be evaluated against the S&P 500. Treehouse expects its Operations and Education Endowment funds, over time, to continue to provide an average rate of return in excess of the 5% distributed from the funds, allowing for increases in value. Treehouse's investment policy states that the assets in the Fostering Futures Endowment are to be invested in 80% equity securities and 20% fixed income securities and performance will be evaluated against the S&P 500 and Barclay's Capital Aggregate Bond Index. Actual returns in any given year may vary.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, Treehouse 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). Following donor restrictions, two of its Endowments are invested in equity securities with the remaining invested in fixed income securities to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

Treehouse follows the donors' request of appropriating for distribution each year 5% of the average ending balances of the previous 12 quarters of its Operations and Education Endowment Fund's value. No funds from the Fostering Futures Endowment will be expended until the balance of the fund grows to \$1,000,000.

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level of original value of the gifts donated. There were no deficiencies of this nature as of September 30, 2013.

Note 6. Lease

Treehouse's current office lease, expiring January 2015, is at a below market rate. The contribution receivable for rent represents the fair value of rent contributed to Treehouse in excess of the actual rent to be paid. The receivable represents the entire contribution over the remaining term of the office lease. The full amount of the contributed rent to be received is \$226,006 at September 30, 2013, which has been discounted at an interest rate of 1.65% to result in a contribution receivable of \$225,243 at September 30, 2013. The amounts are due in the following periods ending September 30:

	Recognized Contribution Receivable	Discount (Interest Portion)	Total
2014	\$ 179,841	\$ -	\$ 179,841
2015	45,402	763	46,165
	<u>\$ 225,243</u>	<u>\$ 763</u>	<u>\$ 226,006</u>

The future minimum lease payments (cash portion) under the office lease are \$221,550 and \$55,593 for the years ending September 30, 2014 and 2015, respectively.

Rent expense for the years ended September 30, 2013 and 2012, was \$401,169 and \$395,721, respectively. The in-kind portion of rent expense was \$180,203 and \$132,486 for the years ended September 30, 2013 and 2012, respectively.

Note 7. Retirement Plan

In July 2013, Treehouse began sponsoring a defined contribution 403(b) plan for employees who meet the eligibility requirements set forth in the plan. Treehouse's contributions were \$20,232 for the year ended September 30, 2013.