



Houston Ballet Foundation and Houston Ballet Guild, Inc.

Combined Financial Statements

As of and for the Year Ended June 30, 2019

**Houston Ballet Foundation and
Houston Ballet Guild, Inc.**

Combined Financial Statements

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Independent Auditor's Report

To the Board of Trustees of the
Houston Ballet Foundation and Houston Ballet Guild, Inc.
Houston, Texas

We have audited the accompanying combined financial statements of the Houston Ballet Foundation and its affiliate, Houston Ballet Guild, Inc. (collectively, the "Foundation"), which comprise the combined statement of financial position as of June 30, 2019, and the related combined statement of activities, cash flows and functional expenses for the year then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Combined Financial Statements

Management is responsible for the preparation and fair presentation of these combined 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 combined 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 combined financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined 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 combined 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 combined 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 combined financial statements referred to above present fairly, in all material respects, the combined financial position of the Foundation as of June 30, 2019, and the changes in their net assets and their cash flows for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

BDO USA, LLP

September 17, 2019

Combined Financial Statements

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Combined Statement of Financial Position

<i>June 30, 2019</i>	General Fund	Endowment Fund	Plant Fund	Total
Assets				
Current Assets				
Cash and cash equivalents	\$ 6,388,779	\$ 2,490,452	\$ 7,985,668	\$ 16,864,899
Pledges receivable	2,093,869	1,250,000	-	3,343,869
Other receivables	32,998	-	-	32,998
Prepaid and deferred production expenses	1,196,930	-	-	1,196,930
Total Current Assets	9,712,576	3,740,452	7,985,668	21,438,696
Pledges receivable	268,885	35,000	-	303,885
Investments, at fair value	966,213	76,763,661	-	77,729,874
Fixed assets, net	575,046	-	42,229,330	42,804,376
Total Assets	\$ 11,522,720	\$ 80,539,113	\$ 50,214,998	\$ 142,276,831
Liabilities and Net Assets				
Liabilities				
Current Liabilities				
Accounts payable and accrued liabilities	\$ 1,662,577	\$ -	\$ -	\$ 1,662,577
Deferred revenue	5,955,662	-	-	5,955,662
Due to (from) other funds	7,622	(18,855)	11,233	-
Total Current Liabilities	7,625,861	(18,855)	11,233	7,618,239
Deferred revenue	25,000	-	-	25,000
Total Liabilities	7,650,861	(18,855)	11,233	7,643,239
Commitments and Contingencies (Notes 11 and 12)				
Net Assets				
Without donor restrictions	1,014,266	45,060,517	50,203,765	96,278,548
With donor restrictions	2,857,593	35,497,451	-	38,355,044
Total Net Assets	3,871,859	80,557,968	50,203,765	134,633,592
Total Liabilities and Net Assets	\$ 11,522,720	\$ 80,539,113	\$ 50,214,998	\$ 142,276,831

See accompanying notes to combined financial statements.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Combined Statement of Activities

<i>Year Ended June 30, 2019</i>	Without Donor Restrictions	With Donor Restrictions	Total
Operating Income			
Performance	\$ 9,469,351	\$ -	\$ 9,469,351
Tuition	4,365,764	-	4,365,764
Special events	11,987,882	-	11,987,882
Investment	1,732,533	-	1,732,533
Other	1,371,974	-	1,371,974
Total Operating Income	28,927,504	-	28,927,504
Operating Expenses			
Production and company	18,367,077	-	18,367,077
Ballet academy	5,332,466	-	5,332,466
Marketing and public relations	4,850,001	-	4,850,001
Fund-raising	2,684,606	-	2,684,606
General and administrative	2,147,688	-	2,147,688
Special events	4,968,892	-	4,968,892
Total Operating Expenses	38,350,730	-	38,350,730
Decrease in Net Assets from Operating Activities Before Public and Private Support, Releases from Restrictions and Transfers	(9,423,226)	-	(9,423,226)
Public and Private Support Contributions	5,003,181	2,717,593	7,720,774
Increase (Decrease) in Net Assets from Operating Activities Before Releases from Restrictions and Transfers	(4,420,045)	2,717,593	(1,702,452)
Net Assets Released from Restrictions	4,416,523	(4,416,523)	-
Decrease in Net Assets from Operating Activities Before Interfund Transfers	(3,522)	(1,698,930)	(1,702,452)
Interfund Reclassification	17,657	-	17,657
Increase (Decrease) in Net Assets from Operating Activities	14,135	(1,698,930)	(1,684,795)
Endowment Activities			
Contributions	-	24,169	24,169
Investment income	-	3,897	3,897
Net appreciation on investments	2,597,186	-	2,597,186
Expenses	-	(19,296)	(19,296)
Interfund reclassification	(250,000)	-	(250,000)
Increase in Net Assets from Endowment Activities	2,347,186	8,770	2,355,956
Plant Activities			
Contributions	287,410	-	287,410
Net assets released from restrictions	365,000	(365,000)	-
Interest and other income	144,783	-	144,783
Depreciation expense	(1,427,153)	-	(1,427,153)
Interfund reclassification	232,343	-	232,343
Decrease in Net Assets from Plant Activities	(397,617)	(365,000)	(762,617)
Total Increase (Decrease) in Net Assets	1,963,704	(2,055,160)	(91,456)
Net Assets, beginning of year	94,314,844	40,410,204	134,725,048
Net Assets, end of year	\$ 96,278,548	\$ 38,355,044	\$ 134,633,592

See accompanying notes to combined financial statements.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Combined Statement of Cash Flows

<i>Year Ended June 30, 2019</i>	General Fund	Endowment Fund	Plant Fund	Total
Cash Flows from Operating Activities				
Total increase (decrease) in net assets	\$ (1,684,795)	\$ 2,355,956	\$ (762,617)	\$ (91,456)
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:				
Net realized and unrealized gains on investments	-	-	-	-
Depreciation expense	(67,600)	(2,597,186)	-	(2,664,786)
Changes in operating assets and liabilities:				
Pledges receivable	1,860,216	-	1,427,153	3,287,369
Other receivables	463,948	-	-	463,948
Prepaid and deferred production expenses	144,027	-	-	144,027
Accounts payable and accrued liabilities	(88,820)	-	-	(88,820)
Deferred revenue	(867,850)	(10,045)	20,027	(857,868)
	1,035,585	-	-	1,035,585
Net Cash Provided by (Used in) Operating Activities	794,711	(251,275)	684,563	1,227,999
Cash Flows from Investing Activities				
Capital expenditures	(573,852)	-	(868,896)	(1,442,748)
Purchase of investments	(532,194)	(9,602,876)	-	(10,135,070)
Investment expense payments	(1,661)	(242,060)	-	(243,721)
Proceeds from sales and maturities of investments	-	-	-	-
	503,329	9,505,242	-	10,008,571
Net Cash Used in Investing Activities	(604,378)	(339,694)	(868,896)	(1,812,968)
Net Increase (Decrease) in Cash and Cash Equivalents	190,333	(590,969)	(184,333)	(584,969)
Cash and Cash Equivalents, beginning of year	6,198,446	3,081,421	8,170,001	17,449,868
Cash and Cash Equivalents, end of year	\$ 6,388,779	\$ 2,490,452	\$ 7,985,668	\$ 16,864,899

See accompanying notes to combined financial statements.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Combined Statement of Functional Expenses

<i>Year Ended June 30, 2019</i>	Program Services		Support Services				Total
	Production and Company	Ballet Academy	Marketing and Public Relations	General and Administrative	Fund- Raising	Special Events	
Advertising	\$ 180	\$ 189,123	\$ 2,027,328	\$ -	\$ 187,267	\$ -	\$ 2,403,898
Computer maintenance, software	50,335	74,691	74,691	74,692	50,335	-	324,744
Costumes, scenery and designers	934,653	-	-	-	-	-	934,653
Depreciation	2,359,720	499,504	142,715	142,715	142,715	-	3,287,369
Donor benefit expenses	-	-	-	-	-	4,968,892	4,968,892
Equipment rentals	1,252	1,252	358	358	358	-	3,578
Insurance	135,418	135,418	38,691	38,691	38,691	-	386,909
Music and royalties	245,162	-	-	-	-	-	245,162
Office supplies	15,398	13,708	20,179	16,399	15,852	-	81,536
Postage and handling	5,282	2,726	5,949	3,071	11,599	-	28,627
Printing	-	-	503,298	-	8,967	-	512,265
Professional fees	-	-	-	197,162	-	-	197,162
Repairs and maintenance	546,591	154,083	44,024	44,021	44,024	-	832,743
Salaries, payroll taxes and employee benefits	12,882,343	2,438,180	1,350,582	1,408,652	2,028,866	-	20,108,623
Scholarships	-	869,328	-	-	-	-	869,328
Shipping and freight	199,311	-	-	-	-	-	199,311
Shoes and tights	138,740	-	-	-	-	-	138,740
Stage equipment and supplies	163,823	-	-	-	-	-	163,823
Stipends and subsidized housing	-	325,672	-	-	-	-	325,672
Summer housing	-	582,198	-	-	-	-	582,198
Telephone and utilities	166,617	166,547	47,585	47,587	47,585	-	475,921
Theater costs	704,200	-	-	-	-	-	704,200
Ticket service, booking fees	-	-	267,270	-	-	-	267,270
Travel and entertainment	293,044	154,691	17,105	32,875	37,688	-	535,403
Miscellaneous	24,512	224,849	452,941	303,476	213,374	-	1,219,152
	\$ 18,866,581	\$ 5,831,970	\$ 4,992,716	\$ 2,309,699	\$ 2,827,321	\$ 4,968,892	\$ 39,797,179

See accompanying notes to combined financial statements.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

1. Nature of Operations

The Houston Ballet Foundation was founded in 1955 for educational purposes, namely, spreading an appreciation of ballet in general. The Foundation created the Academy to provide professional ballet training for dancers and, subsequently, in 1969, created a resident professional ballet Company.

The Houston Ballet Guild, Inc. (the “Guild”) is a not-for profit corporations established in 1974 to provide aid and support to Houston Ballet Foundation. The Guild consists of members who volunteer their services to support the Houston Ballet Foundation.

The accompanying combined financial statements include the accounts of Houston Ballet Foundation and its affiliated support organization, Houston Ballet Guild, Inc. (collectively, the “Foundation”). The by-laws of the Guild provide that all funds raised be distributed to Houston Ballet Foundation.

2. Summary of Significant Accounting Policies

The combined financial statements of the Foundation have been prepared on the accrual basis of accounting. The Foundation is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code. Significant accounting policies followed by the Foundation are described below.

Basis of Presentation

The Foundation’s net assets and its revenue, expenses, gains and losses are classified within the statements based on the existence or absence of donor-imposed restrictions. All significant interfund accounts between the Houston Ballet Foundation and the Guild have been eliminated.

The classification of a not-for-profit organization's net assets and its support, revenue and expenses is based on the existence or absence of donor-imposed restrictions. It requires that the amounts for each of the classes of net assets—with donor restrictions and without donor restrictions—be displayed in a statement of financial position and that the amounts of change in each of those classes of net assets be displayed in a statement of activities.

These classes are defined as follows:

With Donor Restrictions - This class consists of net assets resulting from contributions and other inflows of assets whose use by the Foundation is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Foundation, pursuant to those stipulations. When such stipulations end or are fulfilled, such donor-restricted net assets are reclassified to net assets without donor restrictions and reported in the statement of activities. Net assets resulting from contributions and other inflows of assets whose use by the Foundation is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or other removed by actions of the Foundation are classified as net assets with donor restrictions- perpetual in nature.

Without Donor Restrictions - This class consists of the part of net assets that is not restricted by donor-imposed stipulations.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

Preproduction Expenses and Advance Ticket Sales

Program revenues and expenses are recognized in the program year to which they apply. Ticket sales and preproduction costs for future season's programs are recorded as deferred revenue and deferred production expenses, respectively.

Pledges Receivable

Pledges made by donors are initially considered to be net assets with donor restriction and become net assets without donor restriction upon satisfaction of such restriction, which is typically a stipulated time restriction or purpose restriction. Pledges receivable are primarily from large foundations and corporations.

Pledges receivable represent unconditional promises to give and are monitored by the Foundation for potential losses.

Pledges deemed uncollectible are written off against related revenue or contributions. The Foundation has determined, through review of its donors' pledge payment history, that no allowance for uncollectible amounts is necessary as of June 30, 2019.

Contributions

The Foundation accounts for contributions received, including unconditional promises to give, as revenue in the period received at their fair values. The Foundation also distinguishes between contributions that increase net assets without donor restrictions and net assets with donor restrictions. The Foundation reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, with donor restrictions net assets are reclassified to without donor restrictions net assets and reported in the statement of activities as net assets released from restrictions. Donor-restricted contributions whose restrictions are met in the same reporting period are reported as without donor restrictions.

Fixed Assets

Fixed assets include land, building, equipment and costumes and sets related to full-length productions and are recorded at cost. Depreciation of building and equipment is provided over the estimated useful lives of the respective assets on a straight-line basis. Depreciation of costumes and sets related to full-length productions is provided on a straight-line basis over three years, beginning in the year the production is initially performed. Depreciation expense for the year ended June 30, 2019 totaled \$3,287,369. The Foundation did not recognize any impairment charges in fiscal year ended June 30, 2019.

Production and Foundation Costs

Production costs for ballet performances include the salaries of performers, cost of costumes, stage sets, theater rental, orchestra fees and other related expenses. All such costume and stage set costs related to full-length productions are capitalized and depreciated as described above. All other production expenses such as the salaries of performers, theater rental and orchestra fees are expensed in the year of the performance.

Foundation costs include salaries and benefits for dancers, artistic staff and music staff, costs for guest artists and guest music conductors and other miscellaneous expenses.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

Functional Expenses

The financial statements report certain categories of expenses that are attributable to one or more program or supporting functions. These expenses include depreciation, salaries and payroll expenses of the artistic and executive directors, information technology and facilities. Depreciation and facilities are allocated based on square footage. Salaries and payroll expenses of the artistic and executive directors are allocated based on estimates of time and effort. Information technology is allocated based on the numbers of the computers.

Advertising

All costs of advertising that relate to the current year are expensed as incurred. Costs related to productions or events in the subsequent year are recorded as prepaid expense and are expensed at the time the performance or event takes place.

Cash Equivalents

For purposes of the combined statement of cash flows, the Foundation considers all highly liquid investments with an original maturity date of three months or less to be cash equivalents.

Investments and Investment Income

The Foundation accounts for investments in equity securities with readily determinable fair market values and all investments in debt securities at fair market value with gains and losses included in the combined statement of activities.

Endowment funds, which consist primarily of marketable securities, are pooled for investment management purposes. Income from investments is allocated to each endowment based upon the relative market value and the type of endowment.

Investment income, including realized and unrealized gains or losses on investments, is recorded as without donor restrictions for all funds because there are no donor-imposed restrictions. For the year ended June 30, 2019, as stipulated by the Foundation's investment policy, up to 5.5% of the market value of endowment investments and cash may be used for general operating activities. Realized and unrealized gains or losses on endowment investments were reinvested and recorded in endowment activities on the combined statement of activities.

Donated Services and Materials

A substantial number of volunteers have donated time in connection with program services and administration of the Foundation. No value has been reflected in the financial statements for these services because the services would not typically be purchased if they had not been provided by donation. When outside services are donated to the Foundation and the services received (a) create or enhance non-financial assets, or (b) require specialized skills and are provided by individuals possessing those skills and would typically need to be purchased if not provided by donation, a contribution is recorded in the period received. Such contribution is valued at the estimated cost to the Foundation had the services and/or materials cost been purchased. The Foundation recorded \$2,551,997 in the General Fund for donated services and materials during the year ended June 30, 2019, including \$2,309,534 of donated services and materials for special events in the operating income and operating expense in the accompanying combined statement of activities.

Non-Monetary Transactions

During the year ended June 30, 2019, \$237,882 of Houston Ballet Foundation performance tickets were traded in exchange for marketing, public relations, production and development purposes. Such amounts are recorded as both performance income and operating expenses.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

Concentrations of Credit Risk

The Foundation is subject to concentrations of credit risk relating primarily to cash, pledges receivable, and marketable securities. The Foundation's cash and cash equivalent deposits are held in major financial institutions in excess of the federally insured limit. The Foundation has not experienced any losses in such accounts and management believes it is not exposed to any significant credit risk on cash and cash equivalents. Pledges receivable represent unconditional promises to give and are monitored by the Foundation for potential losses. Marketable securities consist primarily of domestic corporate stocks, which could subject the Foundation to losses in the event of a general downturn in the stock market. The Foundation has reduced its risk relating to investment in corporate stocks and bonds through diversification into investments in a variety of industries.

Estimates

The preparation of the Foundation's financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the combined financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from these estimates.

Income Taxes

Houston Ballet Foundation and Houston Ballet Guild, Inc. are both nonprofit organizations which have been recognized as tax-exempt pursuant to Section 501(c)(3) of the Internal Revenue Code and neither are private foundations. For the year ended June 30, 2019, the cost of employee parking benefits, which are taxable as unrelated business income, is expected to result in an immaterial amount of income tax. Estimated income tax was paid during the year ended June 30, 2019 and the total expected amount of tax due is reflected in the accompanying combined statement of activities.

The Foundation follows current guidance in accounting for uncertainty in income taxes. This guidance clarifies the accounting for income taxes by prescribing the minimum recognition threshold an income tax position is required to meet before being recognized in the financial statements and applies to all income tax positions. Each income tax position is assessed using a two-step process. A determination is first made as to whether it is more likely than not that the income tax position will be sustained, based upon technical merits, upon examination by the taxing authorities. If the income tax position is expected to meet the more likely than not criteria, the benefit recorded in the financial statements equals the largest amount that is greater than 50% likely to be realized upon its ultimate settlement. The Foundation had no uncertain tax positions as of June 30, 2019.

The income tax position taken by the Foundation, for any years open under the various statutes of limitations, is that the Foundation continues to be exempt from income taxes by virtue of being a nonprofit organization. Management believes this tax position meets the more-likely-than-not threshold and, accordingly, the tax benefit of this income tax position (no income tax liability) has been recognized for the years ended on or before June 30, 2019.

The Foundation will record income tax related interest and penalties, if applicable, as a component of the provision for income tax expense. However, there were no amounts recognized relating to interest and penalties in the statement of activities for the year ended June 30, 2019. The Foundation's federal exempt organization business tax returns (Form 990) for 2015 and later are subject to examination by the Internal Revenue Service.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

Recent Accounting Pronouncements

In August 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-14, *Not-for-Profit Entities - Presentation of Financial Statements of Not-for-Profit Entities*. The ASU amends the current reporting model for nonprofit organizations and enhances their required disclosures. The major changes include (a) requiring the presentation of only two classes of net assets now entitled “net assets without donor restrictions” and “net assets with donor restrictions”, (b) modifying the presentation of underwater endowment funds and related disclosures, (c) requiring the use of the placed in service approach to recognize the expirations of restrictions on gifts used to acquire or construct long-lived assets absent explicit donor stipulations otherwise, (d) requiring that all nonprofits present an analysis of expenses by function and nature in either the statement of activities, a separate statements, or in the notes and disclose a summary of the allocation methods used to allocate costs, (e) requiring the disclosure of quantitative and qualitative information regarding liquidity and availability of resources, (f) presenting investment return net of external and direct expenses, and (g) modifying other financial statement reporting requirements and disclosures intended to increase the usefulness of nonprofit financial statements. The ASU is effective for the Foundation’s combined financial statements for fiscal years beginning after December 15, 2017. Early adoption is permitted. The provisions of the ASU must be applied on a retrospective basis for all years presented although certain option practical expedients are available for periods prior to adoptions. The Foundation has chosen to adopt this ASU as of and for the year ended June 30, 2019.

Revenue from Contracts with Customers

In May 2014, the FASB issued ASU 2014-09, “Revenue from Contracts with Customers,” which supersedes nearly all existing revenue recognition guidance under GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU 2014- 09 defines a five-step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process that are required under existing GAAP. The standard is effective for annual periods beginning after December 15, 2018 for nonpublic entities (though early adoption is permitted), and interim periods therein, using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures). The Foundation is currently evaluating the impact of this ASU on its financial statements.

Accounting for Leases

In February 2016, the FASB issued ASU 2016-02, “Leases,” to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the statement of financial position and disclosing key information about leasing arrangements for lessees and lessors. The new standard applies a right-of-use (ROU) model that requires, for all leases with a lease term of more than 12 months, an asset representing its right to use the underlying asset for the lease term and a liability to make lease payments to be recorded. The ASU is effective for the Foundation’s fiscal years beginning after December 15, 2019 with early adoption permitted. The Foundation is currently evaluating the impact of this ASU on its financial statements.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

3. Fair Value Disclosure

The Foundation follows current guidance on fair value measurements which defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the quality of inputs used to measure fair value and enhances disclosure requirements for fair value measurements.

Current guidance establishes a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy categorizes assets and liabilities measured at fair value into one of three different levels depending on the observability of the inputs employed in the measurement. The three levels are defined as follows:

Level 1 - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 - inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The Foundation's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability. The following table presents information about the Foundation's assets measured at fair value on a recurring basis, and indicates the fair value hierarchy of the valuation techniques utilized by the Foundation to determine such fair value:

	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable Items (Level 2)	Significant Unobservable Items (Level 3)	Balance at June 30, 2019
General Fund				
Corporate stocks and mutual funds	\$ 966,213	\$ -	\$ -	\$ 966,213
Endowment Fund				
Corporate stocks and mutual funds	69,569,916	-	-	69,569,916
Total Investments at Fair Value	70,536,129	-	-	70,536,129
Investments Measured at Net Asset Value *	-	-	-	7,193,745
Total Fair Value of Investments	\$ 70,536,129	\$ -	\$ -	\$ 77,729,874

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

* Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the Statements of Net Assets Available for Benefits.

For the investment measured at net asset value, there are no unfunded commitments, redemption frequency, or redemption notice period.

4. Investments

Investment returns for all funds are classified as without donor restrictions on the combined statement of activities. The components of investment returns for each fund for the year ended June 30, 2019 were as follows:

	General Fund	Endowment Fund	Plant Fund	Total
Interest and dividend income	\$ 211,845	\$ 1,456,985	\$ 144,783	\$ 1,813,613
Net realized gains	37,139	1,056,178	-	1,093,317
Net unrealized gains	32,122	1,783,068	-	1,815,190
Investment expenses	(1,661)	(242,060)	-	(243,721)
	279,445	4,054,171	144,783	4,478,399
Amounts designated for general operating activities	(279,445)	(1,453,088)	-	(1,732,533)
Excess of amounts designated for general operating activities	\$ -	\$ 2,601,083	\$ 144,783	\$ 2,745,866

Total cumulative net unrealized gains on General Fund and Endowment Fund investments held at June 30, 2019 were \$297,386 and \$23,567,068, respectively.

Investments consisted of the following as of June 30, 2019:

	General Fund		Endowment Fund	
	Cost	Market	Cost	Market
Domestic Equity Securities	\$ 668,827	\$ 966,213	\$ 20,373,664	\$ 38,002,002
Government Bonds	-	-	6,095,404	6,143,755
International Equity securities	-	-	12,414,547	14,798,026
Hedged Equity securities	-	-	8,312,978	10,626,133
Absolute Return Fund	-	-	6,000,000	7,193,745
	\$ 668,827	\$ 966,213	\$ 53,196,593	\$ 76,763,661

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

5. Fixed Assets

The following components are included in land, building, equipment, and costumes and sets at June 30, 2019:

	Estimated Useful Life		
Buildings and improvements	15-39 years	\$	40,117,201
Office furniture and equipment	5-7 years		4,329,975
Costumes and sets	3 years		13,087,393
			57,534,569
Less: accumulated depreciation			(24,526,565)
			33,008,004
Land	N/A		9,689,178
Improvements in progress			107,194
Costumes and sets-production in progress			-
			\$ 42,804,376

6. Special Events

The Guild is an affiliated, nonprofit organization that sponsors various fund-raising activities throughout the year for the benefit of the Foundation. The Guild's largest fund-raising event include operating the annual Nutcracker Market in November and the annual Nutcracker Market Spring Spectacular in April. The revenues and expenses of the Guild are presented as special events on the combined statement of activities.

7. Pledges

The Foundation continues its pursuit of endowment funds to guarantee future financial security. Multi-year pledges receivable are recorded at present value on the date of the pledge for the amount of discounted cash flows using an interest rate of approximately 2%. The Foundation also receives pledges for annual operations, which are recorded in the General Fund.

As of June 30, 2019, pledges receivable were:

	General Fund	Plant Fund	Endowment Fund	Total
Less than one year	\$ 2,093,869	\$ -	\$ 1,250,000	\$ 3,343,869
One to five years	268,885	-	-	268,885
Greater than five years	-	-	35,000	35,000
				\$ 2,362,754 \$ - \$ 1,285,000 \$ 3,647,754

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

8. Endowments

The Foundation follows current guidance on net asset classification of endowments. This guidance clarifies the accounting for donor-restricted endowment funds for a nonprofit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). This guidance also requires additional disclosures about an organization's endowment funds (both donor-restricted endowment funds and board-designated endowment funds) whether or not the organization is subject to UPMIFA.

Balances of the funds included in with donor restriction net assets for permanent purpose at June 30, 2019 were as follows:

Endowment Funds:	
Use of income is without restrictions	\$ 35,293,230
Use of income is restricted for:	
Dancer Career Transition - Artists Reserve Fund	204,221
Total Endowment Funds	\$ 35,497,451

Endowment funds with unrestricted use of income are as follows:

- *The Endowed Artistic Positions Fund* - assists Houston Ballet in attracting talented artists.
- *The Fayez Sarofim & Co. Touring Fund* - sponsors Houston Ballet's domestic and international tours.
- *The Carolyn Lee and Frederick Adrian Lee Production Fund* - supports the creation of new productions and the restoration of existing works.
- *The Margaret Wiess Elkins Young Artist Fund* - trains talented young people for careers in dance.
- *The AIG American General/AIG VALIC Education and Community Outreach Programs Fund* - helps Houston Ballet reach a broad population of all ages and economic levels.
- The Albert and Margaret Alkek Foundation endowed the *Margaret Alkek Williams Jubilee of Dance*, Houston Ballet's annual gala performance.
- *The Billie Bath Perlman Scholarship Fund; The Roy M. Huffington Scholarship Fund; The Ben Stevenson Scholarship Fund; The Winifred Wallace Scholarship Fund; The Anita Borges Stude Scholarship Fund; The C.C. Conner Scholarship Fund*- each provides the full cost for training one Houston Ballet II dancer each year.
- *The Ira and Myra Brown Young Dancer Scholarship Fund* - provides the full cost for training for five Academy students each year.

The Foundation's endowments consist of funds established for a variety of purposes. Its endowments include donor-restricted funds. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

The Foundation's Board has interpreted the UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as net assets with donor restriction for permanent purpose, the original value of subsequent gifts to the permanent endowment, and accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. In accordance with UPMIFA, the Foundation 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 Foundation 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 Foundation, and the investment policies of the Foundation.

Board-designated funds are used to support program services and may be released for general operations when the Foundation approves the release.

The endowment net asset composition by type of fund as of June 30, 2019 was as follows:

	Without Donor Restrictions	With Donor Restrictions	Total
Endowment Funds:			
With donor restrictions			
Purpose restricted	\$ -	\$ 35,497,451	\$ 35,497,451
Total with donor restrictions	-	35,497,451	35,497,451
Without donor restrictions			
Unrestricted	40,087,183	-	40,087,183
Board-designated	4,973,334	-	4,973,334
Total without donor restrictions	45,060,517	-	45,060,517
Total Endowment Funds	\$ 45,060,517	\$ 35,497,451	\$ 80,557,968

The changes in endowment net assets for the year ended June 30, 2019 were as follows:

	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, beginning of year	\$ 42,713,331	\$ 35,488,681	\$ 78,202,012
Investment return:			
Investment income	1,453,088	3,897	1,456,985
Net realized and unrealized appreciation	2,839,246	-	2,839,246
Total investment return	4,292,334	3,897	4,296,231
Contributions	-	24,169	24,169
Investment expenses	(242,060)	-	(242,060)
Appropriation of endowment assets for expenditures	(1,703,088)	(19,296)	(1,722,384)
Endowment net assets, end of year	\$ 45,060,517	\$ 35,497,451	\$ 80,557,968

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

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 UPMIFA requires the Foundation to retain as a fund of perpetual duration. In accordance with accounting principles generally accepted in the United States of America, there were no deficiencies of this nature as of June 30, 2019.

The Foundation 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 maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Foundation must hold in perpetuity or for a donor-specified period.

9. Description of Program and Supporting Services

The following program and supporting services are included in the accompanying consolidated statements of activities:

Program Services

Production and Company

The Foundation supports a professional company of dancers and engages audiences throughout the city of Houston and the world with its performances and programs each year. Production and Company program services include expenditures for salaries of performers, production of stage sets and costumes, theater rental and other related expenses in connection with producing and staging ballet performances and programs locally, nationally and internationally.

Ballet Academy

The Foundation's Ballet Academy trains over 1,000 unique students each year. The artistic team includes many teaching artists and live accompanists that work to conduct a variety of weekly classes for all levels, ranging from pre-school students to Houston Ballet II dancers, the Foundation's second company, as well as adult students. The Foundation's Education and Community Engagement programs captivate the imagination of kindergarten-12th grade students, adults and children living with disabilities, and unite communities through a multitude of school and community programs.

Supporting Services

General and Administrative

General and Administrative expenditures include those related to other areas and departments that ensure the success of the Foundation's performances, programs, professional company, Academy, and community outreach efforts.

Marketing and Public Relations

Marketing and Public Relations services provides support in all brand identity and consistency matters including marketing, advertising and other promotional collateral designed to promote the activities, performances and programs of the Foundation. These services also promote media and public relations by managing campaigns through production of video, television, radio, and print media and overseeing all activities relating to ticket sales and promotion of the Foundation's production performances.

Fundraising

Fundraising supporting services include expenditures which provide the structure necessary to encourage and secure both public and private financial support. Fundraising activities include expenses towards donor cultivation activities and donor benefits for their support as well as benefits for corporate sponsors of production performances and education and community engagement programs. Fundraising supporting services both promote the Foundation and provide important support toward operations.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

Special Events

This supporting service category includes expenditures for special events which both promote the Foundation and provide support for operations. These events help grow the Foundation's donor base, promote the Foundation's operations, and engage the Foundation's constituents and stakeholders in activities outside of performances.

10. Net Assets - General and Plant Funds

Net assets - general and plant funds consist of the following:

	Without Donor Restrictions	With Donor Restrictions	Total
General Fund:			
With donor restrictions			
Time restricted only, for periods after June 30, 2019	\$ -	\$ 2,857,593	\$ 2,857,593
Without donor restrictions	1,014,266	-	1,014,266
Total General Fund	\$ 1,014,266	\$ 2,857,593	\$ 3,871,859
Plant Fund:			
Without donor restrictions	\$ 50,203,765	\$ -	\$ 50,203,765
Total Plant Fund	\$ 50,203,765	\$ -	\$ 50,203,765

When the donor-imposed stipulations are either expired by passage of time or fulfilled by actions of the Foundation, pursuant to those stipulations, such donor-restricted net assets are reclassified to net assets without donor restrictions and reported in the statement of activities.

11. Employee Benefits

The Foundation contributes to a defined contribution retirement plan represented by Variable Annuity Life Insurance Company ("VALIC") for the benefit of all dancers and all qualified, nonunion employees. This plan is administered by VALIC. Contributions to the VALIC plan aggregated \$599,670 for the year ended June 30, 2019.

The Foundation contributes to a defined contribution retirement plan for the benefit of all musicians represented by American Federation of Musicians ("AFM"). Contributions to this plan, administered by AFM, aggregated \$100,212.

The Foundation has a tax-sheltered annuity program for the benefit of its employees. Participating employees may contribute up to 20% of their annual income to one of the programs. All contributed amounts are managed by an independent trustee and are exempt from federal income taxes until such time as they are withdrawn.

The Foundation provides health insurance for all union dancers and qualified, nonunion employees through American Guild of Musical Artists ("AGMA"). Premiums paid by the Foundation for such insurance were \$1,885,621 for the year ended June 30, 2019.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

The Foundation provides dental insurance for qualified nonunion employees. Premiums paid by the Foundation for such insurance were \$41,512 for the year ended June 30, 2019.

The Foundation has an agreement to pay a retirement benefit of \$55,000 per year, to a former employee. The actuarially determined liability for this obligation was recalculated assuming a life expectancy of 18.4 years and an investment return of 7.5%. The balance of the liability of \$47,972 for this obligation and the fair market value of the related investment assets of \$289,433 are included in the combined statement of financial position as of June 30, 2019. The employee retired and was vested in the plan as of July 1, 2003. Distributions in the aggregate amount of \$37,908, net of tax, were paid during the year ended June 30, 2019.

The Foundation has an agreement to pay a current employee deferred compensation of \$20,000 per annum plus 5% interest beginning July 1, 2010 over the duration of employment. The deferred compensation amounts will vest at 75% four years after the effective date and payments began on July 1, 2014. If the employee is still employed on his 55th birthday or acting in his service capacity with the Foundation on either his retirement date or on his involuntary termination date, all amounts will vest 100%. In addition, all amounts will become 100% vested on date of death or disability, as applicable. The balance of the liability of \$145,778 for this obligation is included in the combined statement of financial position as of June 30, 2019 and the vested amounts will be paid out of general assets of the Foundation, although a separate investment account to fund the liability was established in July 2011.

The Foundation entered into an agreement to pay a 15-year retirement benefit of \$30,000 per year, cost of living adjusted annually at a rate of 3.0%, beginning in March 2015 to a former employee. The actuarially determined liability for this obligation was calculated using an investment return of 4.5%. The balance of the liability of \$207,076 for this obligation is included in the combined statements of financial position as of June 30, 2019 and will be paid out of general assets of the Foundation.

The Foundation entered into an agreement to contribute to a section 457(b) "top hat" plan on behalf of four current employees in an amount up to or equal to the maximum amount allowed by IRS guidelines, currently \$19,000 per calendar year. The net balance of the liability for these obligations as of June 30, 2019 is \$547,642 and is included in the combined statement of financial position and will be paid out of general assets of the Foundation.

12. Commitments and Contingencies

Grants, bequests and endowments require the fulfillment of certain conditions as set forth in the instructions of the gift. The Foundation intends to fulfill the conditions of all bequests, grants and endowments, recognizing that failure to fulfill the conditions could result in the return of the funds to donors. The Foundation, by accepting the gifts and their terms, has agreed to the conditions of the donor. Management believes that the Foundation has complied with all donors' conditions.

The Foundation entered into a lease agreement with the Wortham Theater Foundation in May 1987, and the Foundation has the right to terminate the lease at any time, after giving six months written notice. Box office space is also leased. Rent expense for the year ended June 30, 2019 for these leases was \$289,179.

In June 2016, the Foundation entered into an agreement to lease 10 apartments to use as subsidized housing for upper level students at Houston Ballet. The 56-month lease term began in November 2016. Lease payments relating to these leases were \$218,663 and the related rent expense, recognized on a straight-line basis, was \$214,675 during the fiscal year ended June 30, 2019.

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

The scheduled future minimum lease payments under operating leases as of June 30, 2019 are:

<i>Year Ending June 30,</i>	
2020	\$ 226,417
2021	231,069
	\$ 457,486

General Liability Claims

The Foundation is, from time to time, subject to claims and suits arising in the ordinary course of business, including claims for damages for personal injuries and employment related claims. In certain of these actions, plaintiffs request punitive or other damages against the Foundation which may be covered by insurance. The Foundation is currently not a party to any proceeding which, in management's opinion, would have a material adverse effect on the Foundation's business, financial condition or results of operations.

13. Liquidity

The Foundation plans each year to provide funding for operating expenditures through a combination of earned income, special events net income, investment income and interfund transfers, including an annual allocation from its Endowment Fund. The Foundation's investment policy allows a withdrawal for any fiscal year not to exceed 5.5% of the trailing three-year average of the total value of the Endowment Fund. The Foundation maintains high liquidity and low risk through cash and cash equivalents and longer-term investments in the General Fund, maintains cash and cash equivalents in the Plant Fund and maintains cash and cash equivalents as well as longer-term investments in the Endowment Fund.

Financial assets available within one year of the statement of financial position date for general expenditure are as follows:

Cash and cash equivalents	\$ 14,374,447
Accounts and interest receivable	32,998
Amounts due to (from) general and plant funds	(18,855)
Contributions receivable	2,093,869
Investments appropriated for current use - general fund	966,213
Investments appropriated for current use - endowment fund	3,945,457
Financial assets available within one year of the statement of financial position date for general expenditure	
	\$ 21,394,129

The investments appropriated for current use - endowment fund represent 5.5% of the trailing three-year average of cash and investments (net of due to/from other funds).

Houston Ballet Foundation and Houston Ballet Guild, Inc.

Notes to Combined Financial Statements

Financial assets available to meet cash needs for general expenditures within one year are as follows:

Financial assets at June 30, 2019	\$ 98,275,525
Less those unavailable for general expenditures within one year, due to:	
Contractual or donor-imposed restrictions:	
Restricted by donor with time or purpose restrictions	(1,553,885)
Subject to appropriation and satisfaction of donor restrictions	(70,354,177)
Board designations:	
Endowment funds	(4,973,334)

Financial assets available to meet cash needs for general expenditures within one year	\$ 21,394,129
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14. Subsequent Events

The Foundation has evaluated subsequent events through September 17, 2019 for recognition or disclosure, which is the date these combined financial statements were available for issuance.