

INSTITUTE FOR JUSTICE

FINANCIAL STATEMENTS
WITH
INDEPENDENT AUDITOR'S REPORT
Years Ended June 30, 2014 and 2013

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Institute for Justice

Report on the Financial Statements

We have audited the accompanying financial statements of the Institute for Justice (a nonprofit organization), which comprise the statements of financial position as of June 30, 2014 and 2013, and the related statements of activities and cash flows for the year ended June 30, 2014, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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 the Institute for Justice as of June 30, 2014 and 2013, and the changes in its net assets and its cash flows for the year ended June 30, 2014, in conformity with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited the Institute for Justice's June 30, 2013 financial statements, and our report dated November 14, 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 June 30, 2013, is consistent, in all material respects, with the audited financial statements from which it has been derived.

October 28, 2014
Bethesda, Maryland

A handwritten signature in black ink that reads "Rubins & Company". The signature is written in a cursive, flowing style. The word "Rubins" is followed by an ampersand "&" and then the word "Company".

INSTITUTE FOR JUSTICE
STATEMENTS OF FINANCIAL POSITION
June 30, 2014 and 2013

| | <u>2014</u> | <u>2013</u> |
|--------------------------------------|--------------------------|--------------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 24,341,203 | \$ 18,602,799 |
| Pledges receivable, net | 3,646,257 | 5,478,892 |
| Other receivables | 12,097 | 11,649 |
| Prepaid expenses and deposits | 394,778 | 218,605 |
| Reserve fund | 25,117,486 | 17,246,038 |
| Property and equipment, net | <u>758,646</u> | <u>814,509</u> |
| Total assets | <u>\$ 54,270,467</u> | <u>\$ 42,372,492</u> |
| LIABILITIES AND NET ASSETS | | |
| Accounts payable | \$ 245,689 | \$ 110,611 |
| Accrued liabilities | 619,536 | 350,720 |
| Capital lease obligations | 27,363 | 26,027 |
| Deferred rent | 108,117 | 162,865 |
| Deferred revenue | <u>25,137</u> | <u>-</u> |
| Total liabilities | <u>1,025,842</u> | <u>650,223</u> |
| Net assets | | |
| Unrestricted net assets | 49,103,431 | 35,891,338 |
| Temporarily restricted net assets | <u>4,141,194</u> | <u>5,830,931</u> |
| Total net assets | <u>53,244,625</u> | <u>41,722,269</u> |
| Total liabilities and net assets | <u>\$ 54,270,467</u> | <u>\$ 42,372,492</u> |

The accompanying notes are an integral part of these financial statements.

INSTITUTE FOR JUSTICE
STATEMENT OF ACTIVITIES
Year Ended June 30, 2014
(With Comparative Totals for 2013)

| | <u>Unrestricted</u> | <u>Temporarily Restricted</u> | <u>2014 Total</u> | <u>2013 Total</u> |
|---|----------------------|-----------------------------------|-----------------------|-----------------------|
| Support and revenue | | | | |
| Contributions | \$ 14,658,255 | \$ 9,259,264 | \$ 23,917,519 | \$ 18,598,848 |
| Attorney fees | 503,954 | - | 503,954 | 116,621 |
| Other income | 25,748 | - | 25,748 | 51,239 |
| Net assets released from restrictions - satisfaction of program and time restrictions | <u>10,949,001</u> | <u>(10,949,001)</u> | <u>-</u> | <u>-</u> |
| Total support and revenue | <u>26,136,958</u> | <u>(1,689,737)</u> | <u>24,447,221</u> | <u>18,766,708</u> |
| Expenses | | | | |
| Program services | 11,625,758 | - | 11,625,758 | 10,670,468 |
| Management | 1,380,523 | - | 1,380,523 | 1,210,423 |
| Development/fundraising | <u>1,082,044</u> | <u>-</u> | <u>1,082,044</u> | <u>931,217</u> |
| Total expenses | <u>14,088,325</u> | <u>-</u> | <u>14,088,325</u> | <u>12,812,108</u> |
| Change in net assets from operations | 12,048,633 | (1,689,737) | 10,358,896 | 5,954,600 |
| Non-operating activity | | | | |
| Investment return, net | <u>1,163,460</u> | <u>-</u> | <u>1,163,460</u> | <u>278,804</u> |
| Change in net assets | 13,212,093 | (1,689,737) | 11,522,356 | 6,233,404 |
| Net assets, beginning of year | <u>35,891,338</u> | <u>5,830,931</u> | <u>41,722,269</u> | <u>35,488,865</u> |
| Net assets, end of year | <u>\$ 49,103,431</u> | <u>\$ 4,141,194</u> | <u>\$ 53,244,625</u> | <u>\$ 41,722,269</u> |

The accompanying notes are an integral part of these financial statements.

INSTITUTE FOR JUSTICE
STATEMENT OF CASH FLOWS
Year Ended June 30, 2014

| | |
|---|---------------|
| Cash flows from operating activities | |
| Change in net assets | \$ 11,522,356 |
| Reconciling adjustments: | |
| Depreciation and amortization | 302,206 |
| Allowance for present value of pledges receivable | 32,429 |
| Provision for uncollectible pledges receivable | (76,002) |
| Loss on disposal of property and equipment | 3,444 |
| Net realized and unrealized gains from reserve fund investments | (1,008,606) |
| Stock contributions | (1,432,963) |
| Changes in operating assets and liabilities | |
| Pledges receivable | 1,876,208 |
| Other receivables | (448) |
| Prepaid expenses and deposits | (176,173) |
| Accounts payable | 125,010 |
| Accrued liabilities | 268,816 |
| Deferred rent | (54,748) |
| Deferred revenue | 25,137 |
| | <hr/> |
| Net cash provided by operating activities | 11,406,666 |
| | <hr/> |
| Cash flows from investing activities | |
| Acquisition of property and equipment | (232,219) |
| Purchase of reserve fund investments | (8,125,984) |
| Redemption of reserve fund investments | 2,696,105 |
| | <hr/> |
| Net cash used by investing activities | (5,662,098) |
| | <hr/> |
| Cash flows from financing activities | |
| Payment of capital lease obligations | (6,164) |
| | <hr/> |
| Net increase in cash and cash equivalents | 5,738,404 |
| Cash and cash equivalents, beginning of year | 18,602,799 |
| | <hr/> |
| Cash and cash equivalents, end of year | \$ 24,341,203 |
| | <hr/> |

The accompanying notes are an integral part of these financial statements.

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

1. Organization

The Institute for Justice (the Institute) was incorporated and began operations in 1991. The Institute is a publicly-supported not-for-profit organization which works toward protection of productive livelihoods, school choice, private property, and the free exchange of ideas through litigation and education.

2. Summary of Significant Accounting Policies

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 the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Income Taxes

The Institute is recognized as tax-exempt under Section 501(c)(3) of the Internal Revenue Code. However, income from certain activities not directly related to the Institute's tax-exempt purpose is subject to taxation as unrelated business income. There was no unrelated business income for the years ended June 30, 2014 and 2013. Tax years ended June 30, 2011-2013 remain open to examination by the taxing jurisdictions to which the Institute is subject, and they have not been extended beyond the applicable statute of limitations; however, the Institute believes there are no matters that would require recognition in the financial statements or that may have any effect on its tax-exempt status.

Cash and Cash Equivalents

Cash includes interest and non-interest bearing operating accounts and a sweep account with insured financial institutions. Deposits often exceed federally insured limits. Management, however, does not consider this a significant concentration of credit risk. Cash equivalents include highly liquid investments with an initial maturity of three months or less. Cash and cash equivalents exclude such amounts included with the operations reserve fund as those funds are part of the investment strategy and portfolio.

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

2. Summary of Significant Accounting Policies (continued)

Contributions

Contributions and unconditional promises to give are recorded as support, at fair value, when received. Contributions that are restricted by the donor as to time or purpose are reported as an increase in temporarily restricted net assets. When a time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Pledges Receivable

Unconditional promises to give are reported at their net realizable value as pledges receivable in the accompanying statements of financial position. Conditional promises to give are not recorded as receivables until the conditions are satisfied. Contributions and pledges received by the Institute consist of support provided primarily by individuals and foundations. The Institute does not accept grants from the Government. A provision for uncollectible pledges receivable is recorded in the period such a determination is made.

Investments

Investments are recorded at estimated fair value based on quoted market prices provided by independent investment managers. Purchases and sales are recorded on a trade-date basis. Realized and unrealized holding gains and losses are included with investment income in the statement of activities. Investment income is reported as an increase in unrestricted net assets, unless restricted by donor or law.

Expense Allocation

The costs of providing various programs and other activities of the Institute have been summarized on a functional basis in the statement of activities. Expenses are allocated among the programs and support services based on the functions they directly benefit or upon management's estimates of the proportion of the expenses applicable to each function.

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

2. Summary of Significant Accounting Policies (continued)

Property and Equipment

The Institute capitalizes all property and equipment with a cost of \$1,000 or more. Property and equipment are carried at cost if purchased and at estimated fair value at the date contributed, if applicable. The Institute depreciates all office equipment, furniture and fixtures using the straight-line method over the estimated useful lives of the assets (three to five years). Leasehold improvements are recorded at cost and are being amortized over their estimated useful lives or the terms of the lease, whichever is shorter.

Maintenance and repair costs are charged to expense as incurred. Replacements and betterments are capitalized. At the time properties are retired or otherwise disposed of, the property and related accumulated depreciation or amortization accounts are relieved of the applicable amounts and any gain or loss is credited or charged to income.

Comparative Information

The statement of activities includes certain 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 the Institute's financial statements for the year ended June 30, 2013, from which the summarized information was derived.

Subsequent Events

Management has evaluated subsequent events through October 28, 2014, which is the date the financial statements were available to be issued. The accompanying financial statements recognize the effects of subsequent events that provided evidence about conditions that existed at the statement of financial position date, including the estimates inherent in the process of preparing financial statements. The accompanying financial statements do not recognize the effect of subsequent events with conditions that did not exist at the statement of financial position date, but disclosures of such events, if any, are included in the accompanying notes.

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

3. Reserve Fund

It is the Board's and management's intent to set aside sufficient reserves to be able to meet the future financial obligations of current program services with which the Institute is involved, in the event of a downturn in contributions. In addition, the Institute has set aside reserves to fund its charitable gift annuities (Note 6). The Institute's reserve fund is comprised of the following investments at June 30, 2014 and 2013:

| | (Fair Value Levels) | | |
|---------------------------------------|---------------------|----------------------|----------------------|
| | (Note 10) | <u>2014</u> | <u>2013</u> |
| Operations Reserve Fund: | | | |
| Vanguard Group | | | |
| Money market funds | 1 | \$ 9,899,109 | \$ 9,822,551 |
| Exchange traded funds | | | |
| International | 1 | 3,521,453 | 2,368,978 |
| S&P 500 Index | 1 | 1,961,358 | 1,572,324 |
| Commodity | 1 | 1,524,709 | 1,238,105 |
| Other | 1 | <u>1,574,507</u> | <u>899,757</u> |
| | | 8,582,027 | 6,079,164 |
| Index funds - short-term bonds | 1 | <u>1,169,625</u> | <u>1,150,136</u> |
| | | <u>19,650,761</u> | <u>17,051,851</u> |
| Ameritrade - money market funds | 1 | <u>113,678</u> | <u>4,946</u> |
| Millennium International, Ltd | | | |
| Diversified strategy hedge fund | 3 | <u>4,960,861</u> | <u>-</u> |
| Total operations reserve | | <u>24,725,300</u> | <u>17,056,797</u> |
| Charitable Gift Annuity Reserve Fund: | | | |
| Charles Schwab | | | |
| Money market funds | 1 | 16,995 | 12,942 |
| Mutual funds - bonds | 1 | <u>174,500</u> | <u>172,307</u> |
| | | <u>191,495</u> | <u>185,249</u> |
| Millenium private banking | | | |
| Index fund - total bond market | 1 | <u>200,691</u> | <u>3,992</u> |
| Total charitable gift annuity reserve | | <u>392,186</u> | <u>189,241</u> |
| Total reserve fund | | <u>\$ 25,117,486</u> | <u>\$ 17,246,038</u> |

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

3. Reserve Fund (continued)

The investments are subject to market risks and their values fluctuate daily. Investment return is comprised of the following:

| | <u>2014</u> | <u>2013</u> |
|-----------------------------------|---------------------|-------------------|
| Interest and dividends | \$ 154,854 | \$ 158,644 |
| Net realized and unrealized gains | <u>1,008,606</u> | <u>120,160</u> |
| Investment return, net | <u>\$ 1,163,460</u> | <u>\$ 278,804</u> |

4. Fair Value of Financial Instruments

The Institute reports its fair value measures using a three-level hierarchy that prioritizes the inputs used to measure fair value. This hierarchy, established by generally accepted accounting principles, gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The fair value hierarchy is as follows:

- Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities that the Institute has the ability to access.
- Level 2: Inputs to the valuation methodology include:
 - Quoted prices for similar assets or liabilities in active markets;
 - Quoted prices for identical or similar assets or liabilities in inactive markets;
 - Inputs other than quoted prices that are observable for the asset or liability;
 - Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

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

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

4. Fair Value of Financial Instruments (continued)

Following is a description of the valuation methodologies used for investments measured at fair value and their classification in the valuation hierarchy:

- Investments in *money market* and *mutual funds* are valued at the net asset value of shares held by the Institute at year end reported in the listing of the applicable major exchanges. Such securities are classified within Level 1 of the valuation hierarchy.
- Investments in *exchange traded funds (ETFs)* are valued at the closing price reported in the active markets in which the ETFs are traded. Such securities are classified within Level 1 of the valuation hierarchy.
- Investments in *hedge funds* are valued at the fund's NAV or its equivalent, as provided by the fund. The net assets of alternative investments are valued based on each underlying investment within the alternative investment funds, incorporating valuations that consider the evaluation of financing and sale transactions with third parties, expected cash flows and market-based information, including comparable transactions, and performance multiples, among other factors. Such securities are classified within Level 3 of the valuation hierarchy.

The following presents a reconciliation of investments in which significant unobservable inputs (Level 3) were used to determine fair value:

| <u>Investment</u> | <u>Balance</u> <u>July 1, 2013</u> | <u>Purchases</u> | <u>Realized and</u> <u>Unrealized</u> <u>Gains (Losses)</u> | <u>Settlements and</u> <u>Redemptions</u> | <u>Balance</u> <u>June 30, 2014</u> |
|----------------------|---------------------------------------|------------------|---|--|--|
| Diversified strategy | | | | | |
| hedge funds | \$ - | \$ 5,000,000 | \$ (39,139) | \$ - | \$ 4,960,861 |

The following table includes additional disclosures required for the fair value measurements of investments that do not have a readily determinable fair value and are in certain entities that calculate net asset value per share:

| <u>Investment</u> | <u>June 30, 2014</u> <u>Fair Value</u> | <u>Unfunded</u> <u>Commitments</u> | <u>Redemption</u> <u>Frequency</u> | <u>Redemption</u> <u>Notice Period</u> |
|----------------------|---|---------------------------------------|---------------------------------------|---|
| Diversified strategy | | | | |
| hedge funds | \$ 4,960,861 | \$ - | Quarterly | 90 days |

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

5. Pledges Receivable

Pledges receivable that are expected to be collected in future years are discounted to present values using a blended rate that contemplates the donor's estimated borrowing rate, and a risk-free rate of return, at the date the unconditional promise is made. (This is a Level 3 input of fair value discussed in Note 4). The discount rates for 2014 and 2013 ranged from 2.26% to 2.51%. The discount is amortized to support from contributions over the pledge collection period. The outstanding pledges at June 30, 2014 and 2013, are as follows:

| <u>Purpose</u> | <u>2014</u> | <u>2013</u> |
|---|---------------------|---------------------|
| Economic Liberty | \$ 604,263 | \$ 1,831,686 |
| Revitalize the Constitution | - | 3,309,283 |
| School Choice | 1,000,000 | 400,000 |
| Asset Forfeiture | 10,000 | - |
| Fellowship | 25,000 | - |
| Operating support | 75,498 | 50,000 |
| General support for future years | <u>2,000,000</u> | <u>-</u> |
| Total pledges receivable | 3,714,761 | 5,590,969 |
| Provision for uncollectible pledges receivable | (30,949) | (106,951) |
| Allowance for present value of pledges receivable | <u>(37,555)</u> | <u>(5,126)</u> |
| Pledges receivable, net | <u>\$ 3,646,257</u> | <u>\$ 5,478,892</u> |

The June 30, 2014 and 2013, pledges receivable are expected to be collected as follows:

| | <u>2014</u> | <u>2013</u> |
|--------------------------|---------------------|---------------------|
| Due in one year | \$ 2,664,761 | \$ 5,382,969 |
| Due in two years | 550,000 | 183,000 |
| Due in three years | <u>500,000</u> | <u>25,000</u> |
| Total pledges receivable | <u>\$ 3,714,761</u> | <u>\$ 5,590,969</u> |

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

5. Pledges Receivable (continued)

On August 24, 2011, the Institute entered into a conditional matching grant from the Robert W. Wilson Charitable Trust (Wilson Trust) for the period beginning January 1, 2011 and ending June 30, 2014. The objective of the grant was to increase the amount of support from existing and new donors for the purposes of expanding the Institute's programs to *Revitalize the Constitution* (IJ Matching Grants) and in particular to expand its *Campaign for Economic Liberty* (IJ Program Matching Grants). The maximum amount under the grant agreement was \$10 million. At June 30, 2014 and 2013, aggregate amounts receivable from the Wilson Trust for conditions met were approximately \$429,000 and \$1.3 million, respectively. As of December 31, 2013 and June 30, 2014, the Institute met the maximum allowable amount of funds available for the IJ Matching Grants and IJ Program Matching Grants, respectively.

During the current year, the Institute received a Challenge Grant (Grant) of \$5 million. Effective July 1, 2014, the Grant is to establish the Bill and Rebecca Dunn Liberty Defense Fund and provide one dollar for every two dollars of new support raised by the Institute. All eligible donations and matching funds are to be directed into the Fund and used to support the Institute's overall mission. As part of the Grant the donor made an unconditional promise to give \$2 million at June 30, 2014. The Institute recorded the unconditional promise at year end; the remainder amounts under the agreement will be recognized as the conditions under the Grant are met.

6. Charitable Gift Annuities

The Institute has received cash contributions totaling approximately \$265,000 in the form of charitable gift annuities since establishing the Four Pillars Society in 2006. The related monies are housed in a discrete diversified investment portfolio and are included in the reserve fund, in the accompanying statements of financial position (Note 3). The liability under the agreements is recorded at the net present value of the estimated income owed to the donor based upon an actuarial report. The estimated liability is included with accrued liabilities in the accompanying statements of financial position and was approximately \$126,000 and \$21,000 at June 30, 2014 and 2013, respectively. The discount is computed using the risk-free rates applicable to the current year's calculation. The agreements stipulate that the donors are to receive quarterly payments for the remainder of their lives. Any income not distributed will revert to the Institute when the agreement ends.

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

7. Property and Equipment

A summary of property and equipment is as follows:

| | <u>2014</u> | <u>2013</u> |
|---|--------------------|--------------------|
| Furniture and equipment | \$ 1,335,451 | \$ 1,319,768 |
| Computers and software | 336,478 | 352,273 |
| Leasehold improvements | 1,243,813 | 1,243,813 |
| Construction in progress | <u>160,832</u> | <u>-</u> |
| | 3,076,574 | 2,915,854 |
| Accumulated depreciation and amortization | <u>(2,317,928)</u> | <u>(2,101,345)</u> |
| Property and equipment, net | <u>\$ 758,646</u> | <u>\$ 814,509</u> |

Construction in progress at June 30, 2014, includes tenant improvement allowance costs related to the expansion of the headquarters office space. See Note 10 for further information regarding the operating lease. Depreciation and amortization expense for the years ended June 30, 2014 and 2013, was \$302,206 and \$329,015, respectively.

8. Temporarily Restricted Net Assets

Temporarily restricted net assets at June 30, 2014 and 2013, include purpose and time restricted contributions and are available to support the following program areas:

| | <u>2014</u> | <u>2013</u> |
|----------------------------------|---------------------|---------------------|
| School Choice | \$ 1,108,535 | \$ 527,007 |
| Economic Liberty | 653,068 | 1,925,457 |
| Revitalize the Constitution | 73,053 | 3,245,830 |
| Fellowship | 24,375 | 48,211 |
| Asset Forfeiture | 24,887 | - |
| Strategic Research | 47,276 | - |
| Property Rights | 10,000 | - |
| New Media Proposal | - | 71,926 |
| General support for future years | <u>2,200,000</u> | <u>12,500</u> |
| | <u>\$ 4,141,194</u> | <u>\$ 5,830,931</u> |

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

9. Retirement Plans

The Institute has a 401(k) plan for all employees with one year of service, subject to age limitations. The plan provides for employee voluntary contributions and employer matching contributions. The employer match is currently 100% of employee contributions up to 4% of compensation during the plan year. In addition, the plan provides for a discretionary contribution for all participants employed on the last day of the plan year who are credited with at least 1,000 hours of service during that year. Vesting in the benefits of the plan is based on years of service with full vesting after five years.

The Institute sponsors a non-qualified deferred compensation plan pursuant to Section 457(f) of the Internal Revenue Code for the benefit of certain management or highly compensated employees. The purpose of the plan is to offer those employees a deferred compensation opportunity and is intended to be an unfunded deferred compensation plan exempt from the requirements of Section 409A of the Code as a short-term deferral program. The Plan's investments, while specifically identified, remain the Institute's assets and are subject to general creditor claims with the benefit payout limited to the value of the underlying assets. Plan obligations for the above non-qualified plan totaled \$225,000 and \$150,000 for the years June 30, 2014 and 2013, respectively, and are included with accrued liabilities on the statements of financial position.

The Institute also sponsors a separate tax deferred annuity plan through elective salary reductions under Section 403(b) of the Internal Revenue Code.

Retirement expense incurred for the above plans totaled \$800,732 and \$708,995, for the years ended June 30, 2014 and 2013, respectively.

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

10. Lease Commitments

Operating Leases

The Institute leases office space for its offices under operating leases with expiration dates ranging from March 31, 2015, through April 30, 2027. These leases call for monthly rent plus the pass-through of increases in operating expenses. In addition, the Institute leases office equipment under operating leases which have lease terms of three to five years. The required minimum lease payments, net of lease incentives, are recognized as expense on a straight-line basis over the applicable lease terms resulting in a deferred rent liability at June 30, 2014 and 2013, of \$108,117 and \$162,865, respectively. Rental expense under all operating leases for the years ended June 30, 2014 and 2013, was \$1,163,795 and \$1,124,731, respectively.

Effective February 20, 2014, the operating lease associated with the Institute's headquarters was amended. Among the modifications are provisions for an increase in rentable square feet, an extension of the lease term, minimum annual escalation increases, and a tenant improvement allowance of \$1,257,455 to be paid by the landlord as construction progresses. The amended lease terms are effective October 1, 2014. The total future minimum lease commitments under these lease agreements at June 30, 2014 are as follows:

| | |
|---------------------------|----------------------|
| Year ending June 30, 2015 | \$ 1,318,600 |
| 2016 | 1,529,600 |
| 2017 | 1,457,700 |
| 2018 | 1,455,700 |
| 2019 | 1,373,900 |
| Thereafter | <u>13,354,600</u> |
| | <u>\$ 20,490,100</u> |

INSTITUTE FOR JUSTICE
NOTES TO FINANCIAL STATEMENTS
Years Ended June 30, 2014 and 2013

10. Lease Commitments (continued)

Capital Leases

The Institute entered into lease agreements during fiscal years 2012 and 2014 to finance certain equipment over five-year periods. The lease agreements have been classified as capital leases, which are generally accounted for as additions to property and equipment using lease financing. Future minimum lease payments under the Institute's capital leases are as follows:

| | | |
|---|----|----------------------|
| Year ending June 30, 2015 | \$ | 11,741 |
| 2016 | | 11,741 |
| 2017 | | 6,723 |
| 2018 | | 3,138 |
| 2019 | | <u>3,138</u> |
| Total minimum lease payments | | 36,481 |
| Amount representing interest | | <u>(9,118)</u> |
| Present value of minimum lease payments | \$ | <u><u>27,363</u></u> |

At June 30, 2014 and 2013, the book value of the capital lease assets is \$25,375 and \$25,802, net of accumulated depreciation of \$19,885 and \$11,958, respectively, and is included with property and equipment.

11. Cash Flow Information

During the current year, the Institute had noncash investing and financing activities related to capital leases and accounts payable on new equipment of \$7,500 and \$10,068, respectively. Interest paid in 2014 was \$2,498.