

**THE REASON FOUNDATION  
COMPARATIVE FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT  
SEPTEMBER 30, 2011 AND 2010**

THE REASON FOUNDATION  
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SEPTEMBER 30, 2011 AND 2010

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CERTIFIED PUBLIC ACCOUNTANTS  
&  
BUSINESS CONSULTANTS

January 11, 2012

## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
The Reason Foundation  
Los Angeles, California

We have audited the accompanying statement of financial position of The Reason Foundation, (a nonprofit foundation) as of September 30, 2011, and the related statements of activities, functional expenses and cash flows for the year then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Organization's 2010 financial statements and, in our report dated December 2, 2010 we expressed an unqualified opinion on those financial statements.

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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Reason Foundation, as of September 30, 2011 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads 'NSBN LLP' in a cursive, stylized font.

NSBN LLP

THE REASON FOUNDATION  
STATEMENTS OF FINANCIAL POSITION  
SEPTEMBER 30, 2011  
WITH COMPARATIVE TOTALS AT JUNE 30, 2010

|                                                  | <u>2011</u>                | <u>2010</u>                |
|--------------------------------------------------|----------------------------|----------------------------|
| <b>CURRENT ASSETS</b>                            |                            |                            |
| Cash and cash equivalents (Note 2, 5, 14)        | \$ 1,216,615               | \$ 1,090,599               |
| Accounts receivable, net (Note 2)                | 67,758                     | 35,834                     |
| Pledges receivable, net (Note 2)                 | 476,890                    | 818,402                    |
| Investments (Note 2, 6)                          | <u>3,428,157</u>           | <u>2,765,320</u>           |
| <b>TOTAL CURRENT ASSETS</b>                      | <u>5,189,420</u>           | <u>4,710,155</u>           |
| <b>PROPERTY AND EQUIPMENT (Note 2)</b>           |                            |                            |
| Furniture and equipment                          | 901,747                    | 880,899                    |
| Leasehold improvements                           | <u>21,725</u>              | <u>21,725</u>              |
| Total                                            | 923,472                    | 902,624                    |
| Less: Accumulated depreciation                   | <u>(892,434)</u>           | <u>(872,409)</u>           |
| <b>NET PROPERTY AND EQUIPMENT</b>                | <u>31,038</u>              | <u>30,215</u>              |
| <b>OTHER ASSETS</b>                              |                            |                            |
| Deposits                                         | <u>124,444</u>             | <u>96,137</u>              |
| <b>TOTAL ASSETS</b>                              | <u><b>\$ 5,344,902</b></u> | <u><b>\$ 4,836,507</b></u> |
| <b>CURRENT LIABILITIES</b>                       |                            |                            |
| Accounts payable                                 | \$ 117,295                 | \$ 78,788                  |
| Accrued expenses                                 | 546,911                    | 381,925                    |
| Deferred revenue                                 | 9,000                      | -                          |
| Unearned subscriptions, current portion (Note 9) | <u>315,317</u>             | <u>312,359</u>             |
| <b>TOTAL CURRENT LIABILITIES</b>                 | 988,523                    | 773,072                    |
| <b>LONG TERM LIABILITIES</b>                     |                            |                            |
| Unearned subscriptions (Note 9)                  | <u>103,442</u>             | <u>126,845</u>             |
| <b>TOTAL LIABILITIES</b>                         | <u>1,091,965</u>           | <u>899,917</u>             |
| <b>NET ASSETS</b>                                |                            |                            |
| Unrestricted                                     | 4,107,708                  | 3,556,310                  |
| Temporarily restricted (Note 11)                 | 101,950                    | 338,001                    |
| Permanently restricted (Note 11)                 | <u>43,279</u>              | <u>42,279</u>              |
| <b>TOTAL NET ASSETS</b>                          | <u>4,252,937</u>           | <u>3,936,590</u>           |
| <b>TOTAL LIABILITIES AND NET ASSETS</b>          | <u><b>\$ 5,344,902</b></u> | <u><b>\$ 4,836,507</b></u> |

See accompanying auditors' report.  
The notes are an integral part of these financial statements.

THE REASON FOUNDATION  
STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED SEPTEMBER 30, 2011  
WITH COMPARATIVE TOTALS FOR THE YEAR ENDED SEPTEMBER 30, 2010

|                                                     | 2011                 |                                   |                                   | 2010                |                     |
|-----------------------------------------------------|----------------------|-----------------------------------|-----------------------------------|---------------------|---------------------|
|                                                     | Unrestricted<br>Fund | Temporarily<br>Restricted<br>Fund | Permanently<br>Restricted<br>Fund | Total<br>Funds      | Total<br>Funds      |
| <b>REVENUE AND SUPPORT</b>                          |                      |                                   |                                   |                     |                     |
| Contributions                                       | \$ 7,122,746         | \$ -                              | \$ 1,000                          | \$ 7,123,746        | \$ 6,399,733        |
| Magazine                                            | 757,806              | -                                 | -                                 | 757,806             | 750,790             |
| Special events                                      | 313,506              | -                                 | -                                 | 313,506             | 118,800             |
| Net investment income (loss) and other income       | 85,818               | -                                 | -                                 | 85,818              | 194,881             |
| Released from restriction (Note 12)                 | 236,051              | (236,051)                         | -                                 | -                   | -                   |
| <b>TOTAL REVENUE AND SUPPORT</b>                    | <u>8,515,927</u>     | <u>(236,051)</u>                  | <u>1,000</u>                      | <u>8,280,876</u>    | <u>7,464,204</u>    |
| <b>EXPENSES</b>                                     |                      |                                   |                                   |                     |                     |
| Program services                                    |                      |                                   |                                   |                     |                     |
| Foundation                                          | 309,244              | -                                 | -                                 | 309,244             | 1,510,793           |
| Reason- Rupe                                        | 349,338              | -                                 | -                                 | 349,338             | -                   |
| Reason-TV                                           | 1,195,539            | -                                 | -                                 | 1,195,539           | -                   |
| Magazine                                            | 2,550,499            | -                                 | -                                 | 2,550,499           | 2,346,083           |
| Research                                            | 2,211,232            | -                                 | -                                 | 2,211,232           | 2,006,442           |
| <b>Total program services</b>                       | <u>6,615,852</u>     | <u>-</u>                          | <u>-</u>                          | <u>6,615,852</u>    | <u>5,863,318</u>    |
| Supporting services                                 |                      |                                   |                                   |                     |                     |
| Management and general                              | 311,173              | -                                 | -                                 | 311,173             | 242,316             |
| Fundraising                                         | 859,636              | -                                 | -                                 | 859,636             | 758,154             |
| <b>Total supporting services</b>                    | <u>1,170,809</u>     | <u>-</u>                          | <u>-</u>                          | <u>1,170,809</u>    | <u>1,000,470</u>    |
| <b>Total expenses before special events</b>         | <u>7,786,661</u>     | <u>-</u>                          | <u>-</u>                          | <u>7,786,661</u>    | <u>6,863,788</u>    |
| Special events expenses                             | 177,868              | -                                 | -                                 | 177,868             | 143,077             |
| <b>TOTAL EXPENSES</b>                               | <u>7,964,529</u>     | <u>-</u>                          | <u>-</u>                          | <u>7,964,529</u>    | <u>7,006,865</u>    |
| <b>CHANGE IN NET ASSETS</b>                         | <u>551,398</u>       | <u>(236,051)</u>                  | <u>1,000</u>                      | <u>316,347</u>      | <u>457,339</u>      |
| <b>NET ASSETS AT BEGINNING OF YEAR</b>              | 3,556,310            | 338,001                           | 42,279                            | 3,936,590           | 3,468,569           |
| <b>PRIOR PERIOD ADJUSTMENT</b>                      | -                    | -                                 | -                                 | -                   | 10,682              |
| <b>NET ASSETS AT BEGINNING OF YEAR- AS ADJUSTED</b> | <u>3,556,310</u>     | <u>338,001</u>                    | <u>42,279</u>                     | <u>3,936,590</u>    | <u>3,479,251</u>    |
| <b>NET ASSETS AT END OF YEAR</b>                    | <u>\$ 4,107,708</u>  | <u>\$ 101,950</u>                 | <u>\$ 43,279</u>                  | <u>\$ 4,252,937</u> | <u>\$ 3,936,590</u> |

See accompanying auditors' report.  
The notes are an integral part of these financial statements.

THE REASON FOUNDATION  
STATEMENT OF FUNCTIONAL EXPENSES  
FOR THE YEAR ENDED SEPTEMBER 30, 2011  
WITH COMPARATIVE TOTALS FOR THE YEAR ENDED SEPTEMBER 30, 2010

|                                           | 2011                     |                          |                            |                            |                            |                            | 2010                     |                          |                            |                            |
|-------------------------------------------|--------------------------|--------------------------|----------------------------|----------------------------|----------------------------|----------------------------|--------------------------|--------------------------|----------------------------|----------------------------|
|                                           | Program Services         |                          |                            |                            |                            | Total Program<br>Services  | Supporting Services      |                          | Total<br>Expenses          | Total<br>Expenses          |
|                                           | Foundation               | Reason-Rupe              | Reason-TV                  | Magazine                   | Research                   |                            | Administration           | Development              |                            |                            |
| Books and periodicals                     | \$ 6,049                 | \$ 138                   | \$ 6,287                   | \$ 4,143                   | \$ 6,151                   | \$ 22,768                  | \$ 714                   | \$ 2,023                 | \$ 25,505                  | \$ 25,690                  |
| Commissions                               | -                        | -                        | -                          | 40,616                     | -                          | 40,616                     | -                        | -                        | 40,616                     | 52,718                     |
| Contract services                         | 9,121                    | 118,119                  | 70,745                     | 216,551                    | 604,131                    | 1,018,667                  | 6,440                    | 13,109                   | 1,038,216                  | 769,449                    |
| Dues and subscriptions                    | 8,940                    | -                        | 5,156                      | 9,000                      | 51,675                     | 74,771                     | 1,715                    | 11,803                   | 88,289                     | 64,157                     |
| Insurance                                 | 3,926                    | -                        | 14,666                     | 19,486                     | 17,718                     | 55,796                     | 3,360                    | 8,642                    | 67,798                     | 54,028                     |
| Manufacturing and distribution            | 419                      | -                        | 1,391                      | 510,207                    | 814                        | 512,831                    | -                        | 75                       | 512,906                    | 524,951                    |
| Media tracking and placement service:     | 13,084                   | 1,697                    | -                          | -                          | -                          | 14,781                     | -                        | -                        | 14,781                     | 16,033                     |
| Miscellaneous                             | 4,496                    | 34,264                   | 10,388                     | 11,886                     | 18,497                     | 79,531                     | 1,625                    | 3,747                    | 84,903                     | 72,282                     |
| On-line services                          | 6,060                    | 189                      | 19,605                     | 24,206                     | 27,746                     | 77,806                     | 2,612                    | 9,725                    | 90,143                     | 78,520                     |
| Postage and shipping                      | 5,463                    | 1,928                    | 6,993                      | 22,789                     | 15,350                     | 52,523                     | 2,342                    | 42,643                   | 97,508                     | 106,951                    |
| Printed material                          | 11                       | 636                      | 4,863                      | 49,981                     | 17,927                     | 73,418                     | 10                       | 31,574                   | 105,002                    | 68,132                     |
| Professional fees                         | 6,631                    | -                        | 20,206                     | 27,569                     | 25,304                     | 79,710                     | 4,877                    | 12,786                   | 97,373                     | 59,879                     |
| Promotion and advertising                 | -                        | 947                      | 6,098                      | 319,724                    | 3,903                      | 330,672                    | 1,172                    | 37,969                   | 369,813                    | 256,514                    |
| Rent and parking                          | 11,493                   | -                        | 84,073                     | 109,904                    | 96,510                     | 301,980                    | 18,284                   | 46,749                   | 367,013                    | 388,889                    |
| Salaries, benefits, and taxes             | 199,637                  | 186,691                  | 844,267                    | 1,114,421                  | 1,069,810                  | 3,414,827                  | 204,533                  | 543,571                  | 4,162,931                  | 3,771,622                  |
| Supplies                                  | 13,732                   | 518                      | 22,811                     | 9,860                      | 12,138                     | 59,058                     | 1,474                    | 13,424                   | 73,956                     | 85,590                     |
| Telephone                                 | 5,942                    | 40                       | 9,723                      | 10,574                     | 17,719                     | 43,998                     | 1,490                    | 6,598                    | 52,086                     | 53,967                     |
| Travel and entertainment                  | 13,026                   | 4,172                    | 63,970                     | 43,818                     | 220,625                    | 345,611                    | 4,525                    | 72,658                   | 422,794                    | 346,013                    |
| Unfulfilled pledges                       | -                        | -                        | -                          | -                          | -                          | -                          | 55,000                   | -                        | 55,000                     | -                          |
| <b>Total expenses before depreciation</b> | <b>308,030</b>           | <b>349,338</b>           | <b>1,191,242</b>           | <b>2,544,735</b>           | <b>2,206,018</b>           | <b>6,599,363</b>           | <b>310,173</b>           | <b>857,096</b>           | <b>7,766,632</b>           | <b>6,795,385</b>           |
| Depreciation                              | 1,214                    | -                        | 4,297                      | 5,764                      | 5,214                      | 16,489                     | 1,000                    | 2,540                    | 20,029                     | 68,403                     |
| <b>Total Expenses</b>                     | <b><u>\$ 309,244</u></b> | <b><u>\$ 349,338</u></b> | <b><u>\$ 1,195,539</u></b> | <b><u>\$ 2,550,499</u></b> | <b><u>\$ 2,211,232</u></b> | <b><u>\$ 6,615,852</u></b> | <b><u>\$ 311,173</u></b> | <b><u>\$ 859,636</u></b> | <b><u>\$ 7,786,661</u></b> | <b><u>\$ 6,863,788</u></b> |

See accompanying auditors' report.  
The notes are an integral part of these financial statements.

THE REASON FOUNDATION  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED SEPTEMBER 30, 2011 AND 2010

| CASH FLOWS FROM OPERATING ACTIVITIES                                                           | <u>2011</u>         | <u>2010</u>         |
|------------------------------------------------------------------------------------------------|---------------------|---------------------|
| Change in net assets                                                                           | \$ 316,347          | \$ 457,339          |
| Adjustments to reconcile net assets<br>to net cash provided by (used in) operating activities: |                     |                     |
| Depreciation                                                                                   | 20,029              | 68,403              |
| Investment in commodities                                                                      | -                   | (1,159)             |
| Net unrealized (gains) / losses on investments                                                 | (24,945)            | (125,117)           |
| (Increase) decrease in assets:                                                                 |                     |                     |
| Prepaid expenses                                                                               | -                   | 65,729              |
| Accounts receivable, net                                                                       | (31,924)            | (5,711)             |
| Pledges receivable, net                                                                        | 341,512             | 211,966             |
| Deposits                                                                                       | (28,307)            | (1,589)             |
| Increase (decrease) in liabilities:                                                            |                     |                     |
| Accounts payable                                                                               | 38,507              | 8,438               |
| Accrued expenses                                                                               | 164,986             | (77,395)            |
| Deferred revenue                                                                               | 9,000               | -                   |
| Unearned subscriptions                                                                         | (20,445)            | (15,083)            |
| <u>NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES</u>                                     | <u>784,760</u>      | <u>585,821</u>      |
| CASH FLOWS FROM INVESTING ACTIVITIES                                                           |                     |                     |
| Purchases of property and equipment                                                            | (20,848)            | (23,931)            |
| Purchases of investments                                                                       | (656,796)           | (186,168)           |
| Proceeds from sales of investments                                                             | 18,900              | 160,472             |
| <u>NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES</u>                                     | <u>(658,744)</u>    | <u>(49,627)</u>     |
| CASH FLOWS FROM FINANCING ACTIVITIES                                                           | -                   | -                   |
| <u>NET INCREASE (DECREASE) IN CASH<br/>AND CASH EQUIVALENTS</u>                                | <u>126,016</u>      | <u>536,194</u>      |
| CASH AND CASH EQUIVALENTS,<br>BEGINNING OF YEAR                                                | <u>1,090,599</u>    | <u>554,405</u>      |
| <u>CASH AND CASH EQUIVALENTS,<br/>END OF YEAR</u>                                              | <u>\$ 1,216,615</u> | <u>\$ 1,090,599</u> |
| SUPPLEMENTAL CASH FLOW INFORMATION                                                             |                     |                     |
| CASH PAID DURING THE YEAR:                                                                     |                     |                     |
| Income taxes paid                                                                              | \$ -                | \$ -                |
| Interest paid                                                                                  | \$ -                | \$ -                |

See accompanying auditors' report.  
The notes are an integral part of these financial statements.

THE REASON FOUNDATION  
NOTES TO FINANCIAL STATEMENTS  
SEPTEMBER 30, 2011

Note 1 ORGANIZATION

The Reason Foundation (Foundation) was organized for the purpose of educating Americans in the basic principles of the classical liberal/libertarian political philosophy. Toward this end, the Foundation provides research and publications which apply free-market principles to public policy issues. The Foundation's activities include the monthly publication of Reason magazine and the publication of various studies on public policy issues.

Note 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation-

The financial statements are presented on the accrual basis and in accordance with the basis of Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) Numbers 958-605 and 958-205. These standards require that the Foundation report information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted and permanently restricted net assets.

Summarized Comparative Financial Information-

The financial statements include certain prior-year summarized comparative information in total, but not by net asset category. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Foundation's financial statements for the year ended September 30, 2010 from which the summarized information was derived.

Cash and Cash Equivalents-

For the purposes of the financial statement, the Foundation considers all highly liquid debt instruments purchased with a maturity date of three months or less to be cash equivalents.

Investments-

Investments in equity securities with readily determinable fair market values and all investments in debt securities are measured at fair value in the statement of financial position. Realized and unrealized gains and losses, interest and dividends on investments are reflected in the statement of activities as unrestricted unless these activities are restricted by donor or by law.

Contributions-

The Foundation has also adopted FASB ASC Number 958-605 and 958-720, "Accounting for Contributions Received and Contributions Made." In accordance with FASB ASC 958-605 and 958-720, contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. When a restriction expires (that is, when a stipulated time restriction ends or 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.



THE REASON FOUNDATION  
NOTES TO FINANCIAL STATEMENTS  
SEPTEMBER 30, 2011

Note 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT.)

Subsequent Event

Date of Management's Review - Subsequent events have been evaluated through January 11, 2012, the date that these financial statements were available to be issued.

Property and Equipment-

Property and equipment are recorded at historical cost and are being depreciated using the straight-line method over the estimated useful life of the assets. The following lives have been assigned:

|                         |         |
|-------------------------|---------|
| Furniture and equipment | 3 years |
| Leasehold improvements  | 5 years |

Expenditures for maintenance, repairs, and renewals of minor items are charged to expense as incurred. Major renewals and improvements are capitalized. Upon disposition, the cost and related accumulated depreciation are removed from the accounts and the resulting gain or loss is reflected in operations for the year. It is the Foundation's policy to expense items under \$1,000.

Tax Status-

The Foundation is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code, and is exempt from California franchise taxes under Section 23701(d) of the State Revenue and Taxation Code. In addition, the Foundation has been determined by the Internal Revenue Service not to be a private foundation within the meaning of Section 509(a) of the code.

Use of Estimates-

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

Advertising-

Advertising costs are charged to operations when incurred and are included in functional expenses.

Accounts and Pledges Receivable-

Accounts receivable at September 30, 2011 consist of individually small amounts from a large number of entities, and include advertising sales, list rentals, and magazine subscriptions. Management of the Foundation has assessed the credit risk associated with these accounts receivable and has established an allowance for doubtful accounts to reduce the net carrying value of the receivables to net realizable value. For the year ended September 30, 2011, the allowance for doubtful accounts was \$9,578.

THE REASON FOUNDATION  
NOTES TO FINANCIAL STATEMENTS  
SEPTEMBER 30, 2011

Note 2      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT.)

Pledges receivable at September 30, 2011 are due from organizations, corporations, and individuals well-known to the Foundation, with a favorable past payment history. Management of the Foundation has assessed the credit risk associated with these pledges receivable and has determined that an allowance for potential uncollectible amounts is not necessary.

Note 3      FUND ACCOUNTING

The financial statements of the Foundation are reported in self-balancing fund groups as follows:

Unrestricted Fund-

The unrestricted fund is part of the net assets of the Foundation that are not subject to donor-imposed stipulations. The only limits on unrestricted net assets are broad limits resulting from the nature of the Foundation and the purposes specified in its articles of incorporation or bylaws and, perhaps, limits resulting from contractual agreements.

Temporarily Restricted Fund-

The temporarily restricted fund is part of the net assets of the Foundation 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. The majority of contributions with restrictions are stipulated to be used as funds for educating Americans in the basic principles of the classical liberal/libertarian political philosophy. The use and nature of these contributions can result in a continually increasing balance in temporarily restricted net assets.

Permanently Restricted Fund-

The permanently restricted fund is used to record resources received that are permanently restricted as to use by the donor or grantor.

Note 4      FUNCTIONAL ALLOCATION OF EXPENSES

In accordance with FASB ASC Number 958-720-45 the costs of providing the program and the supporting services have been summarized on a functional basis in the statement of activities, and in the statement of functional expenses. Accordingly, certain costs have been allocated between the program and the supporting services in reasonable ratios determined by management.

THE REASON FOUNDATION  
 NOTES TO FINANCIAL STATEMENTS  
 SEPTEMBER 30, 2011

Note 5 CASH AND CASH EQUIVALENTS

The cash balance includes money market funds that earn interest at a rate which fluctuates according to prime and are carried at cost which approximates market. The cash balance is comprised of the following:

|                                 |                     |
|---------------------------------|---------------------|
| Checking                        | \$ 537,956          |
| Savings                         | 572,945             |
| Money market funds              | <u>105,714</u>      |
| Total cash and cash equivalents | <u>\$ 1,216,615</u> |

Note 6 INVESTMENTS

The Foundation's investments are reported at fair value in the accompanying statements of financial position for September 30, 2011.

|                   |                                                                      |
|-------------------|----------------------------------------------------------------------|
|                   | <u>Fair Value Measurements Using:</u>                                |
|                   | Quoted Prices in Active<br>Markets for Identical Assets<br>(Level 1) |
| Mutual funds      |                                                                      |
| Equity funds      | \$ 880,575                                                           |
| Bond funds        | <u>2,547,582</u>                                                     |
| Total investments | \$ 3,428,157                                                         |

FASB ASC Number 820-10 defines fair value, establishes a framework for measuring fair value, and expands disclosure about fair value measurements. This standard provides a consistent definition of fair value which focuses on an exit price between market participants in an orderly transaction, prioritizes the use of market based information over entity specific information and establishes a three level hierarchy for fair value measurements based on the transparency of information used in the valuation of an asset or liability as of the measurement date.

Fair values determined by Level 1 inputs utilize quoted prices in active markets for identical assets. Fair values determined by level 2 inputs utilize data points that are observable such as quoted prices, interest rates and yield curves. Fair values determined by level 3 inputs are unobservable data points for the asset and include situations where there is little, if any, market activity for the asset. There were no level 2 or 3 inputs as of September 30, 2011.

Note 7 MAILING LISTS

The Foundation has developed a mailing list of its subscribers during the course of its operations. For the year ended September 30, 2011, rentals of this list to certain list brokers generated revenue of \$21,541.

THE REASON FOUNDATION  
NOTES TO FINANCIAL STATEMENTS  
SEPTEMBER 30, 2011

Note 8      LINE OF CREDIT

The Foundation maintains a \$200,000 line of credit with a bank, collateralized by non-governmental accounts receivable, inventory, and equipment, which expires June 1, 2012. Interest accrues at the greater of the prime annual interest rate plus 1.00%, or the floor rate of 5.00%. The interest rate at September 30, 2011 was 5.00%. There was no outstanding balance at September 30, 2011.

Note 9      UNEARNED SUBSCRIPTIONS

Deferred revenue from prepaid magazine subscriptions is recognized as revenue over the term of the subscriptions. At September 30, 2011, the unearned portion of subscription revenue was as follows:

|                        |                   |
|------------------------|-------------------|
| Unearned subscriptions | \$ 418,759        |
| Less: current portion  | <u>(315,317)</u>  |
| Long-term portion      | <u>\$ 103,442</u> |

The long-term portion of the unearned subscriptions expires principally through the year ending September 30, 2014.

Note 10      COMMITMENTS

The Foundation leases office space in Los Angeles, California and Washington, District of Columbia expiring October 31, 2012 and February 28, 2013, respectively. The Foundation has a month-to-month operating lease expiring on September 25, 2011 and an automobile lease expiring September 9, 2014. Future minimum annual rental payments under these lease agreements are as follows:

| <u>Year Ending<br/>September 30,</u> | <u>Los Angeles<br/>Office</u> | <u>Washington<br/>Office</u> | <u>Automobile</u> | <u>Total</u>      |
|--------------------------------------|-------------------------------|------------------------------|-------------------|-------------------|
| 2012                                 | \$ 183,693                    | \$ 161,842                   | \$ 5,460          | \$ 345,535        |
| 2013                                 | 15,356                        | 68,129                       | 5,460             | 83,485            |
| 2014                                 | <u>-</u>                      | <u>-</u>                     | <u>5,005</u>      | <u>-</u>          |
| <b>Totals</b>                        | <u>\$ 199,049</u>             | <u>\$ 229,971</u>            | <u>\$ 15,925</u>  | <u>\$ 429,020</u> |

Rental expense for the year ended September 30, 2011, amounted to \$364,740.

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Note 11    **RESTRICTED NET ASSETS**

The restricted net assets are available for the various research programs for the following purposes:

Temporarily Restricted Funds:

|                        |                   |
|------------------------|-------------------|
| Magazine               | \$ 33,333         |
| Donor restricted funds | <u>68,617</u>     |
| Total                  | <u>\$ 101,950</u> |

Permanently Restricted Fund:

|                                                                                                   |                  |
|---------------------------------------------------------------------------------------------------|------------------|
| Donor restricted investments in perpetuity income<br>is expendable to support general operations. | <u>\$ 43,279</u> |
|---------------------------------------------------------------------------------------------------|------------------|

Note 12    **NET ASSETS RELEASED FROM RESTRICTION**

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrences of other events specified by donors.

Purpose/ Time Restrictions Accomplished:

|                                      |                   |
|--------------------------------------|-------------------|
| Magazine                             | \$ 18,900         |
| Pledges satisfied by passage of time | <u>217,151</u>    |
| Total                                | <u>\$ 236,051</u> |

Note 13    **TAX-SHELTERED RETIREMENT PLAN**

Any full time employee of the Foundation may set up a tax-sheltered retirement plan in accordance with Section 403(b) of the Internal Revenue Code. The Foundation assists the employee in setting up the plan and will arrange for the contributions to be made through payroll deductions. The Foundation does not make contributions to such plans.

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Note 14 CONCENTRATION OF CREDIT RISK

Financial instruments which potentially subject the Foundation to concentrations of credit risk consist of cash and cash equivalents, investments, accounts receivable and pledges receivable. The Foundation places its cash and money market funds principally with a high credit quality financial institution where the funds are guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 per institution. At times, such cash and money market fund balances may be in excess of the FDIC insurance limits. Management of the Foundation regularly reviews the financial stability of its cash and money market fund depository and deems the risk of loss due to these concentrations to be minimal. Management of the Foundation has assessed the credit risk associated with the investments held at September 30, 2011 and has determined that an allowance for potential losses due to credit risk in the investment portfolio is not necessary. At September 30, 2011, the amount over FDIC limits was \$890,418.

Note 15 ACCOUNTING FOR UNCERTAINTY IN INCOME TAXES

The Foundation has evaluated its tax positions and the certainty as to whether those tax positions will be sustained in the event of an audit by taxing authorities at the federal and state levels. The primary tax positions evaluated are related to the Foundation's continued qualification as a tax-exempt organization and whether there is unrelated business income activities conducted that would be taxable. Management has determined that all income tax positions are more likely than not (>50%) of being sustained upon potential audit or examination; therefore, no disclosures of uncertain income tax positions are required. Due to the statute of limitations, with very few exceptions, the foundation is no longer subject to examinations by federal and state tax authorities prior to year 2005.

Note 16 DONOR DESIGNATED ENDOWMENT

The Foundation's endowment consists of a fund established to create a permanent endowment. As required by generally accepted accounting principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Board of Trustees of the Foundation has interpreted the 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 absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) 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.

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Note 16 DONOR DESIGNATED ENDOWMENT (CONT.)

The investment committee has recommended the following investment policy which includes the endowment fund. This policy was adopted by the full Board of Trustees. Net assets are to be invested 70% in fixed income and 30% in equities. The spending policy is to allow distribution of an amount equal to 5% of the fair market value of the endowment fund. In any year in which the endowment experiences a net investment loss, no distributions will be made.

Endowment Net Asset Composition by Type of Fund as of September 30, 2011 is as follows:

|                                  | <u>Permanently<br/>Restricted</u> |
|----------------------------------|-----------------------------------|
| Donor-restricted endowment funds | \$ 43,279                         |
| Total funds                      | <u>\$ 43,279</u>                  |

Changes in endowment net assets as of September 30, 2011 are as follows:

|                                         | <u>Permanently<br/>Restricted</u> |
|-----------------------------------------|-----------------------------------|
| Endowment net assets, beginning of year | \$ 42,279                         |
| Contributions                           | 1,000                             |
| Investment income                       | -                                 |
| Net appreciation (depreciation)         | -                                 |
| Amounts appropriated for expenditure    | -                                 |
| Endowment net assets, end of year       | <u>\$ 43,279</u>                  |