

The David and Lucile Packard Foundation

**Consolidating Financial Statements
December 31, 2014**

The David and Lucile Packard Foundation
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December 31, 2014

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Independent Auditor's Report

To the Board of Trustees of
The David and Lucile Packard Foundation:

We have audited the accompanying individual and consolidated financial statements of The David and Lucile Packard Foundation ("Packard Foundation") and its affiliate, The Monterey Bay Aquarium Research Institute ("MBARI") (collectively, the "Foundation"), which comprise the individual and consolidated statements of financial position as of December 31, 2014, and the related individual and consolidated statements of activities and changes in net assets and cash flows for the year then ended.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the individual and consolidated 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 individual and consolidated 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 the individual and consolidated 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 individual and consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the individual and consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the individual and consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Foundation's preparation and fair presentation of the individual and consolidated 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 Foundation'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 individual and consolidated 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 individual and consolidated financial statements referred to above present fairly, in all material respects, the individual financial positions of the Packard Foundation and MBARI and the consolidated financial position of the Foundation at December 31, 2014, and the individual and consolidated changes in net assets and individual and consolidated cash flows for the Packard Foundation, MBARI and the Foundation, respectively, for the year then ended in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP

July 9, 2015

The David and Lucile Packard Foundation
Consolidating Statement of Financial Position
December 31, 2014

(dollars in thousands)

	Packard Foundation	MBARI	Eliminations	Total
Assets				
Cash and cash equivalents	\$ 61,214	\$ 8,844	\$ -	\$ 70,058
Interest and dividends receivable	1,581	-	-	1,581
Investment sales receivable	87,345	-	-	87,345
Investments, at fair value	6,744,765	-	-	6,744,765
Contributions receivable	-	49,714	(48,527)	1,187
Program-related investments	105,391	-	-	105,391
Property and equipment, net	75,345	52,049	-	127,394
Other assets	9,262	4,791	-	14,053
Total assets	<u>\$ 7,084,903</u>	<u>\$ 115,398</u>	<u>\$ (48,527)</u>	<u>\$ 7,151,774</u>
Liabilities and Net Assets				
Liabilities				
Accounts payable and other liabilities	\$ 10,189	\$ 10,239	\$ -	\$ 20,428
Investment purchases payable	4	-	-	4
Grants payable	123,635	-	(48,527)	75,108
Deferred federal excise tax liabilities	48,820	-	-	48,820
Postretirement benefit liabilities	20,372	31,646	-	52,018
Total liabilities	<u>203,020</u>	<u>41,885</u>	<u>(48,527)</u>	<u>196,378</u>
Net assets				
Unrestricted	6,881,883	34,539	38,974	6,955,396
Temporarily restricted	-	38,974	(38,974)	-
Total net assets	<u>6,881,883</u>	<u>73,513</u>	<u>-</u>	<u>6,955,396</u>
Total liabilities and net assets	<u>\$ 7,084,903</u>	<u>\$ 115,398</u>	<u>\$ (48,527)</u>	<u>\$ 7,151,774</u>

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

The David and Lucile Packard Foundation
Consolidating Statement of Activities and Changes in Net Assets
December 31, 2014

(dollars in thousands)

	<u>Packard Foundation</u>	<u>MBARI</u>	<u>Eliminations</u>	<u>Total</u>
Changes in unrestricted net assets				
Revenue and net investment income				
Interest and dividends	\$ 98,556	\$ 3	\$ -	\$ 98,559
Federal awards	-	5,804	-	5,804
Rental and other income	172	2,229	-	2,401
Contributions	-	14	-	14
Net realized and unrealized gain on investments	496,437	-	-	496,437
Investment related expenses	(13,982)	-	-	(13,982)
Net assets released from restriction	-	38,210	(38,210)	-
Revenue and net investment income before federal excise tax expense	581,183	46,260	(38,210)	589,233
Federal excise tax expense	(13,396)	-	-	(13,396)
Revenue and net investment income	567,787	46,260	(38,210)	575,837
Expenses				
Grants awarded	294,979	-	(38,974)	256,005
Direct charitable expenses	3,363	41,880	-	45,243
Program operating expenses	29,716	8,456	-	38,172
Total expenses	328,058	50,336	(38,974)	339,420
Increase (decrease) in unrestricted net assets before change in unrestricted net assets from actuarial gains/losses and amortization	239,729	(4,076)	764	236,417
Change in unrestricted net assets from actuarial gains/losses and amortization	(6,675)	(9,171)	-	(15,846)
Increase (decrease) in unrestricted net assets	233,054	(13,247)	764	220,571
Changes in temporarily restricted net assets				
Contributions	-	38,974	(38,974)	-
Net assets released from restriction	-	(38,210)	38,210	-
Increase in temporarily restricted net assets	-	764	(764)	-
Increase (decrease) in net assets	233,054	(12,483)	-	220,571
Net assets				
Beginning of year	6,648,829	85,996	-	6,734,825
End of year	\$ 6,881,883	\$ 73,513	\$ -	\$ 6,955,396

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

The David and Lucile Packard Foundation
Consolidating Statement of Cash Flows
December 31, 2014

(dollars in thousands)

	<u>Packard Foundation</u>	<u>MBARI</u>	<u>Eliminations</u>	<u>Total</u>
Cash flows from operating activities				
Increase (decrease) in net assets	\$ 233,054	\$ (12,483)	\$ -	\$ 220,571
Adjustments to reconcile increase (decrease) in net assets to net cash (used in) provided by operating activities				
Net realized and unrealized gains on investments	(496,437)	-	-	(496,437)
Change in net assets from actuarial gains/losses and amortization	6,675	9,171	-	15,846
Depreciation and amortization	4,064	6,751	-	10,815
Loss on disposal of property and equipment	-	17	-	17
Changes in operating assets and liabilities				
Interest and dividends receivable	4,165	-	-	4,165
Contributions receivable	-	(878)	-	(878)
Other assets	226	(410)	-	(184)
Grants payable	5,996	-	-	5,996
Accounts payable and other liabilities	554	251	-	805
Postretirement benefit liabilities	1,710	1,801	-	3,511
Deferred federal excise tax liabilities	5,614	-	-	5,614
Net cash (used in) provided by operating activities	<u>(234,379)</u>	<u>4,220</u>	<u>-</u>	<u>(230,159)</u>
Cash flows from investing activities				
Purchases of investments	(3,177,554)	-	-	(3,177,554)
Proceeds from sales and maturities of investments	3,345,372	-	-	3,345,372
Principal advances to program-related investment loan recipients	(53,922)	-	-	(53,922)
Principal repayments received from program-related investment loan recipients	34,447	-	-	34,447
Purchases of property and equipment	(1,435)	(4,505)	-	(5,940)
Net cash provided by (used in) investing activities	<u>146,908</u>	<u>(4,505)</u>	<u>-</u>	<u>142,403</u>
Net decrease in cash and cash equivalents	(87,471)	(285)	-	(87,756)
Cash and cash equivalents				
Beginning of year	148,685	9,129	-	157,814
End of year	<u>\$ 61,214</u>	<u>\$ 8,844</u>	<u>\$ -</u>	<u>\$ 70,058</u>
Supplemental disclosures of cash flow information				
Cash paid for federal excise and other taxes	\$ 7,500	\$ -	\$ -	\$ 7,500
Non-cash capital expenditures	8	-	-	8

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

The David and Lucile Packard Foundation

Notes to Consolidating Financial Statements

December 31, 2014

(dollars in thousands)

1. Organization

The David and Lucile Packard Foundation (the “Packard Foundation”) is a private foundation established by David and Lucile Packard. The Packard Foundation provides funding primarily to not-for-profit organizations operating predominantly in three program areas that are of particular interest to the Board of Trustees: conservation and science; population and reproductive health; and children, families and communities. The Packard Foundation’s primary facilities are located in Los Altos, California.

The Monterey Bay Aquarium Research Institute (“MBARI”) is a not-for-profit organization founded in 1987 for the purpose of conducting scientific research in marine biology, oceanography, underwater geology, and other kinds of marine research in and around the Monterey Bay and elsewhere, and to educate the scientific community and the general public in regard to such research. MBARI’s primary facilities are located in Moss Landing, California.

Certain trustees and officers of the Packard Foundation are also officers or directors of MBARI. Trustees of the Packard Foundation are not permitted to vote for grants to organizations for which they serve as trustees, officers or directors. The Packard Foundation is MBARI’s only member, with the power to elect the Board of Directors.

2. Basis of Presentation and Significant Accounting Policies

Principles of Consolidation

The accompanying consolidating financial statements include the accounts of the Packard Foundation and its affiliate, MBARI (collectively, the “Foundation”). Since the Packard Foundation has both control and an economic interest in MBARI, the financial statements of MBARI have been included in the consolidating financial statements of the Foundation. All significant intercompany transactions and balances have been eliminated in the consolidation.

Basis of Presentation

The accompanying consolidating financial statements are presented on the accrual basis of accounting and in conformity with accounting principles generally accepted in the United States of America applicable to not-for-profit organizations. Revenues are reported as increases in unrestricted net assets, unless there are donor-imposed purposes and/or time restrictions on the gifted assets. Expenses are reported as decreases in unrestricted net assets. Gains or losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law.

Use of Estimates

The preparation of consolidating financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include the valuation of the Foundation’s investments and program-related investments, the expected useful lives of property and equipment, the determination of postretirement benefit liabilities, and the determination of functional expense allocations.

The David and Lucile Packard Foundation

Notes to Consolidating Financial Statements

December 31, 2014

(dollars in thousands)

Unrestricted Net Assets

Unrestricted net assets represent unrestricted resources available to support the Foundation's operations and temporarily restricted resources that have become available for use by the Foundation in accordance with the intentions of donors.

Temporarily Restricted Net Assets

Temporarily restricted net assets represent gifts that are limited in use by MBARI in accordance with donor-imposed stipulations. These stipulations may expire with time or may be satisfied and removed by the actions of MBARI according to the terms of the gift. At December 31, 2014, MBARI's temporarily restricted net assets consist entirely of gifts from the Packard Foundation restricted to the subsequent year's operations. Temporarily restricted net assets of \$38,210 were released from restriction due to the expiration of time restrictions during the year ended December 31, 2014.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash and money market funds. The Foundation considers investments with maturities of three months or less at the time of purchase to be cash equivalents.

Investments

Investments are stated at fair value and purchases and sales are recorded on a trade or contract date basis. The estimated fair value of investments is based on quoted market prices, except for alternative investments for which quoted market prices are not available. Alternative investments include private equities, marketable alternatives (including hedge funds), and real assets. The estimated fair value of alternative investments is based on the net asset value of the fund provided by the general partner. The Packard Foundation reviews and evaluates the net asset values provided by the general partner and assesses the valuation methods and assumptions used in determining the fair value of the alternative investments. Because alternative investments are not readily marketable, their estimated value is subject to uncertainty and therefore may differ from the value that would have been used had a readily available market for such investments existed and differences could be material. Unrealized gains or losses on investments resulting from fair value fluctuations are recorded in the consolidating statement of activities and changes in net assets in the period that such fluctuations occur.

Investment Sales Receivable and Investment Purchases Payable

Investment sales and purchases are recorded on a trade-date basis, which results in both investment receivables and payables on unsettled investment trades. The Packard Foundation is subject to credit risk should a broker be unable to meet its obligations to the Packard Foundation.

Fair Value of Financial Instruments

In accordance with Accounting Standards Codification ("ASC") 820, *Fair Value Measurements*, fair value is defined as the price that the Foundation would receive upon selling an investment in an orderly transaction to an independent buyer in the principal or most advantageous market of the investment. ASC 820 established a three-tier hierarchy to maximize the use of observable market data and minimize the use of unobservable inputs, and to establish classification of fair value measurements for disclosure purposes. Inputs refer broadly to the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the

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Notes to Consolidating Financial Statements

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(dollars in thousands)

reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best available information.

The three-tier hierarchy of inputs is summarized in the three broad levels listed below.

- Level I Quoted prices in active markets for identical assets and liabilities.
- Level II Pricing inputs, including broker quotes, are generally those other than exchange quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.
- Level III Pricing inputs are unobservable for the investment and includes situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation. Investments that are included in this category generally include privately held investments and partnership interests.

See Note 3 for a summary of the inputs used as of December 31, 2014 in determining the fair value of the Packard Foundation's investments.

Concentrations of Credit Risk

Financial instruments that potentially subject the Foundation to credit risk consist primarily of cash, cash equivalents, investments and unsettled investment trades. The Foundation maintains cash and cash equivalents primarily with major financial institutions. Cash equivalents include investments in money market funds. Such amounts may exceed Federal Deposit Insurance Corporation limits. The Packard Foundation's readily marketable securities have been placed with major financial institutions. Contributions receivable consists primarily of funds due to MBARI from the Packard Foundation.

Program-Related Investments

Program-related investments at December 31, 2014 include \$104,108 of loans made to organizations, \$201 of collateral deposits that serve to guarantee loans made by third-party lenders to organizations as a means of assisting them in achieving charitable objectives and \$1,082 equity investments in sustainable forest management and carbon offset project companies. Interest rates on loans receivable range from 0% to 5% as of December 31, 2014, and are generally repayable over 2 to 14 years. Management has reviewed the collectability of all program-related investments and has determined no allowance is necessary as of December 31, 2014.

Property and Equipment

Property and equipment is stated at cost when purchased or fair value at the date of donation and is depreciated using the straight-line method over estimated useful lives of 3 to 30 years. Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

Grants

Grants are recognized when the unconditional promise to give is approved. Conditional promises to give are recognized as grant expense in the period in which the recipient meets the terms of the condition. There were no conditional promises to give at December 31, 2014.

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(dollars in thousands)

Revenue Recognition

Contributions are recognized as revenues when they are received or unconditionally pledged. MBARI 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, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the accompanying consolidating statement of activities and changes in net assets as net assets released from restriction. Temporarily restricted contributions are reported as unrestricted support when the restriction is met in the same period as the contribution is received.

Functional Expense Allocations

The Packard Foundation's operating expenses have been allocated between direct charitable and program operating activities based on direct charitable activity and estimates made by the Packard Foundation's management of time spent by employees on various activities.

The Packard Foundation's direct charitable expenses pertain to charitable activities for the benefit of others initiated and conducted in whole or in part by the Packard Foundation. Program operating expenses pertain to the general grant making activities of the Packard Foundation, such as reviewing proposals and awarding, monitoring and evaluating grants.

MBARI's direct charitable expenses pertain to the general purpose of conducting scientific research in marine biology, oceanography, underwater geology, and other kinds of marine research in and around the Monterey Bay. Program operating expenses include costs related to managing MBARI.

Tax-Exempt Status

The Foundation is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code and from California franchise and/or income taxes under section 23701(d) of the Revenue and Taxation Code. To the extent the Foundation carries out investment activities that are subject to unrelated business income tax, it is subject to income taxation.

Recent Accounting Pronouncements

In May 2015, the Financial Accounting Standards Board issued *Accounting Standards Update No. 2015-07, Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, which eliminates the requirement to categorize investments measured using the Net Asset Value ("NAV") practical expedient in the fair value hierarchy table. Entities will be required to disclose the fair value of investments measured using the NAV practical expedient so that financial statement users can reconcile amounts reported in the fair value hierarchy table to amounts reported on the balance sheet. The new guidance will be applied retrospectively and is effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. Early adoption is permitted. Foundation management is currently evaluating the impact that the new guidance will have on the financial statements.

The David and Lucile Packard Foundation

Notes to Consolidating Financial Statements

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(dollars in thousands)

3. Investments

The investment goal of the Packard Foundation is to maintain or grow its spending power in real inflation adjusted terms with risk at a level appropriate to the Packard Foundation's programmatic spending and objectives. To accomplish this investment goal, the Packard Foundation diversifies its investments (held directly and indirectly) across various financial instruments and asset categories, and implements multiple investment strategies. The Packard Foundation's financial assets, with the exception of Hewlett-Packard, Agilent and Keysight common stock, are managed by a select group of external investment management firms and held in custody by major banks. Investments allocated to partnerships, limited liability companies and commingled funds have separate arrangements appropriate to their legal structure.

The Packard Foundation's investments (held directly or indirectly) in developed market securities and emerging market securities consist of exchange traded public equities, treasury and corporate bonds. The Packard Foundation's investments in marketable alternatives consist of long/short, opportunistic and special situation investment management firms, trading public securities and over-the-counter securities. The Packard Foundation's investments in limited partnerships, private equity and real assets are in securities and companies that cannot be immediately liquidated, such as buyout and venture capital firms, real estate and natural resource firms. The Packard Foundation's investments (held directly or indirectly) in fixed income securities consist primarily of investment grade instruments issued by the U.S. government and its agencies and by U.S. corporations, U.S. Treasury securities and mortgage-backed securities.

The Packard Foundation's real estate investment is located in Los Altos, California and is valued based upon recent appraisals.

Investment securities are exposed to various risks, such as changes in interest rates or credit ratings and market fluctuations. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is possible that the value of the Packard Foundation's investments and total net assets balance could fluctuate materially.

Legal, tax and regulatory changes could occur during the term of the Packard Foundation's private partnerships. The regulatory environment for private partnerships is evolving, and changes in the regulation of these partnerships may adversely affect the value of investments held by the Packard Foundation. The Packard Foundation believes that the effect of any future regulatory change on the Packard Foundation's assets would not be material.

The David and Lucile Packard Foundation
Notes to Consolidating Financial Statements
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(dollars in thousands)

The following table summarizes the valuation of the Packard Foundation's investments per the ASC 820 fair value hierarchy levels as of December 31, 2014:

	<u>Level I</u>	<u>Level II</u>	<u>Level III</u>	<u>Ending Balance at December 31, 2014</u>
Developed market equities	\$ 322,150	\$ -	\$ 1,384,198	\$ 1,706,348
Emerging market equities	108,468	-	716,175	824,643
Private equities	-	-	656,190	656,190
Marketable alternatives	-	-	2,116,906	2,116,906
Real assets	-	-	769,713	769,713
Fixed income securities	-	669,310	-	669,310
Los Altos real estate and other	-	-	1,655	1,655
Total investments	<u>\$ 430,618</u>	<u>\$ 669,310</u>	<u>\$ 5,644,837</u>	<u>\$ 6,744,765</u>
Total cash and cash equivalents	<u>\$ 61,214</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 61,214</u>

There were no transfers between each level of the fair value hierarchy during the year ended December 31, 2014.

The David and Lucile Packard Foundation
Notes to Consolidating Financial Statements
December 31, 2014

(dollars in thousands)

The following table summarizes the Packard Foundation's Level III rollforward per ASC 820 as of December 31, 2014:

	Beginning Balance at December 31, 2013	Realized Gains (Losses)	Change in Unrealized Gains (Losses)	Purchases	Sales and Settlements	Ending Balance at December 31, 2014	Change in Unrealized Gains (Losses) for Open Positions Held December 31, 2014
Level III Assets							
Developed market equities	\$ 1,341,020	\$ 18,017	\$ 69,671	\$ 20,000	\$ (64,510)	\$ 1,384,198	\$ 69,671
Emerging market equities	531,485	9	125,232	59,604	(155)	716,175	125,232
Private equities	450,543	27,132	105,017	169,040	(95,542)	656,190	104,880
Marketable alternatives	1,896,309	4,428	59,018	228,705	(71,554)	2,116,906	59,018
Real assets	671,582	31,231	192	204,448	(137,740)	769,713	192
Los Altos real estate and other	1,591	-	64	-	-	1,655	64
	<u>\$ 4,892,530</u>	<u>\$ 80,817</u>	<u>\$ 359,194</u>	<u>\$ 681,797</u>	<u>\$ (369,501)</u>	<u>\$ 5,644,837</u>	<u>\$ 359,057</u>

All net realized and change in unrealized gains (losses) in the table above are reflected in the consolidating statement of activities and changes in net assets.

The net gain on the Packard Foundation's investment portfolio for the year ended December 31, 2014 consists of the following:

	Packard Foundation
Net realized gain	\$ 235,024
Net change in unrealized gain	<u>261,413</u>
	<u>\$ 496,437</u>

The David and Lucile Packard Foundation
Notes to Consolidating Financial Statements
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(dollars in thousands)

The Packard Foundation's Level III assets are valued using unobservable but nonquantitative inputs. These assets include financial instruments for which the determination of fair value is based on prices from prior transactions or third-party pricing information without adjustment from management and financial instruments for which fair value is determined using NAV as a practical expedient. The Packard Foundation uses NAV to determine the fair value of all the underlying investments which (a) do not have a readily determinable fair value and (b) prepare their financial statements consistent with the measurement principles of an investment company or have the attributes of an investment company. Per the fair value measurements guidelines, the below table lists investment companies (in partnership format) by major asset class:

<u>Asset Class</u>	<u>Strategy</u>	<u>NAV in Funds</u>	<u># of Funds</u>	<u>Remaining Life (yrs.)</u>	<u>Amount of Unfunded Commitments</u>	<u>Timing to Draw Down Commitments (yrs.)</u>	<u>Redemption Terms</u>	<u>Redemption Restrictions</u>
Public equity	Contains developed and emerging equity	\$ 2,100,373	17	1 to 16	\$ 84,000	1 to 5	Ranges between monthly redemption with 90 day notice, to annual redemption with 90 day notice	Lock up provisions of up to 5 years
Private equity	Contains growth, international, leveraged buyouts and venture capital	656,190	37	1 to 12	402,993	1 to 5	Not eligible for redemption	Not eligible for redemption
Marketable alternatives	Contains global long/short equity, opportunistic and special situations	2,116,906	20	1 to 10	60,363	1 to 4	Ranges between quarterly redemption with 30 day notice, to annual redemption with 180 day notice	Lock up provisions of up to 5 years
Real assets	Contains natural resources and real estate	769,713	48	1 to 12	640,039	1 to 5	Not eligible for redemption	Not eligible for redemption
		<u>\$ 5,643,182</u>	<u>122</u>		<u>\$ 1,187,395</u>			

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Notes to Consolidating Financial Statements
December 31, 2014

(dollars in thousands)

4. Property and Equipment

Property and equipment at December 31, 2014 consisted of the following:

	<u>Packard Foundation</u>	<u>MBARI</u>	<u>Total</u>
Land	\$ 26,648	\$ 4,236	\$ 30,884
Buildings	53,295	50,312	103,607
Research vessels	-	42,635	42,635
Remotely operated vehicles	-	19,739	19,739
Ocean deployed equipment	-	25,752	25,752
Office furniture and equipment	16,004	20,169	36,173
Capital projects in progress	1,109	5,421	6,530
	<u>97,056</u>	<u>168,264</u>	<u>265,320</u>
Accumulated depreciation	<u>(21,711)</u>	<u>(116,215)</u>	<u>(137,926)</u>
Property and equipment, net	<u>\$ 75,345</u>	<u>\$ 52,049</u>	<u>\$ 127,394</u>

Depreciation expense for the year ended December 31, 2014 was \$4,064 and \$6,751 for the Packard Foundation and MBARI, respectively.

5. Grants Payable

The Packard Foundation ordinarily makes grants to organizations that qualify as public charities under the Internal Revenue Code ("IRC"). When distributions are made to nonqualifying organizations, the Packard Foundation assumes the responsibility for the ultimate charitable use.

Grants awarded but unpaid are payable at December 31, 2014 as follows:

	<u>Packard Foundation</u>
Less than 1 year	\$ 86,260
1 to 5 years	<u>37,375</u>
	<u>\$ 123,635</u>

The David and Lucile Packard Foundation

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(dollars in thousands)

6. Federal Excise Taxes and Other Taxes

In accordance with the applicable provisions of the IRC, the Packard Foundation is a private foundation and qualifies as a tax-exempt organization. Private foundations are liable for an excise tax of 2% (1% if minimum payout requirements prescribed by the IRC are met) on net investment income, excluding unrealized gains, as defined. The Packard Foundation was subject to the 2% rate for the year ended December 31, 2014. Deferred excise taxes arise primarily from unrealized tax basis gains on investments and are calculated at the effective rate expected to be paid by the Packard Foundation.

The income from certain investments is subject to unrelated business income tax.

The provision for current and deferred federal excise taxes for the year ended December 31, 2014 was as follows:

	Packard Foundation
Current	\$ 7,782
Deferred	<u>5,614</u>
	<u>\$ 13,396</u>

Distribution Requirements

The Packard Foundation is subject to the distribution requirements of the IRC. Accordingly, it must distribute within one year after the end of each fiscal year 5% of the fair value of its investment assets, as defined. The investments that can be included for the 5% distribution requirement are based on average monthly balances and are exclusive of those investments deemed to be held for charitable activities or program-related investments. In determining qualifying distributions, grant payments are considered on a cash basis and certain expenses are considered as qualifying distributions. The Packard Foundation has complied with the distribution requirements through December 31, 2014.

MBARI is a private operating foundation within the meaning of Section 509(a) of the IRC that makes its required charitable expenditures by sponsoring and managing its own programs. Pursuant to Section 4940(a) of the IRC, MBARI's investment income, reduced by certain allowable expenses, is subject to excise tax at a rate of 2% of investment income. MBARI's status as an operating foundation is determined annually by satisfying the income test and certain other numerical tests. Generally, a private operating foundation must make qualifying distributions of 4.25% of the average fair value of the foundation's investment assets directly for the active conduct of the activities for which it is organized and operating. MBARI has met the requirements for private operating foundation status through December 31, 2014.

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7. Retirement Plans

The Packard Foundation Retirement Plans are as follows:

The Packard Foundation sponsors defined contribution plans under both IRC Section 401(a) and 403(b). The plans cover all employees who meet eligibility requirements. Contributions to the 401(a) plan are made by the Packard Foundation at 15% of an employee's annual salary. Under the 403(b) plan and subject to statutory limits, employees make voluntary deferred salary contributions to the plan. Total expense related to such plans was \$2,012 during 2014. As of December 31, 2014, \$117 was accrued related to the plans.

The Packard Foundation also has a voluntary salary deferral plan for highly compensated employees under IRC Section 457(b). Employees with a base salary of \$175 and above are eligible to participate in the plan. As of December 31, 2014, \$1,017 was deferred based on elections made by the participants.

The Packard Foundation has a Nonqualified Benefits Restoration Plan (the "Restoration Plan") primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees to accumulate retirement assets. The Restoration Plan allows the Packard Foundation to make contributions to a participant's account equal to the amount in excess of IRC limits that the participant would otherwise have been eligible for in accordance with the Packard Foundation's 401(a) plan. The Restoration Plan is intended to be an unfunded plan although voluntary contributions are made to a grantor trust. Total expense related to the Restoration Plan was \$157 during 2014.

The Packard Foundation has a contributory retiree medical program (the "Plan") that will cover substantially all employees who meet eligibility requirements. The Packard Foundation will pay from 55% to 75% of the insurance premium for eligible retired employees with a minimum age of 55 and the combination of years of service and age equal to 65 or greater. This Plan can be amended at any time upon Board approval.

The following information presents the Plan's unfunded status and amounts recognized in the consolidating statement of financial position as of December 31, 2014, based on a measurement date of December 31, 2014:

	Packard Foundation
Benefit obligation	\$ (20,372)
Fair value of plan assets	<u>-</u>
Unfunded status	<u>(20,372)</u>
Amount recognized in the consolidating statement of financial position as postretirement benefit liabilities	<u>\$ (20,372)</u>

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Amounts recognized in unrestricted net assets at December 31, 2014 were as follows:

	<u>Packard Foundation</u>
Prior service cost	\$ 1,187
Net loss	<u>8,036</u>
	<u>\$ 9,223</u>

The estimated prior service cost and net loss for the Plan that will be amortized from unrestricted net assets into net periodic postretirement benefit cost in 2015 is as follows:

	<u>Packard Foundation</u>
Amortization of prior service cost	\$ 184
Amortization of net loss	<u>732</u>
	<u>\$ 916</u>

Changes in unrestricted net assets as a result of actuarial gains/losses and amounts amortized for the year ended December 31, 2014 were as follows:

	<u>Packard Foundation</u>
Net actuarial gains and losses	\$ 6,859
Amortization of net gain	-
Amortization of prior service cost	<u>(184)</u>
Total recognized in unrestricted net assets	<u>\$ 6,675</u>

The Packard Foundation's contributions to the Plan and benefit payments made from the Plan for the year ended December 31, 2014 were \$121. Participants' contributions totaled \$69 for the year ended December 31, 2014.

The net periodic postretirement benefit cost reflected in the consolidating statement of activities and changes in net assets related to the Plan for the year ended December 31, 2014 was \$1,831.

A weighted-average discount rate of 3.99% was used in determining the accumulated postretirement benefit obligation as of December 31, 2014 and a weighted-average discount rate of 4.96% was used in determining the net periodic postretirement benefit cost for the year ended December 31, 2014.

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The Plan is fully insured and is funded on a pay-as-you-go basis. The estimated minimum benefit payments by year that reflect expected future service, as appropriate, to be paid by the Packard Foundation are as follows:

Years Ending December 31,	<u>Packard Foundation</u>
2015	\$ 209
2016	265
2017	337
2018	405
2019	501
2020-2024	3,740

The annual rate of increase in the per capita cost of medical benefits (i.e., health care cost trend rate) is assumed to be 8% in 2016, declining by 0.25% per year through 2028 and then remaining at 5% thereafter. A 1% point increase in this rate would increase the accumulated postretirement benefit obligation by \$4,852 and the service cost plus interest cost components of the net periodic postretirement benefit cost by \$398. A 1% point decrease in this rate would decrease the accumulated postretirement benefit obligation by \$3,716 and the service cost plus interest cost components of net periodic postretirement benefit cost by \$306.

MBARI Retirement Plans are as follows:

MBARI sponsors defined contribution plans under both IRC Section 401(a) and 403(b). The plans cover all employees who meet eligibility requirements. Contributions to the 401(a) plan are made by MBARI at 10% of an employee's annual salary. Under the 403(b) plan and subject to statutory limits, employees make voluntary deferred salary contributions to the plan. Total expense related to such plans was \$2,058 during 2014.

MBARI sponsors a Section 457(b) Qualified Eligible Salary Deferral Plan (the "Salary Deferral Plan") primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees to accumulate retirement assets. The Salary Deferral Plan enables participants to defer income on a pre-tax basis. At December 31, 2014, MBARI held related assets of \$2,670 that are included in other assets. These assets are designated by MBARI to pay future Salary Deferral Plan liabilities of \$2,670 as of December 31, 2014. These liabilities are included in accounts payable and other liabilities.

MBARI also sponsors a Nonqualified Deferred Compensation Restoration Plan (the "Compensation Restoration Plan") primarily for the purpose of providing deferred compensation for a select group of management or highly compensated employees to accumulate retirement assets. The Compensation Restoration Plan provides for MBARI to make contributions to a participant's account equal to the amount in excess of IRC limits which the participant would otherwise have been eligible for in accordance with MBARI's 401(a) plan. At December 31, 2014, MBARI held other assets of \$8 that are included in other assets, which are designated by MBARI to pay future Deferred Compensation Restoration Plan liabilities of \$8 as of December 31, 2014. These liabilities are included in accounts payable and other liabilities.

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MBARI has a contributory retiree health insurance program (the "Plan") which covers substantially all employees who meet the eligibility requirements. Each August 1st, MBARI makes a contribution on behalf of each retired employee to a healthcare savings account (HSA). The amount of the contribution is 50% of the annual premium that is charged by MBARI's health insurer for an employee with the same family status (single or two-party coverage) as the retiree. The retiree may then spend the amount in the HSA on any medical expenses that are tax-deductible, including premiums for health insurance.

As a result of a plan amendment, the accumulated plan benefit obligation was re-measured on March 1, 2009. On that date, the discount rate was set as 6.68%. The accumulated plan benefit obligation on March 1, 2009 was \$7,051 before the plan amendment and \$7,635 after the plan amendment. The difference of \$584 was added to the unrecognized prior service cost and is being amortized in periods after March 1, 2009.

The following information presents the MBARI Plan's unfunded status and amount recognized in the consolidating statement of financial position as of December 31, 2014, based on a measurement date of December 31, 2014:

	<u>MBARI</u>
Benefit obligation	\$ (31,646)
Fair value of plan assets	<u>-</u>
Unfunded status	<u>(31,646)</u>
Amount recognized in the consolidating statement of financial position as postretirement benefit liabilities	<u>\$ (31,646)</u>

Amounts recognized in unrestricted net assets at December 31, 2014 were as follows:

	<u>MBARI</u>
Prior service cost	\$ 24
Net loss	<u>9,507</u>
	<u>\$ 9,531</u>

The estimated prior service cost and net loss for the Plan that will be amortized from unrestricted net assets into net periodic postretirement benefit cost in 2015 is as follows:

	<u>MBARI</u>
Amortization of prior service cost	\$ 24
Amortization of net loss	<u>881</u>
	<u>\$ 905</u>

Changes in postretirement benefit liabilities recognized in unrestricted net assets were as follows:

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	<u>MBARI</u>
Net loss	\$ 9,267
Prior service cost	-
Amortization of net gain	-
Amortization of prior service cost	<u>(96)</u>
Total recognized in unrestricted net assets	9,171
Net periodic postretirement benefit cost	<u>1,844</u>
Total recognized in net periodic benefit cost and unrestricted net assets	<u>\$ 11,015</u>

Total contributions paid and benefit payments made from the MBARI Plan for the year ended December 31, 2014 were \$43 and \$43, respectively.

The weighted-average discount rate used in determining the accumulated postretirement benefit obligation was 4% as of December 31, 2014, and in determining the net periodic postretirement benefit cost was 5.04% for the year ended December 31, 2014.

The MBARI Plan is fully insured and is funded on a pay-as-you-go basis. The estimated minimum benefit payments by year that reflect expected future service, as appropriate, to be paid by MBARI are as follows:

	<u>MBARI</u>
Years Ending December 31,	
2015	\$ 165
2016	291
2017	408
2018	521
2019	624
2020-2024	4,870

The annual rate of increase in the per capita cost of medical benefits (i.e., health care cost trend rate) was assumed to be 10% in 2014 and 12% in 2015, declining by 2% per year through 2018, and then remaining at 5% thereafter. A 1% point increase or decrease in this rate would increase or decrease the accumulated postretirement benefit obligation by \$7,852 and \$(6,006), respectively, and increase or decrease the service cost plus interest cost components of the net periodic postretirement benefit cost by \$455 and \$(345), respectively, for the year ended December 31, 2014.

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8. Commitments and Contingent Liabilities

The Foundation has noncancelable operating leases for certain land, facilities, furniture and equipment. The terms of these leases expire in 2016 through 2039, with certain options to renew. Certain rental rates are subject to adjustment based on increases in the consumer price index. Future minimum lease payments under noncancelable operating leases at December 31, 2014 are as follows:

	<u>Packard Foundation</u>	<u>MBARI</u>	<u>Total</u>
Years Ending December 31,			
2015	\$ 27	\$ 164	\$ 191
2016	9	169	178
2017	-	137	137
2018	-	28	28
2019	-	29	29
Thereafter	-	749	749
	<u>\$ 36</u>	<u>\$ 1,276</u>	<u>\$ 1,312</u>

Rent expense for the Foundation for the year ended December 31, 2014 was \$188.

As of December 31, 2014, MBARI has \$500 on deposit as collateral to guarantee that MBARI will comply with the provisions of a land lease entered into with the State of California, California State Lands Commission to obtain right-of-way use needed for the construction of one of MBARI's projects, the MARS Project. This amount is included in other assets in the consolidating statement of financial position.

MBARI derives a portion of its revenues from various federally funded programs that are subject to review and audit by governmental oversight agencies. MBARI management believes that MBARI is in material compliance with the standards set forth by the federal governmental agencies and that the outcome of reviews and audits conducted by such agencies will not have a significant effect on the financial position or changes in net assets of MBARI.

Claims

Claims are filed from time to time against MBARI in the ordinary course of business. MBARI is not aware of any such matters that would have a material adverse effect on MBARI's financial position.

9. Minimum Future Rental Revenues

MBARI leases land and facilities to others under noncancelable leases with lease terms expiring in 2015 and 2017, with options to renew. Certain rental rates are subject to annual increases ranging up to 3%.

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Minimum future rental receipts from operating leases having noncancelable lease terms in excess of one year as of December 31, 2014 are approximately as follows:

	<u>MBARI</u>
Years Ending December 31,	
2015	\$ 154
2016	119
2017	<u>61</u>
	<u>\$ 334</u>

10. Credit Facilities

The Packard Foundation has an uncommitted line of credit ("LOC") of \$100,000 with The Northern Trust Company. This LOC note is annually renewable. At December 31, 2014, the outstanding principal balance on the line of credit was \$0. The Packard Foundation has the option of choosing the interest rate on the LOC based upon the Prime-Based Rate, London Interbank Offered Rate ("Libor") or Bank Offered Rate.

11. Subsequent Events

The Foundation has evaluated subsequent events for the period December 31, 2014 through July 9, 2015, the date the financial statements were available to be issued, and believes no additional disclosures are required.