

THE MUSEUM OF ART AND HISTORY  
AT THE MCPHERSON CENTER

(A California Public Benefit Corporation)

\* \* \*

FINANCIAL STATEMENTS

AND

SUPPLEMENTARY INFORMATION

\* \* \*

June 30, 2012

THE MUSEUM OF ART AND HISTORY  
AT THE MCPHERSON CENTER  
(A California Public Benefit Corporation)

June 30, 2012

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**EMERITUS**

Alexander W. Berger (1916-2005)  
Griffith R. Lewis

CERTIFIED PUBLIC ACCOUNTANTS AND BUSINESS ADVISORS

## INDEPENDENT AUDITOR'S REPORT

Board of Directors  
Museum of Art and History  
at the McPherson Center  
Santa Cruz, California

We have audited the accompanying statement of financial position of the Museum of Art and History at the McPherson Center (a California public benefit corporation) as of June 30, 2012, and the related statements of activities and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States 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 Museum of Art and History at the McPherson Center as of June 30, 2012, and the changes in its net assets and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 8 on page 11 to the financial statements, the Museum of Art and History at the McPherson Center is party to a draft agreement with the County of Santa Cruz covering the office/retail building. No payments have been made since inception of the agreement. Management believes that settlement of the agreement will not have a material effect on the Museum's financial position. Nevertheless, it is at least reasonably possible that upon settlement of the agreement such an effect will occur, although the amount cannot be estimated.

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The schedules of unrestricted funds financial position, activities and changes in net assets, and functional expenses on pages 19 through 24 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

*Berger Lewis Accountancy Corporation*

BERGER LEWIS ACCOUNTANCY CORPORATION  
Santa Cruz, California  
October 2, 2012

THE MUSEUM OF ART AND HISTORY  
AT THE MCPHERSON CENTER  
(A California Public Benefit Corporation)

STATEMENT OF FINANCIAL POSITION

June 30, 2012

ASSETS				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
CURRENT ASSETS:				
Cash and Cash Equivalents	\$ 565,067	\$ 356,029		\$ 921,096
Accounts Receivable	45,130	69,000		114,130
Prepaid Expenses	10,199			10,199
Inventories	53,572			53,572
Total Current Assets	673,968	425,029		1,098,997
PROPERTY, EQUIPMENT, AND IMPROVEMENTS, NET	4,235,762			4,235,762
OTHER ASSETS:				
Investments		17,605	\$ 233,071	250,676
Funds Held by Community Foundation	44,556			44,556
Origination Fee, Net of Amortization	17,333			17,333
Lease Reserve	176,000			176,000
Total Other Assets	237,889	17,605	233,071	488,565
TOTAL ASSETS	\$ 5,147,619	\$ 442,634	\$ 233,071	\$ 5,823,324

See Independent Auditor's Report and Accompanying Notes to the Financial Statements

THE MUSEUM OF ART AND HISTORY  
AT THE MCPHERSON CENTER  
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STATEMENT OF FINANCIAL POSITION  
(Continued)

June 30, 2012

LIABILITIES AND NET ASSETS

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
CURRENT LIABILITIES:				
Current Portion - Capital Lease	\$ 100,000			\$ 100,000
Accrued Interest	37,030			37,030
Accounts Payable	19,673			19,673
Tenant Deposits	28,990			28,990
Accrued Personal Time Off	22,286			22,286
	<u>207,979</u>			<u>207,979</u>
Total Current Liabilities				
	<u>207,979</u>			<u>207,979</u>
NON-CURRENT LIABILITIES:				
Capital Lease Payable	1,299,156			1,299,156
	<u>1,299,156</u>			<u>1,299,156</u>
Total Non-Current Liabilities				
	<u>1,299,156</u>			<u>1,299,156</u>
NET ASSETS:				
Unrestricted:				
Operating	3,626,051			3,626,051
Board Designated - Publications Fund	14,433			14,433
Total Unrestricted Net Assets	3,640,484			3,640,484
Temporarily Restricted		\$ 442,634		442,634
Permanently Restricted			\$ 233,071	233,071
	<u>3,640,484</u>	<u>442,634</u>	<u>233,071</u>	<u>4,316,189</u>
Total Net Assets				
	<u>3,640,484</u>	<u>442,634</u>	<u>233,071</u>	<u>4,316,189</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 5,147,619</u>	<u>\$ 442,634</u>	<u>\$ 233,071</u>	<u>\$ 5,823,324</u>

See Independent Auditor's Report and Accompanying Notes to the Financial Statements

THE MUSEUM OF ART AND HISTORY  
AT THE MCPHERSON CENTER  
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STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

For the Year Ended June 30, 2012

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUE AND OTHER SUPPORT:				
Contributions	\$ 258,861	\$ 415,833		\$ 674,694
In-Kind Contributions	51,148			51,148
Grants	31,375			31,375
Fundraising Events, Net of Direct Costs	65,906			65,906
Special Appeals	17,385			17,385
Memberships	116,961			116,961
Rent and Assessments	743,307			743,307
Santa Cruz County Contract	110,611			110,611
Interest Income	5,885	4,095		9,980
Other Income	6,508			6,508
Museum Store Sales	12,434			12,434
Admissions	17,242			17,242
Program Service Fees	90,776			90,776
Facility Rental Income	39,195			39,195
Unrealized Gains & Losses on Investments	137	(11,914)		(11,777)
Net Assets Released from Restrictions	22,500	(22,500)		
Total Revenue and Other Support	<u>1,590,231</u>	<u>385,514</u>		<u>1,975,745</u>
EXPENSES:				
Program -				
Museum	727,884			727,884
Expenses Related to Rents	417,657			417,657
Special Events	22,737			22,737
Supporting Services -				
Management and General	121,117			121,117
Development	64,859			64,859
Total Expenses	<u>1,354,254</u>	<u>0</u>		<u>1,354,254</u>
CHANGE IN NET ASSETS	235,977	385,514		621,491
NET ASSETS, Beginning of Year	<u>3,404,507</u>	<u>57,120</u>	<u>\$ 233,071</u>	<u>3,694,698</u>
NET ASSETS, End of Year	<u>\$ 3,640,484</u>	<u>\$ 442,634</u>	<u>\$ 233,071</u>	<u>\$ 4,316,189</u>

See Independent Auditor's Report and Accompanying Notes to the Financial Statements

THE MUSEUM OF ART AND HISTORY  
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STATEMENT OF CASH FLOWS

For the Year Ended June 30, 2012

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CASH FLOWS FROM OPERATING ACTIVITIES:

Change in Net Assets	\$ 621,491
Adjustments to Reconcile Decrease in Net Assets to Net Cash Provided by Operating Activities:	
Depreciation and Amortization	213,513
Unrealized Loss on Investments	9,894
(Increase) Decrease in Operating Assets:	
Receivables	(1,014)
Grants Receivable	(69,000)
Other Assets	(6,825)
Increase (Decrease) in Operating Liabilities:	
Accounts Payable	16,012
Accrued Personal Time Off	2,774
Accrued Interest	(3,372)
Deposits	<u>13,490</u>

CASH FLOWS PROVIDED BY OPERATING ACTIVITIES	<u>796,963</u>
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CASH FLOWS FROM FINANCING ACTIVITIES:

Purchase of Fixed Assets	(21,905)
Principal Payments on Capital Lease - Building	<u>(95,000)</u>

CASH FLOWS USED IN FINANCING ACTIVITIES	<u>(116,905)</u>
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INCREASE IN CASH AND CASH EQUIVALENTS	680,058
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CASH AND CASH EQUIVALENTS, Beginning of Year	<u>241,038</u>
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CASH AND CASH EQUIVALENTS, End of Year	<u><u>\$ 921,096</u></u>
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SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

Interest Paid	<u><u>\$ 77,432</u></u>
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See Independent Auditor's Report and Accompanying Notes to Financial Statements



THE MUSEUM OF ART AND HISTORY  
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NOTES TO FINANCIAL STATEMENTS

June 30, 2012

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1. GENERAL INFORMATION:

The Museum of Art and History at the McPherson Center is a California nonprofit public benefit corporation that operates under the direction of a board of trustees. The Museum's objectives and purposes include exploring diverse cultural ideas, issues and perspectives through artistic experience and regional history. Dedicated to excellence, the Museum provides accessible programs, exhibits, resources and services for exploration, education and research; collection and preservation of works of art and regional historic resources; and development and maintenance of public awareness and appreciation.

The Organization receives a substantial amount of support from donations from individuals and businesses located in Santa Cruz County, which is affected by the local economy. Additional sources of revenue include grants from foundations and a contract with the County of Santa Cruz.

The McPherson Center consists of two components: 1) Museum building, housing the exhibit and administrative offices of the Museum of Art and History and, 2) Office/Retail Building, containing approximately 23,873 square feet of office and retail space. The Museum has hired a professional management company, PACCOM, to manage the office and retail space.

The funding mix for the project consisted of the following:

Economic Development Administration of the United States - Economic Adjustment Assistance Award in the amount of \$1,920,000 and California Department of Commerce local match of \$640,000.

Capital lease from Santa Cruz County in the amount of \$2,255,000 at an annual interest rate of 7.1 percent.

Major Fundraising Campaign - The predecessors, the Art Museum of Santa Cruz County and the History Museum of Santa Cruz County, under their joint venture agreement raised \$3,590,006, toward the project.

Significant subcommittees of the Board responsible for overseeing certain aspects of the Organization are: 1) Finance Management Committee, responsible for preparing annual budgets for Board approval and related tasks; 2) Center Management Committee, responsible for physical plan management and leasing and operation of the Office/Retail building; and 3) Development Committee, responsible for guiding Museum efforts for contribution and membership growth.

THE MUSEUM OF ART AND HISTORY  
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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Basis of Presentation - The financial statements of the Organization are presented in accordance with Statement of Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) (formerly Statement of Financial Accounting Standards (SFAS)). Under ASC the Organization is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. As of June 30, 2012, the Organization had \$442,634 in temporarily restricted net assets and \$233,071 in permanently restricted net assets.

Temporarily Restricted Funds - As provided by ASC, the Organization has classified donor-restricted assets as unrestricted assets in cases where the restrictions are met in the same period as when the resources are received.

Recognition of Donor Restricted Contributions - Donor-restricted support is reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restriction. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets.

Cash and Cash Equivalents - For purposes of reporting cash flows, the Organization considers all cash accounts which are not subject to withdrawal restrictions or penalties, and certificates of deposit with original maturities of 90 days to be cash or cash equivalents.

Accounts Receivable - Receivables consist of rent and related charges due from tenants. All receivables are expected to be collected.

Property and Equipment - All property and equipment are stated at cost. Major improvements are charged to the property accounts, while maintenance and repairs which do not extend the life for the respective assets are expensed currently. When property is retired or otherwise disposed of, the cost of the property and the related accumulated depreciation are removed from the accounts and any resulting gains or losses are reflected in income.

Depreciation - Depreciation is computed by use of the straight-line method based on the estimated useful life of the respective assets.

Inventory - Inventory is comprised of books and goods for sale and is stated at the lower of cost or market determined by the first-in, first-out basis.

THE MUSEUM OF ART AND HISTORY  
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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

Collections - The Organization acquires its collections through purchase or by donation in-kind. No value has been assigned to the collections on the balance sheet in accordance with policies followed by art museums and only current year purchases, and not donations in-kind, are reflected in the Statement of Activities. The Organization acquires most of its archival collections through donations. The value of archives acquired through donations is not susceptible to objective valuation and have not been reflected in the financial statements. The collection consists of books, ledgers, clothing, furniture, documents and photographs of items of historical interest.

Taxes on Income - The Organization is exempt from income taxation under Internal Revenue Code Section 501(c)(3) and California Revenue and Taxation Code Section 23701(d). Therefore, no provision for income taxes has been recorded on the financial statements.

Donated Materials, Services and Facilities - Donated materials and professional services are recorded as contributions at their estimated values at date of receipt. Donated volunteer services have not been reflected in the financial statements since no objective basis is available to measure the value of such services. Nevertheless, a substantial number of volunteers donate significant amounts of their time in the Organization's program and supporting services, principally in membership development and in the display of exhibits.

Estimates - The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that 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.

Expenses Subject to Common Area Charges - Office/Retail Building - Certain expenses are reimbursable to the Museum by tenants under lease agreements entered into with the Museum of Art and History. The assessment is subject to an annual accounting and adjustment.

3. CAPITAL LEASE PAYABLE:

Capital lease payable at June 30, 2012, consisted of the following:

Santa Cruz County - Entered into on March 22, 1993, principal payable in annual escalating amounts, with interest of 7.1 percent per annum, payable in semi-annual amounts based on outstanding balance.	\$1,399,156
Less: Current Portion	(100,000)
	<u>\$1,299,156</u>

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THE MUSEUM OF ART AND HISTORY  
AT THE MCPHERSON CENTER  
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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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3. CAPITAL LEASE PAYABLE (Continued):

Minimum future lease payments are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>
2013	\$ 100,000
2014	110,000
2015	115,000
2016	125,000
2017	135,000
Thereafter	<u>814,156</u>
	<u>\$1,399,156</u>

During the fiscal years ended June 30, 2000 and 2001, the County of Santa Cruz deferred a portion of the payments due under the capital lease noted above, which totaled \$174,156. This balance is being treated as a 0% interest bearing loan, payment of which will become due at the end of the lease term in 2021 and is included in the long-term portion of capital lease balance. Interest expense on the lease for fiscal year ended June 30, 2012 was \$74,060.

4. SUPPORT:

The Organization received a substantial amount of its support from local government. A significant reduction in the level of this support, if this were to occur, may have an effect on the Organization's programs and activities.

5. SALES AND SUBSEQUENT REPURCHASE OF THE MUSEUM IMPROVEMENTS:

In March of 1993, to secure additional funds the Museum Venture sold the Museum Building and leasehold improvements to the County of Santa Cruz with the Museum Venture retaining the right to buy back the Museum Building and leasehold improvements for an amount equal to the debt service payments on the Series C Bonds totaling \$2,255,000 sold by the County to complete the funding of The Museum Venture Project. Terms of the capital lease are disclosed in Note 3. Due to bond requirements, recorded title to the building remains in the name of the County of Santa Cruz until the Series C bonds are retired.

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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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6. ORIGINATION FEES:

Origination fees attributable to the Santa Cruz County note have been capitalized as part of the capital lease agreement (see Note 3). They are being amortized over the 315-month life of the lease which corresponds to the loan held by the County on the old jail building.

Original Loan Fee	\$ 65,000
Accumulated Amortization	<u>(47,667)</u>
Loan Fee, Net	<u>\$ 17,333</u>

7. LEASE RESERVE:

As part of the funding of the Santa Cruz County Capital Lease, \$176,000 was set up as a Lease Reserve as part of the capital lease agreement (see Note 3). The interest earned on that reserve reduces the interest paid on the Santa Cruz County Lease on an annual basis.

8. LEASE AGREEMENT/CONTINGENCY:

A draft lease agreement with the County of Santa Cruz covering the Office/Retail Building, which specifies that a percent of net rent be paid to the County, is under negotiation. The amount of any liability to the County is undetermined at this time.

9. MAJOR TENANT:

As of June 30, 2012, rent from two tenants in the Office/Retail Building represented the majority of gross base rent. Gross base rent from tenants is as follows:

	Average Monthly Base Rent	Percent of Gross Base Rent
Tenant A	\$ 18,995	39%
Tenant B	17,302	36%
Various Other Tenants	<u>12,168</u>	<u>25%</u>
	<u>\$ 48,465</u>	<u>100%</u>

THE MUSEUM OF ART AND HISTORY  
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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

10. PROPERTY, EQUIPMENT, AND IMPROVEMENTS:

Details of Property Equipment and Improvements as of June 30, 2012 and related depreciation expense for the year then ended were as follows:

<u>Asset</u>	<u>Museum</u>	<u>McPherson Center</u>	<u>Total</u>
Equipment	\$ 61,985		\$ 61,985
Museum Furnishings	16,162		16,162
Equipment	15,308	\$ 23,386	38,694
Museum Store	68,625		68,625
Leasehold Improvements	212,712		212,712
Museum Building	3,655,268		3,655,268
Jail/Office Building		<u>4,162,809</u>	<u>4,162,809</u>
	<u>4,030,060</u>	<u>4,186,195</u>	<u>8,216,255</u>
Depreciation	<u>(1,972,243)</u>	<u>(2,008,250)</u>	<u>(3,980,493)</u>
	<u>\$ 2,057,817</u>	<u>\$ 2,177,945</u>	<u>\$ 4,235,762</u>
Depreciation Expense	<u>\$ 102,692</u>	<u>\$ 108,345</u>	<u>\$ 211,037</u>

11. CONCENTRATION OF CREDIT AND MARKET RISK FOR CASH AND EQUIVALENTS AND INVESTMENTS:

The Organization maintains their cash and cash equivalents in bank deposit accounts at various financial institutions. The balances at times may exceed federally insured limits. At June 30, 2012, the Organization had \$164,169 in bank deposits in excess of the \$250,000 FDIC limits. Those funds may be covered by other provisions.

The Organization holds investment funds in various brokerage accounts with investments in mutual funds subject to market risk, the risk that investment will decrease due to market risk factors.

12. CONCENTRATION OF RISK:

The Organization is mainly dependent on membership revenue, donations and contributions from the community, and net rent revenue from its Office/Retail Building for its operations. The Organizations rent income is concentrated in two major tenants as disclosed in note 9.

THE MUSEUM OF ART AND HISTORY  
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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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13. TEMPORARILY RESTRICTED NET ASSETS:

Temporarily restricted net assets are available for the following purposes or periods:

Anonymous Donor - History Gallery Upgrade	\$ 29,696
Unrealized gain on investments	17,605
Foundation Grants for Programs	363,333
Individual Donations towards Specific Exhibition Projects	<u>32,000</u>
Total Temporarily Restricted Net Assets	<u>\$ 442,634</u>

14. INVESTMENT IN SPLIT-INTEREST AGREEMENTS:

The Museum has a remainder interest in a charitable remainder annuity trust for which it is not acting as trustee. The trust was originally created in June 1997. The present value of the estimated proceeds is computed using Internal Revenue Service actuarial tables which take into account required annuity distributions to the donor (8%) as well as return on investment over the years. The present value is shown on the Statement of Financial Position as "Contributions Receivable - Split-Interest Agreements" in the period in which all relevant information is received. At the end of each year, the trust is revalued and the change recorded as a gain or loss in the Statement of Activities. The fair market value of the Harding Charitable Remainder Annuity Trust assets was written down to zero in fiscal year ended June 30, 2011, as the value was negligible.

15. COLLECTIONS:

The Organization's collections are made up of artifacts of historical significance; and art objects that are held for educational, research, scientific, and curatorial purposes. Each of the items is cataloged, preserved, and cared for, and activities verifying their existence and assessing their condition are performed continuously. The collections are subject to a policy that requires proceeds from their sales to be used to acquire other items for collections.

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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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16. EMPLOYEE BENEFIT PLANS:

During the year ended June 30, 2001, the Museum entered into a tax-deferred annuity plan qualified under Section 403(b) of the Internal Revenue Code. The plan covers all employees of the Museum. The Museum has discretion to vary the contribution rate from year to year. For the year ended June 30, 2012, the Museum contributed 0% of gross salaries for qualified employees to the plan. Employees may make contributions to the plan up to the maximum amount allowed by the Internal Revenue Code, if they wish.

17. INVESTMENTS:

Investments are presented in the financial statements at fair market value in accordance with ASC 958. As of June 30, 2012, investments consisted of:

	<u>Cost</u>	<u>Fair Value</u>	<u>Unrealized Appreciation (Depreciation)</u>
Mutual Funds	\$ 294,477	\$ 250,676	\$ (43,801)
Assets Held at Community Foundation	40,513	44,556	4,043

Investment return is summarized as follows:

Dividend and Interest Income	\$ 9,980
Net Realized & Unrealized Gain (Loss)	(11,777)

18. FAIR VALUE MEASUREMENTS:

The Organization follows the provisions of ASC 820-10 (formerly SFAS No. 157, *Fair Value Measurements*). ACS 820-10 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements.

***Fair Value Hierarchy***

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820-10 also establishes a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value.



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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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18. FAIR VALUE MEASUREMENTS (Continued):

In accordance with ASC 820, the Organization applied the following fair value hierarchy:

Level 1 - Assets and liabilities for which the identical item is traded on an active exchange, such as publicly-traded instruments or future contracts.

Level 2 - Assets and liabilities valued based on observable market data for similar instruments.

Level 3 - Assets and liabilities for which significant valuation assumptions are not readily observable in the market; instruments valued based on best available data some of which is internally developed, and considers risk premiums that a market participant would require.

The following is a description of calculation methodologies used for assets and liabilities recorded at fair value and the basis for estimating fair value. These are reflected as recurring or non-recurring in compliance with required disclosures.

Assets:

Cash and Cash Equivalents - Cash equivalents include money market and investment accounts that hold excess liquid funds. The fair value measurement of these assets are based on quoted market prices in active markets, and therefore are recorded at fair value on a recurring basis and are classified as Level 1 assets.

The following table presents the Organization's fair value hierarchy for those assets measured at fair value as of June 30, 2012:

	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Investment Held By Community Fdn.	\$ 44,556		\$44,556	
Investment held at Fidelity	102,637	\$102,637		
Investment held at TD Ameritrade	148,038	148,038		

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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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19. SUBSEQUENT EVENTS:

The Organization's management has evaluated events and transactions subsequent to June 30, 2012, for potential recognition or disclosure in the financial statements. The Organization did not have subsequent events that required recognition or disclosure in the financial statements for the year ended June 30, 2012. Subsequent events have been evaluated through October 2, 2012, the date the financial statements became available to be issued. The entity has not evaluated subsequent events after October 2, 2012.

20. INCOME TAXES:

The Organization is a tax-exempt corporation under Internal Revenue Code Section 501(c)(3) and California state franchise tax under Section 23701(d) of the Revenue and Taxation Code. Therefore, no provisions for income taxes have been recorded on the financials.

The Organization follows ASC 740-10 (formerly FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48)). ASC 740-10 clarifies accounting for uncertainty in income taxes and prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement for tax positions taken or expected to be taken in a tax return. No amounts have been recorded in the financial statements under ASC 740-10. The Organization is current in all Federal and State tax filing obligations and the returns are subject to standard statute of limitations applicable under the governing Federal and State tax statutes.

21. ENDOWMENT FUND:

The Organization's endowment consists of funds established for a variety of purposes. Its endowment includes both donor restricted endowment funds and funds designated by the Board of Directors to function as endowments. As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor imposed restrictions.

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NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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21. ENDOWMENT FUND (Continued):

Interpretation of Relevant Law - The Board of Directors of the Organization has interpreted the California version of the Uniform Prudent Management of Institutional Funds Acts (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 Organization 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. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Organization in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- (1) The duration and preservation of the fund.
- (2) The purposes of the donor-restricted endowment funds.
- (3) General economic conditions.
- (4) The possible effect of inflation and deflation.
- (5) The expected total return from income and the appreciation of investments.
- (6) The other resources of the Organization.
- (7) The investment policies of the Organization.

Funds with Deficiencies - From time to time, the fair value of assets associated with donor-restricted endowment funds may fall below the permanently restricted net assets balance. In accordance with *Generally Accepted Accounting Principles* (GAAP), deficiencies of this nature that are reported in unrestricted net assets totaled \$-0- as of June 30, 2012.

Investment Return Objectives, Risk Parameters and Strategies - The Organization has adopted investment and spending policies, approved by the Board of Directors, for endowment assets. The investment policy seeks to maintain fund principal and provide a reasonable rate of return. Safety of principal and preservation of capital is based on prudent investment principles. While short-term stability is desirable, achieving superior long-term returns takes precedence as an investment objective.

THE MUSEUM OF ART AND HISTORY  
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(A California Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS  
(Continued)

June 30, 2012

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21. ENDOWMENT FUND (Continued):

Spending Policy - The Organization has a policy of classifying investment income on endowment funds as temporarily restricted, unless otherwise specified by the donor. However as the Organization is actively working to increase the total endowment, investment income has remained as temporarily restricted. Along with working to increase endowed funds, the Organization is also working on revising and fully developing its investment and spending policies.

Endowment net asset composition by type of fund as of June 30, 2012, consisted of the following:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor Restricted Endowment Funds	\$ <u>-0-</u>	\$ <u>17,605</u>	\$ <u>233,071</u>	\$ <u>250,676</u>

Changes in endowment net assets for the fiscal year ended June 30, 2012, consisted of the following:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment, Net Assets, Beginning of Year		\$ 25,424	\$ 233,071	\$ 258,495
Contributions				
Investment Loss		(7,819)		(7,819)
Endowment, Net Assets, End of Year	\$ <u>-0-</u>	\$ <u>17,605</u>	\$ <u>233,071</u>	\$ <u>250,676</u>

## SUPPLEMENTARY INFORMATION

THE MUSEUM OF ART AND HISTORY  
AT THE MCPHERSON CENTER  
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SCHEDULE OF FINANCIAL POSITION -  
UNRESTRICTED FUNDS

June 30, 2012

ASSETS				
	Museum	Supporting Organizations	McPherson Center	Total
CURRENT ASSETS:				
Cash and Cash Equivalents	\$ 342,104	\$ 16,629	\$ 206,334	\$ 565,067
Accounts Receivable (Net of Allowance)	30,070		15,060	45,130
Other Assets	2,682		7,517	10,199
Inventories	53,572			53,572
Total Current Assets	428,428	16,629	228,911	673,968
PROPERTY, EQUIPMENT AND IMPROVEMENTS, NET	2,057,817		2,177,945	4,235,762
OTHER ASSETS:				
Funds Held by Community Foundation	44,556			44,556
Origination Fee, Net of Amortization	17,333			17,333
Lease Reserve	176,000			176,000
Total Other Assets	237,889		0	237,889
TOTAL ASSETS	\$ 2,724,134	\$ 16,629	\$ 2,406,856	\$ 5,147,619

See Independent Auditor's Report and Accompanying Notes to the Financial Statements

THE MUSEUM OF ART AND HISTORY  
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SCHEDULE OF FINANCIAL POSITION -  
UNRESTRICTED FUNDS  
(Continued)

June 30, 2012

LIABILITIES AND NET ASSETS

	<u>Museum</u>	<u>Supporting Organizations</u>	<u>McPherson Center</u>	<u>Total</u>
CURRENT LIABILITIES:				
Current Portion Capital Lease	\$ 100,000			\$ 100,000
Accrued Interest	37,030			37,030
Accounts Payable	19,000		\$ 673	19,673
Tenant and Facilities Rental Deposits	13,590		15,400	28,990
Accrued Personal Time Off	22,286			22,286
Total Current Liabilities	<u>191,906</u>		<u>16,073</u>	<u>207,979</u>
NON-CURRENT LIABILITIES:				
Capital Lease Payable	<u>1,299,156</u>			<u>1,299,156</u>
Total Non-Current Liabilities	<u>1,299,156</u>		<u>0</u>	<u>1,299,156</u>
NET ASSETS, UNRESTRICTED	<u>1,233,072</u>	<u>\$ 16,629</u>	<u>2,390,783</u>	<u>3,640,484</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 2,724,134</u>	<u>\$ 16,629</u>	<u>\$ 2,406,856</u>	<u>\$ 5,147,619</u>

See Independent Auditor's Report and Accompanying Notes to the Financial Statements

THE MUSEUM OF ART AND HISTORY  
AT THE MCPHERSON CENTER  
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SCHEDULE OF ACTIVITIES AND CHANGES IN NET ASSETS -  
UNRESTRICTED FUNDS

For the Year Ended June 30, 2012

	<u>Museum</u>	<u>Supporting Organizations</u>	<u>McPherson Center</u>	<u>Total</u>
REVENUE AND OTHER SUPPORT:				
Contributions	\$ 258,861			\$ 258,861
In-Kind Contributions	51,148			51,148
Grants	31,375			31,375
Special Events Fundraising (Net of Expenses)	33,058	\$ 32,848		65,906
Special Appeals	17,385			17,385
Memberships	96,378	20,583		116,961
Rent and Assessments			\$ 743,307	743,307
Santa Cruz County Contract	110,611			110,611
Interest Income	5,732	5	148	5,885
Other Income	6,508			6,508
Museum Store Sales	12,434			12,434
Admissions	17,242			17,242
Program Service Fees	90,776			90,776
Facility Rental Income	39,195			39,195
Unrealized Gains	137			137
Net Assets Released from Restrictions	22,500			22,500
 TOTAL REVENUE AND OTHER SUPPORT	 <u>793,340</u>	 <u>53,436</u>	 <u>743,455</u>	 <u>1,590,231</u>

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THE MUSEUM OF ART AND HISTORY  
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SCHEDULE OF ACTIVITIES AND CHANGES IN NET ASSETS -  
UNRESTRICTED FUNDS  
(Continued)

For the Year Ended June 30, 2012

	<u>Museum</u>	<u>Supporting Organizations</u>	<u>McPherson Center</u>	<u>Total</u>
EXPENSES:				
Program -				
Museum	\$ 699,634	\$ 28,250		\$ 727,884
Expenses Related to Operations			\$ 417,657	417,657
Special Events		22,737		22,737
Supporting Services -				
Management and General	120,199	918		121,117
Development	64,859			64,859
Total Expenses	<u>884,692</u>	<u>51,905</u>	<u>417,657</u>	<u>1,354,254</u>
OPERATING TRANSFERS IN (OUT)	<u>221,000</u>		<u>(221,000)</u>	<u>-</u>
CHANGE IN NET ASSETS	129,648	1,531	104,798	235,977
RECLASSIFICATION OF MUSEUM BUILDING ASSETS AND RELATED DEBT	816,776		(816,776)	-
NET ASSETS, BEGINNING OF YEAR	<u>286,648</u>	<u>15,098</u>	<u>3,102,761</u>	<u>3,404,507</u>
NET ASSETS, END OF YEAR	<u>\$ 1,233,072</u>	<u>\$ 16,629</u>	<u>\$ 2,390,783</u>	<u>\$ 3,640,484</u>

See Independent Auditor's Report and Accompanying Notes to the Financial Statements

THE MUSEUM OF ART AND HISTORY  
AT MCPHERSON CENTER  
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SCHEDULE OF FUNCTIONAL EXPENSES

For the Year Ended June 30, 2012

		Program Service	Management & General	Development	Total
EXPENSES:					
5100	Salary/Wages	\$ 226,999	\$ 81,577	\$ 46,109	\$ 354,685
5101	Payroll Service	1,190	427	241	1,858
5105	Benefits	25,445	9,143	5,167	39,755
5110	Payroll Taxes	18,356	6,597	3,729	28,682
5115	Auto/Mileage	286			286
5125	Printing	28,946		1,847	30,793
5126	Stationery	2,882	1,036	586	4,504
5129	Credit Card Fees	10,941			10,941
5131	Major Donors			947	947
5135	Dues	398			398
5143	Staff	790	284	160	1,234
5145	Equipment Lease	3,933	1,414	799	6,146
5155	Postage	3,140		200	3,340
5157	Bulk Mail Postage	3,175			3,175
5165	Supplies	4,489	1,613	912	7,014
5170	Taxes & Licenses	3,704			3,704
5175	Telephone	5,143	1,847	1,045	8,035
5185	Volunteer Expense	1,500			1,500
5190	Auditing Fee		8,000		8,000
5195	Maintenance		1,542		1,542
5200	Computer Expense	5,223	1,877	1,060	8,160
5205	Bank Service Charges		2,785		2,785
5210	Other Professional Service	(431)			(431)
5212	Professional Services	12,267			12,267
5215	Graphics	5,465			5,465
5230	Member Receptions Expense	7,010			7,010
5256	Curatorial Fees	2,337			2,337
5257	Crating and Materials	46			46
5260	Installation Exhibition	20,138			20,138
5265	Permanent Collection Expense	304			304
5270	Exhibition Shipping	781			781
5280	Exhibit Insurance Expense	1,250			1,250

See Independent Auditor's Report and Accompanying Notes to the Financial Statements

THE MUSEUM OF ART AND HISTORY  
AT MCPHERSON CENTER  
(A California Public Benefit Corporation)

STATEMENT OF FUNCTIONAL EXPENSES  
(Continued)

For the Year Ended June 30, 2012

EXPENSES:	<u>Program Service</u>	<u>Management &amp; General</u>	<u>Development</u>	<u>Total</u>
5301 Family and Kids Programs	\$ 1,350			\$ 1,350
5306 Public Programs Expense	15,163			15,163
5310 Gallery Activities	1,233			1,233
5311 School Programs	4,389			4,389
5315 Trunks Expense	67			67
5319 Hawley Classroom	375			375
5320 Evergreen Programs	308			308
5321 Docent Education	22			22
5331 Blue Plaque Expense	1,568			1,568
5360 Promotion	3,783			3,783
5370 Interest	74,068			74,068
5380 Fire/Security	7,929	\$ 81	\$ 81	8,091
5385 Insurance	17,655	180	180	18,015
5390 Janitorial/Landscaping	11,250	115	115	11,480
5400 PG&E	32,971	336	336	33,643
5405 Parking Deficiency Fund	6,227	64	64	6,355
5410 Repair/Replacement	17,349	177	177	17,703
5415 Utility - Other	5,091	52	52	5,195
5420 Depreciation and Amortization Expense	103,065	1,052	1,052	105,169
5590 Other Expense	64			64
	<u>\$ 699,634</u>	<u>\$ 120,199</u>	<u>\$ 64,859</u>	<u>\$ 884,692</u>
Depreciation and Amortization	\$ 108,345			\$ 108,345
McPherson Center Operating Expense	309,312			309,312
	<u>\$ 417,657</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 417,657</u>

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