

THE MUSEUM OF ART AND HISTORY
AT THE MCPHERSON CENTER

(A California Public Benefit Corporation)

* * *

FINANCIAL STATEMENTS

AND

SUPPLEMENTARY INFORMATION

June 30, 2014

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

June 30, 2014

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FOUNDERS

Alexander W. Berger (1916-2005)
Griffith R. Lewis (1930-2012)

CERTIFIED PUBLIC ACCOUNTANTS AND BUSINESS ADVISORS

INDEPENDENT AUDITOR'S REPORT

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

We have audited the accompanying financial statements of The Museum of Art and History at the McPherson Center (a California public benefit corporation), which comprise the statement of financial position as of June 30, 2014, and the related statements of activities, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Museum of Art and History at the McPherson Center as of June 30, 2014, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

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 and activities and changes in net assets, and of functional expenses on pages 18-23 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.

A handwritten signature in cursive script that reads "Berger Lewis Accountancy Corporation".

BERGER LEWIS ACCOUNTANCY CORPORATION
Santa Cruz, California
October 13, 2014

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

STATEMENT OF FINANCIAL POSITION

June 30, 2014

ASSETS				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
CURRENT ASSETS:				
Cash and Cash Equivalents	\$ 907,602	\$ 486,436		\$ 1,394,038
Accounts Receivable	17,562	490,000		507,562
Prepaid Expenses	14,738			14,738
Inventories	59,027			59,027
Total Current Assets	998,929	976,436		1,975,365
PROPERTY, EQUIPMENT, AND IMPROVEMENTS, NET	4,167,615			4,167,615
OTHER ASSETS:				
Investments		68,972	\$ 233,071	302,043
Funds Held by Community Foundation	53,021			53,021
Origination Fee, Net of Amortization	12,382			12,382
Lease Reserve	176,000			176,000
Total Other Assets	241,403	68,972	233,071	543,446
TOTAL ASSETS	\$ 5,407,947	\$ 1,045,408	\$ 233,071	\$ 6,686,426

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, 2014

LIABILITIES AND NET ASSETS

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
CURRENT LIABILITIES:				
Current Portion - Capital Lease	\$ 115,000			\$ 115,000
Accrued Interest	29,575			29,575
Accounts Payable	21,399			21,399
Tenant Deposits	22,575			22,575
Accrued Personal Time Off	29,324			29,324
	<u>217,873</u>			<u>217,873</u>
Total Current Liabilities				
	<u>217,873</u>			<u>217,873</u>
NON-CURRENT LIABILITIES:				
Capital Lease Payable	1,074,156			1,074,156
	<u>1,074,156</u>			<u>1,074,156</u>
Total Non-Current Liabilities				
	<u>1,074,156</u>			<u>1,074,156</u>
NET ASSETS:				
Unrestricted:				
Operating	3,989,572			3,989,572
Board Designated - Operating Reserve	100,000			100,000
Board Designated- Publications Fund	26,346			26,346
Total Unrestricted Net Assets	4,115,918			4,115,918
Temporarily Restricted		\$ 1,045,408		1,045,408
Permanently Restricted			\$ 233,071	233,071
	<u>4,115,918</u>	<u>1,045,408</u>	<u>233,071</u>	<u>5,394,397</u>
Total Net Assets				
	<u>4,115,918</u>	<u>1,045,408</u>	<u>233,071</u>	<u>5,394,397</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 5,407,947</u>	<u>\$ 1,045,408</u>	<u>\$ 233,071</u>	<u>\$ 6,686,426</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, 2014

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUE AND OTHER SUPPORT:				
Contributions	\$ 113,112	\$ 36,500		\$ 149,612
Grants	82,039	700,000		782,039
Fundraising Events, Net of Direct Costs	84,985			84,985
Special Appeals	16,172			16,172
Memberships	108,428			108,428
Santa Cruz County Contract	114,573			114,573
Interest Income	5,241	7,479		12,720
Museum Store Sales	4,191			4,191
Admissions	18,357			18,357
Program Service Fees	80,191			80,191
Facility Rental Income	51,272			51,272
Unrealized Gains & Losses on Investments	7,573	33,740		41,313
Net Assets Released from Restrictions	315,441	(315,441)		
Total Revenue and Other Support	<u>1,001,575</u>	<u>462,278</u>		<u>1,463,853</u>
OTHER GAINS:				
Rents McPherson Center	739,366			739,366
Interest Income McPherson Center Accounts	43			43
Expenses Related to Rents	(407,849)			(407,849)
Total Other Gains	<u>331,560</u>			<u>331,560</u>
EXPENSES:				
Program:				
Museum	1,006,308			1,006,308
Support Organizations	19,400			19,400
Supporting Services:				
Management and General	99,346			99,346
Development	68,313			68,313
Total Expenses	<u>1,193,367</u>			<u>1,193,367</u>
CHANGE IN NET ASSETS	139,768	462,278		602,046
NET ASSETS, Beginning of Year	<u>3,976,150</u>	<u>583,130</u>	<u>\$ 233,071</u>	<u>4,792,351</u>
NET ASSETS, End of Year	<u>\$ 4,115,918</u>	<u>\$ 1,045,408</u>	<u>\$ 233,071</u>	<u>\$ 5,394,397</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, 2014

CASH FLOWS FROM OPERATING ACTIVITIES:

Change in Net Assets	\$ 602,046
Adjustments to Reconcile Decrease in Net Assets to Net Cash Provided by Operating Activities:	
Depreciation and Amortization	231,175
Unrealized Loss on Investments	(41,313)
(Increase) Decrease in Operating Assets:	
Receivables	(405,389)
Other Assets	(276)
Inventory	(10,854)
Increase (Decrease) in Operating Liabilities:	
Accounts Payable	1,297
Accrued Personal Time Off	7,700
Accrued Interest	(3,905)
Deposits	<u>(1,475)</u>

CASH FLOWS PROVIDED BY OPERATING ACTIVITIES	<u>379,006</u>
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CASH FLOWS FROM FINANCING ACTIVITIES:

Purchase of Fixed Assets	(250,170)
Principal Payments on Capital Lease - Building	<u>(110,000)</u>

CASH FLOWS USED IN FINANCING ACTIVITIES	<u>(360,170)</u>
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INCREASE IN CASH AND CASH EQUIVALENTS	18,836
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CASH AND CASH EQUIVALENTS, Beginning of Year	<u>1,375,202</u>
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CASH AND CASH EQUIVALENTS, End of Year	<u><u>\$ 1,394,038</u></u>
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SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:

Interest Paid	<u><u>\$ 63,055</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, 2014

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, 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Basis of Accounting - The Organization follows standards of accounting and financial reporting prescribed for nonprofit organizations that include reporting on the accrual basis of accounting. Contributions are recognized when the donor makes a pledge to give that is in substance an unconditional promise.

Contributions - Contributions are accounted by the Organization in its financial position and operating activities in the following three classes of net assets:

Unrestricted Net Assets include those assets over which the Board of Directors has discretionary control in carrying out the operations of the Organization. Under this category, the Organization maintains an operating fund plus any net assets designated by the Board of Directors for specific purposes.

Temporarily Restricted Net Assets include those assets that are subject to a donor restriction and for which the applicable restriction was not met as of the end of the current reporting period. When the restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets.

Permanently Restricted Net Assets include those assets that are subject to a permanent donor restriction and for which only investment income earned by the funds can be used by the Organization.

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 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.

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 grants and contributions receivable related to the Organization's programs and rent and related charges due from tenants. All receivables are expected to be collected.

Investments - The Organization's investments are valued in accordance with generally accepted accounting principles in the United States, including Fair Value Measurements. As of June 30, 2014, the accounts treated as an investment are (1) Endowment Fund held in various ETF funds and (2) A fund held under a contract with the Community Foundation of Santa Cruz County. Gains and losses that result from market fluctuations are recognized in the period such fluctuations occur.

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

June 30, 2014

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

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 currently 5-7 years for office furniture and equipment and 15-40 years for building and building improvements.

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.

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 federal and state income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the Revenue and Taxation Code. The Organization is not considered a private foundation.

The Organization files tax returns with the federal government and the State of California. All returns have been filed by the initial or extended due dates. The Organization's federal and state income tax returns are subject to possible examination by the taxing authorities until the expiration of the related statutes of limitation for those returns.

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.

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.

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

June 30, 2014

3. 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, 2014, the Organization had \$858,377 in bank deposits in excess of the \$250,000 FDIC limits.

The Organization holds investment funds in various brokerage accounts with investments in mutual funds subject to market risk.

4. CONCENTRATION OF RISK:

The Organization is mainly dependent on membership revenue, donations and contributions from the community, grants from private foundations, and net rent revenue from its Office/Retail Building for its operations. The Organization receives 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. The Organization's rent income is concentrated in two major tenants as disclosed in Note 9.

5. ORIGINATION FEES:

Origination fees attributable to the Santa Cruz County capital lease note have been capitalized as part of the capital lease agreement (see Note 8). 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>(52,618)</u>
Loan Fee, Net	<u>\$ 12,382</u>

6. 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 8). The interest earned on that reserve reduces the interest paid on the Santa Cruz County Lease on an annual basis.

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

June 30, 2014

7. 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 8. 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.

8. CAPITAL LEASE PAYABLE:

Capital lease payable at June 30, 2014, 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.

\$1,189,156

Less: Current Portion

(115,000)
\$1,074,156

Minimum future lease payments are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>
2015	\$ 115,000
2016	125,000
2017	135,000
2018	145,000
2019	155,000
Thereafter	<u>514,156</u>
	<u>\$1,189,156</u>

Interest expense on the lease for fiscal year ended June 30, 2014 was \$59,150.

Subsequent to the final payment due on the capital lease agreement, the Organization will be required to make lease payments to the County of Santa Cruz as described in Note 15.

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

June 30, 2014

9. MAJOR TENANT:

As of June 30, 2014, 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	\$ 19,751	36%
Tenant B	19,524	36%
Various Other Tenants	<u>16,527</u>	<u>28%</u>
	<u>\$ 55,802</u>	<u>100%</u>

10. PROPERTY, EQUIPMENT, AND IMPROVEMENTS:

Details of Property Equipment and Improvements as of June 30, 2014, and related depreciation expense for the year then ended were as follows:

	<u>Museum</u>	<u>McPherson Center</u>	<u>Total</u>
Office Furniture and Equipment	\$ 41,142	\$ 920	\$ 42,062
Equipment	109,389	65,063	174,452
Museum Store	68,625		68,625
Leasehold Improvements	221,385	136,888	358,273
Evergreen Cemetery	70,925		70,925
Construction in Progress	61,500		61,500
Museum Building	3,655,269		3,655,269
McPherson Center Bldg.		<u>4,162,809</u>	<u>4,162,809</u>
	4,228,235	4,365,680	8,593,915
Less: Accumulated Depreciation	<u>(2,193,484)</u>	<u>(2,232,816)</u>	<u>(4,426,300)</u>
	<u>\$2,034,751</u>	<u>\$2,132,864</u>	<u>\$4,167,615</u>
Depreciation Expense	<u>\$ 112,302</u>	<u>\$ 116,397</u>	<u>\$ 228,699</u>

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

June 30, 2014

11. TEMPORARILY RESTRICTED NET ASSETS:

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

History Gallery Upgrade	\$ 134,696
Unrealized Gain on Investments	68,972
Other Temporarily Restricted Funds	39,633
New CA Art Funds	325,000
Renewed Ambition - Abbott Square	250,000
Renewed Ambition - Campaign Program and Other	<u>227,107</u>
Total Temporarily Restricted Net Assets	<u>\$ 1,045,408</u>

12. 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, 2014, 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.

13. FAIR VALUE MEASUREMENTS:

The Organization follows the provisions of the Fair Value Measurements and Disclosure topic of the FASB Accounting Standards Codification.

Fair Value Hierarchy

These standards establish a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. 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.

This hierarchy consists of three broad levels:

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

June 30, 2014

13. FAIR VALUE MEASUREMENTS (Continued):

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:

Investments (Endowment Fund) - Represents assets invested in a mix of funds in a brokerage account.

Funds held at Community Foundation of Santa Cruz County - Represents assets held by the Community Foundation in an investment pool (Long Term Portfolio).

The following table presents the Organization's fair value hierarchy for those assets measured at fair value as of June 30, 2014:

	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Endowment Fund - Exchange				
Traded Funds	\$ 295,135	\$295,135		
Endowment Fund - Money Market Fund	6,908	6,908		
Investment Held By Community Fdn.	53,021	53,021		

14. 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.

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, 2014

14. 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, 2014.

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.

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.

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

NOTES TO FINANCIAL STATEMENTS
(Continued)

June 30, 2014

14. ENDOWMENT FUND (Continued):

Endowment net asset composition by type of fund as of June 30, 2014 consisted of the following:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor Restricted Endowment Funds	\$ -	\$ 68,972	\$ 233,071	\$ 302,043

Changes in endowment net assets for the fiscal year ended June 30, 2014 consisted of the following:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment Net Assets, Beginning of Year		\$ 33,081	\$ 233,071	\$ 266,152
Contributions:				
Investment Income Including Market Appreciation		41,219	-	41,219
Distributions:				
To MAH		(5,328)	-	(5,328)
Endowment Net Assets, End of Year	\$ 0	\$ 68,972	\$ 233,071	\$ 302,043

15. FRONT STREET ANNEX LEASE:

The Organization leases certain real property that houses the commercial and professional space of the McPherson Center under an agreement with the County of Santa Cruz, Amendment No. 1 dated April 9, 2014. Under the agreement rental payments of 10% of gross rent are due on or before September 1 (10% of gross rent from January 1 to June 30) and March 1 (10% of gross rent from July 1 to December 31).

For any six month period for which a use payment has been made (defined as a payment on the capital lease described in Note 8) such use payment shall satisfy the rental payment obligation.

Rental payments, other than those to be satisfied by a use payment, will commence September 1, 2021.

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

June 30, 2014

16. UNRESTRICTED NET ASSETS:

As of the year ended June 30, 2014, the Board has the following designated funds:

Operating Reserve Fund - During fiscal year ended June 30, 2014, to establish an Operating Reserve Fund, the MAH Board of Directors designated \$100,000 of existing accumulated liquid net assets as the beginning balance of the Operating Reserve Fund. The goal is to add \$150,000 to the fund over the next six (6) fiscal years.

Facilities Reserve Fund - During fiscal year ended June 30, 2014 the MAH Board of Directors determined the need for a Facilities Reserve Fund and created a policy for funding. The Facility Reserve Fund will be funded with the net surplus of funds from the McPherson Center Office Building in excess of \$216,000.

Publications Fund -The Organization has a Publications Fund for the purpose of setting aside funds for future publications.

Spendable Net Assets:

Total Unrestricted Net Assets at June 30, 2014	\$ 4,115,918
Less Non-Spendable Net Assets:	
Invested in Property, Plant & Equipment	
Net of Accumulated Depreciation and Debt	(2,978,459)
Invested in Inventories	(59,027)
Invested in Other Long Term Assets	<u>(241,403)</u>
Spendable Net Assets	837,029
Board Designated Unrestricted Net Assets:	
Operating Reserve	(100,000)
Publications Fund	<u>(26,346)</u>
Undesignated Unrestricted Spendable Net Assets	<u>\$ 710,683</u>

17. SUBSEQUENT EVENTS:

The Organization's management has evaluated events and transactions subsequent to June 30, 2014, 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, 2014. Subsequent events have been evaluated through October 13, 2014, the date the financial statements became available to be issued. The entity has not evaluated subsequent events after October 13, 2014.

SUPPLEMENTARY INFORMATION

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

June 30, 2014

	ASSETS			
	Museum	Supporting Organizations	McPherson Center	Total
CURRENT ASSETS:				
Cash and Cash Equivalents	\$ 752,832	\$ 28,190	\$ 126,580	\$ 907,602
Accounts Receivable	6,050		11,512	17,562
Other Assets	10,977		3,761	14,738
Inventories	59,027			59,027
Total Current Assets	828,886	28,190	141,853	998,929
PROPERTY, EQUIPMENT AND IMPROVEMENTS, NET	2,034,751		2,132,864	4,167,615
OTHER ASSETS:				
Funds Held by Community Foundation	53,021			53,021
Origination Fee, Net of Amortization	12,382			12,382
Lease Reserve	176,000			176,000
Total Other Assets	241,403		0	241,403
TOTAL ASSETS	\$ 3,105,040	\$ 28,190	\$ 2,274,717	\$ 5,407,947

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 FINANCIAL POSITION -
UNRESTRICTED FUNDS
(Continued)

June 30, 2014

LIABILITIES AND NET ASSETS

	<u>Museum</u>	<u>Supporting Organizations</u>	<u>McPherson Center</u>	<u>Total</u>
CURRENT LIABILITIES:				
Current Portion Capital Lease	\$ 115,000			\$ 115,000
Accrued Interest	29,575			29,575
Accounts Payable	15,365		\$ 6,034	21,399
Tenant and Facilities Rental Deposits	8,525		14,050	22,575
Accrued Personal Time Off	29,324			29,324
Total Current Liabilities	<u>197,789</u>		<u>20,084</u>	<u>217,873</u>
NON-CURRENT LIABILITIES:				
Capital Lease Payable	<u>1,074,156</u>			<u>1,074,156</u>
Total Non-Current Liabilities	<u>1,074,156</u>		<u>0</u>	<u>1,074,156</u>
NET ASSETS, UNRESTRICTED	<u>1,833,095</u>	<u>\$ 28,190</u>	<u>2,254,633</u>	<u>4,115,918</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 3,105,040</u>	<u>\$ 28,190</u>	<u>\$ 2,274,717</u>	<u>\$ 5,407,947</u>

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

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

SCHEDULE OF ACTIVITIES AND CHANGES IN NET ASSETS -
UNRESTRICTED FUNDS

For the Year Ended June 30, 2014

	<u>Museum</u>	<u>Supporting Organizations</u>	<u>McPherson Center</u>	<u>Total</u>
REVENUE AND OTHER SUPPORT:				
Contributions	\$ 113,112			\$ 113,112
Foundation and Business Grants	82,039			82,039
Special Events Fundraising (Net of Expenses)	77,113	\$ 7,872		84,985
Special Appeals	16,172			16,172
Memberships	91,508	16,920		108,428
Santa Cruz County Contract	114,573			114,573
Interest Income	5,229	12		5,241
Other Income	0			0
Museum Store Sales	4,191			4,191
Admissions	18,357			18,357
Program Service Fees	80,191			80,191
Facility Rental Income	51,272			51,272
Unrealized Gains	7,573			7,573
Net Assets Released from Restrictions	315,441			315,441
	<u>976,771</u>	<u>24,804</u>	<u>0</u>	<u>1,001,575</u>
TOTAL REVENUE AND OTHER SUPPORT				
	<u>976,771</u>	<u>24,804</u>	<u>0</u>	<u>1,001,575</u>
OTHER GAINS:				
Rent and Assessments McPherson Center			\$ 739,366	739,366
Interest Income McPherson Center Accounts			43	43
Expenses Related to Rents			<u>(407,849)</u>	<u>(407,849)</u>
			<u>331,560</u>	<u>331,560</u>
TOTAL OTHER GAINS				

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

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, 2014

	<u>Museum</u>	<u>Supporting Organizations</u>	<u>McPherson Center</u>	<u>Total</u>
EXPENSES:				
Program:				
Museum	\$ 1,006,308	\$ 19,400		\$ 1,025,708
Supporting Services:				
Management and General	99,346			99,346
Development	68,313			68,313
Total Expenses	<u>1,173,967</u>	<u>19,400</u>	<u>0</u>	<u>1,193,367</u>
REVENUE & SUPPORT OVER EXPENSES	(197,196)	5,404	\$ 331,560	139,768
OPERATING TRANSFERS IN (OUT)	<u>389,055</u>		<u>(389,055)</u>	<u>-</u>
CHANGE IN NET ASSETS	191,859	5,404	(57,495)	139,768
NET ASSETS, BEGINNING OF YEAR	<u>1,641,236</u>	<u>22,786</u>	<u>2,312,128</u>	<u>3,976,150</u>
NET ASSETS, END OF YEAR	<u><u>\$ 1,833,095</u></u>	<u><u>\$ 28,190</u></u>	<u><u>\$ 2,254,633</u></u>	<u><u>\$ 4,115,918</u></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, 2014

		Program Service	Management & General	Development	Total
EXPENSES:					
5100	Salary/Wages	\$ 417,480	\$ 59,043	\$ 45,980	\$ 522,503
5101	Payroll Service	1,721	243	190	2,154
5105	Benefits	45,426	6,424	5,003	56,853
5110	Payroll Taxes	38,660	5,468	4,257	48,385
5115	Auto/Mileage	945	-	-	945
5125	Printing	3,597	-	33	3,630
5126	Stationery	908	128	100	1,136
5129	Credit Card Fees	-	-	-	-
5131	Major Donors	-	-	1,037	1,037
5135	Dues	368	-	-	368
5143	Staff	5,272	746	580	6,598
5145	Equipment Lease	2,224	315	245	2,784
5155	Postage	5,365	424	942	6,731
5165	Office Supplies	5,754	813	634	7,201
5170	Taxes & Licenses	1,162	130	-	1,292
5175	Telephone	3,872	548	426	4,846
5185	Volunteer Expense	3,109	-	-	3,109
5190	Auditing Fee	-	12,518	-	12,518
5195	Maintenance	10,350	106	106	10,562
5200	Computer Expense	6,749	954	743	8,446
5205	Bank Service Charges	-	3,449	-	3,449
5210	Other Professional Service	57,106	-	-	57,106
5212	Professional Services	-	-	-	-
5215	Graphics	5,852	-	-	5,852
5230	Member Receptions Expense	11,392	-	-	11,392
5256	Curatorial Fees	41,190	-	-	41,190
5257	Crating and Materials	-	-	-	-
5260	Installation Exhibition	26,218	-	-	26,218
5265	Permanent Collection Expense	863	-	-	863
5270	Exhibition Shipping	6,004	-	-	6,004
5280	Exhibit Insurance Expense	-	-	-	-

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, 2014

		Program Service	Management & General	Development	Total
EXPENSES:					
5306	Public Programs Expense	\$ 29,199	\$ -	\$ -	\$ 29,199
5310	Gallery Activities	2,527	-	-	2,527
5311	School Programs	2,038	-	-	2,038
5315	Trunks Expense	232	-	-	232
5319	Hawley Classroom	-	-	-	-
5320	Evergreen Programs	3,199	-	-	3,199
5321	Docent Education	966	-	-	966
5324	Evergreen Cemetery-Maintenance	2,924	-	-	2,924
5331	Blue Plaque Expense	1,446	-	-	1,446
5360	Promotion	6,947	-	-	6,947
5370	Interest	47,320	5,915	5,915	59,150
5380	Fire/Security	1,582	16	16	1,614
5385	Insurance	14,205	145	145	14,495
5390	Janitorial/Landscaping	14,850	152	152	15,154
5400	PG&E	41,309	422	421	42,152
5405	Parking Deficiency Fund	9,580	97	98	9,775
5410	Repair/Replacement	10,249	105	105	10,459
5415	Utility - Other	3,666	37	37	3,740
5420	Depreciation and Amortization Expense	112,482	1,148	1,148	114,778
5590	Other Expense	-	-	-	-
		<u>\$ 1,006,308</u>	<u>\$ 99,346</u>	<u>\$ 68,313</u>	<u>\$ 1,173,967</u>
McPherson Center Expenses:					
	Depreciation and Amortization	\$ 116,397			\$ 116,397
	McPherson Center Operating Expense	291,452			291,452
		<u>\$ 407,849</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 407,849</u>

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