

***Museum of  
Contemporary Art  
San Diego***

*Financial Statements as of and for the Year  
Ended June 30, 2012 (With Comparative  
Summarized Financial Information for the Year  
Ended June 30, 2011), Independent Auditors'  
Report, and Supplemental Schedule for the Year  
Ended June 30, 2012*

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
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## **INDEPENDENT AUDITORS' REPORT**

To the Audit Committee of  
**Museum of Contemporary Art San Diego**

We have audited the accompanying statement of financial position of the **Museum of Contemporary Art San Diego** (the "Museum") as of June 30, 2012, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the Museum's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior-year comparative summarized financial information has been derived from the Museum's 2011 financial statements and in our report dated October 26, 2011, we expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Museum at 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.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule of functional expenses on page 21 is presented for the purpose of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of the Museum's 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 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 taken as a whole.

*Mayer Hoffman McCann P.C.*

November 8, 2012

# MUSEUM OF CONTEMPORARY ART SAN DIEGO

## STATEMENT OF FINANCIAL POSITION FOR THE YEAR ENDED JUNE 30, 2012

(With Comparative Summarized Financial Information for the Year Ended June 30, 2011)

<b>ASSETS</b>	<b>2012</b>	<b>2011</b>
Current Assets:		
Cash and cash equivalents	\$ 1,296,104	\$ 1,703,528
Unrestricted investments	2,009,074	-
Accounts receivable	43,169	54,718
Pledges and grants receivable - current portion	680,989	1,329,488
Inventory	359,115	396,835
Prepaid expenses and other assets	141,081	253,393
Total current assets	4,529,532	3,737,962
Non-Current Assets:		
Pledges and grants receivable - long-term portion	1,887,593	2,179,302
Notes receivable from officers	7,761	758,716
Property and equipment - net	34,689,449	35,629,964
Restricted cash and investments	32,737,825	37,949,238
Deferred financing costs - net	343,491	358,871
Other assets	112,219	122,907
	\$ 74,307,870	\$ 80,736,960
<b>LIABILITIES AND NET ASSETS</b>		
Current Liabilities:		
Accounts payable and accrued expenses	\$ 649,367	\$ 711,086
Deferred revenue - current portion	669,996	815,373
Deferred rent - current portion	27,090	28,675
Current portion of long-term debt	-	864,854
Total current liabilities	1,346,453	2,419,988
Non-Current Liabilities:		
Deferred compensation	356,327	268,926
Deferred revenue - long-term portion	781,428	791,587
Deferred rent - long-term portion	81,250	106,250
Long-term debt	6,950,000	9,350,000
Total liabilities	9,515,458	12,936,751
Net Assets:		
Unrestricted	17,788,855	19,492,230
Temporarily restricted	7,261,344	8,702,097
Permanently restricted	39,742,213	39,605,882
Total net assets	64,792,412	67,800,209
	\$ 74,307,870	\$ 80,736,960

# MUSEUM OF CONTEMPORARY ART SAN DIEGO

## STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2012

(With Comparative Summarized Financial Information for the Year Ended June 30, 2011)

	Unrestricted	Temporarily Restricted	Permanently Restricted	2012	2011
<b>SUPPORT AND REVENUES:</b>					
<b>SUPPORT:</b>					
Contributions	\$ 1,480,102	\$ 954,304	\$ 136,331	\$ 2,570,737	\$ 2,612,036
City and County of San Diego grants	281,734	45,000	-	326,734	463,351
State and federal grants	30,000	-	-	30,000	211
Net assets released from restrictions	2,461,559	(2,461,559)	-	-	-
Total support	4,253,395	(1,462,255)	136,331	2,927,471	3,075,598
<b>REVENUES:</b>					
Unrealized gain/(loss) on investments	(397,044)	(33,632)	-	(430,676)	1,839,267
Special events	2,268,525	-	-	2,268,525	581,923
Dividend and interest income	808,578	48,731	-	857,309	693,430
Realized gain/(loss) on investments	64,474	6,403	-	70,877	5,493,991
Membership	535,377	-	-	535,377	570,575
Auditorium/Museum space rental	477,878	-	-	477,878	479,545
Museum beverage service	264,527	-	-	264,527	254,318
Admission fees	173,212	-	-	173,212	184,186
Museum store sales	196,233	-	-	196,233	187,000
Touring exhibit fees	7,582	-	-	7,582	77,748
Other income	194,809	-	-	194,809	193,160
Publication sales	33,541	-	-	33,541	15,608
Educational programs and lectures	22,077	-	-	22,077	27,415
Total revenues	4,649,769	21,502	-	4,671,271	10,598,166
Total support and revenues	8,903,164	(1,440,753)	136,331	7,598,742	13,673,764
<b>EXPENSES:</b>					
<b>Program services:</b>					
Exhibitions	2,658,888	-	-	2,658,888	2,534,983
Permanent collection, circulation and accession	1,498,576	-	-	1,498,576	1,322,361
Auditorium	704,050	-	-	704,050	646,076
Curatorial	527,408	-	-	527,408	572,175
Membership support	432,926	-	-	432,926	596,238
Education, performances and library	370,365	-	-	370,365	456,305
Museum stores	245,106	-	-	245,106	230,577
Publications	135,310	-	-	135,310	90,741
Total program services	6,572,629	-	-	6,572,629	6,449,456
<b>Supporting services:</b>					
General and administrative	1,821,145	-	-	1,821,145	1,898,897
Special events	1,199,259	-	-	1,199,259	258,128
Public relations and marketing	455,216	-	-	455,216	467,186
Development	360,761	-	-	360,761	315,365
Museum beverage service	197,529	-	-	197,529	201,106
Total supporting services	4,033,910	-	-	4,033,910	3,140,682
Total expenses	10,606,539	-	-	10,606,539	9,590,138
CHANGE IN NET ASSETS	(1,703,375)	(1,440,753)	136,331	(3,007,797)	4,083,626
NET ASSETS - Beginning of year	19,492,230	8,702,097	39,605,882	67,800,209	63,716,583
NET ASSETS - End of year	\$ 17,788,855	\$ 7,261,344	\$ 39,742,213	\$ 64,792,412	\$ 67,800,209

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

# MUSEUM OF CONTEMPORARY ART SAN DIEGO

## STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED JUNE 30, 2012

(With Comparative Summarized Financial Information for the Year Ended June 30, 2011)

	2012	2011
Cash Flows From Operating Activities:		
Change in net assets	\$ (3,007,797)	\$ 4,083,626
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Net realized and unrealized (gain)/loss on investments	359,798	(7,333,259)
Depreciation and amortization	1,113,263	1,122,850
Contributions of stock and securities	(328,533)	(326,491)
Forgiveness of notes receivable from officers	79,325	89,700
Contribution restricted for long term-investments	(136,331)	-
Loss on equipment disposal	2,517	-
Changes in assets and liabilities:		
Accounts receivable	11,549	17,903
Pledges and grants receivable	940,208	1,532,659
Inventory	37,720	1,820
Prepaid expenses and other assets	123,000	(79,384)
Accounts payable and accrued expenses	(61,719)	(792)
Deferred revenue	(155,536)	41,269
Deferred rent	(26,585)	(23,762)
Deferred compensation	87,401	29,263
Net cash used in operating activities	<u>(961,720)</u>	<u>(844,598)</u>
Cash Flows From Investing Activities:		
Proceeds from sales of investments	21,471,838	29,654,289
Purchases of investments	(18,300,764)	(29,123,810)
Purchases of property and equipment	(159,885)	(161,154)
Payments received on notes receivable from officers	318,769	18,569
Net cash provided by investing activities	<u>3,329,958</u>	<u>387,894</u>
Cash Flows From Financing Activities:		
Principal payments on long-term debt	(2,911,993)	(15,183)
Contributions restricted for long-term investments	136,331	-
Net cash used in financing activities	<u>(2,775,662)</u>	<u>(15,183)</u>
Net Change in Cash and Cash Equivalents	<u>(407,424)</u>	<u>(471,887)</u>
Cash and Cash Equivalents - Beginning of year	<u>1,703,528</u>	<u>2,175,415</u>
Cash and Cash Equivalents - End of year	<u>\$ 1,296,104</u>	<u>\$ 1,703,528</u>
Supplemental Disclosure of Cash Flow Information		
Long-term debt paid from Note Receivable payoff	\$ 352,861	\$ -
Cash paid for interest	\$ 60,078	\$ 268,263

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

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Nature of Activities* - The **Museum of Contemporary Art San Diego** (the "Museum") - one museum with three distinct, complementary locations in San Diego and La Jolla, California - is a visual arts institution with an international constituency. The Museum aims to culturally enrich the lives of residents and visitors from around the world with collections, exhibitions and programs that focus on the art and artists of our time. The general purposes of the Museum are to acquire, exhibit and preserve works of art created since 1950 for the benefit of future generations, to foster the work of living artists and to promote an awareness and appreciation of the value of emerging artistic creativity through an active education program for adults and young people, to present and interpret significant developments in contemporary art, and to offer the public broad, balanced perspectives on contemporary art. The Museum's programs are supported primarily by contributions and investment returns.

*Basis of Presentation* - The financial statements are presented in accordance with the authoritative guidance related to not-for-profit entities. The authoritative guidance requires that net assets, revenue, gains, expenses, and losses be classified as unrestricted, temporarily restricted, and permanently restricted. The Museum distinguishes between contributions that are unrestricted and those that contain donor-imposed restrictions. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Donor-restricted contributions whose restrictions are met in the same reporting period are reported as unrestricted contributions.

Contributions of goods are recognized in the financial statements if the goods received (a) create or enhance non-financial assets, or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. The Museum reports such contributions at their estimated fair value when received. Included in unrestricted contributions and related expenses for 2012, is approximately \$795,000 of contributed goods and services.

Contributions of long-lived assets with explicit restrictions that specify how the assets are to be used and other assets that must be used to acquire long-lived assets are reported as temporarily restricted contributions. Absent explicit donor stipulation about how long these long-lived assets must be maintained, the Museum reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

Net assets and revenues, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Museum and changes therein are classified and reported as follows:

*Unrestricted Net Assets* – All net assets that are not subject to donor-imposed restrictions are reported as unrestricted net assets.

*Temporarily Restricted Net Assets* – Temporarily restricted net assets include gifts for which donor-imposed restrictions have not been met and funds for which the ultimate purpose of the proceeds is not permanently restricted. Temporarily restricted net assets are restricted primarily for exhibitions, the acquisition of art works, capital expansion, and time.

*Permanently Restricted Net Assets* – Permanently restricted net assets include gifts which require by donor-imposed restrictions that the corpus is invested in perpetuity and only the investment income be made available for the Museum's operations in accordance with donor restrictions, if any.

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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**Grants** - City and County of San Diego grants and other grants are recognized as permanently restricted, temporarily restricted, or unrestricted support, depending on the stipulations of the grant agreements. When a grant restriction expires, stipulated time restrictions end or purpose restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities as net assets released from restrictions. Grants whose restrictions are met in the same reporting period are reported as unrestricted support.

**Pledges and Grants Receivable** - Unconditional promises to give are recorded as pledges receivables, and revenues in the period received. Pledges receivable consist of unconditional promises to give. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. Discounts to present value are computed using risk adjusted rates applicable in the years in which those promises are received. Risk adjusted interest rates ranged from approximately 0.51% to 2.7% per annum.

Amortizations of the discounts are included in contributions. Conditional promises to give are not recorded as contributed income until the conditions are substantially met.

**Cash Equivalents** - For financial statement purposes, the Museum considers all highly liquid unrestricted investments with a maturity of three months or less when purchased to be cash equivalents.

**Investments** - Investments are accounted for in accordance with the authoritative guidance. Under the provisions of the authoritative guidance, investments in equity securities with readily determinable fair market values and all debt securities should be reported at fair market value with gains and losses included in the statement of activities. Realized gains or losses recognized on the sale of securities are based upon the original cost of the security, as determined by the specific identification method. Unrealized gains and losses represent the change in the fair market value of the individual investments for the year or since the acquisition date if acquired during the year and are recorded in the statement of activities as part of current-year operations.

Investments consisted of U.S. government securities and other debt and equity securities and are recorded at fair market value. The fair value of investments in securities traded on national security exchanges are valued at the closing price on the last business day of the fiscal year. Securities are generally held in custodial investment accounts administered by certain financial institutions.

Investments are made according to the Investment Policy Statement adopted by the Museum's Board of Trustees. These guidelines provide for investments in equities, fixed income, and other securities with performance measured against appropriate indices. Outside parties are contracted by the Museum for the purpose of providing investment management and consulting.

**Property and Equipment** - Property and equipment is stated at cost or, in the case of donated property and equipment, at fair value at the date of gift, less accumulated depreciation. Depreciation is provided for using the straight-line method over the estimated useful lives of the assets, which is 50 years for buildings, the lesser of the useful life or the lease term for leasehold improvements, and 3 to 10 years for furniture and equipment. The Museum capitalizes acquisitions of property and equipment meeting specified criteria, in excess of \$1,000 and with a minimum useful life of three years.

**Collections** - The permanent collection of the Museum consists of paintings, sculpture, installations, works on paper (including photography), video, and other media.



**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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The cornerstone of any museum is its collection. It is the responsibility of the Museum to acquire objects for its collection, to maintain them for use in exhibitions, education and research, and to preserve the collection in perpetuity. Acquisition and preservation of objects are primary responsibilities of the Board of Trustees, the executive director and the curatorial staff.

The collections, which were acquired through purchases and contributions since the Museum's inception, are not recognized as assets on the statement of financial position. Purchases of collection items are recorded as decreases in unrestricted net assets in the year in which the items are acquired. Contributed collection items are not reflected on the financial statements. Proceeds from deaccessions or insurance recoveries are reflected as increases in the appropriate net asset classes.

**Charitable Remainder Trusts** - The Museum is a beneficiary of certain trust funds held by others and has recorded an asset for the net present value of the estimated future amount to be received from such trusts. Charitable remainder trusts are trusts established in connection with a split-interest agreement, in which the donor or a third-party beneficiary receives specified distributions during the agreement's term. Upon termination of the trust, the Museum receives the assets remaining in the trust. The present values are calculated by using recent life expectancy tables and risk adjusted discount rates of between 1.08% and 2.65% as of June 30, 2012. The Museum did not receive any new charitable trusts during 2012. During 2012, the present value of the expected future benefit to the Museum of these assets increased by approximately \$83,000. At June 30, 2012, these assets were valued at approximately \$771,000 and are included in pledges and grants receivable on the statement of financial position.

**Inventory** - Inventory, consisting primarily of merchandise held for sale in the Museum's stores, is carried at the lower of cost, determined principally on a first-in, first-out basis, or market.

**Other Assets** - In December 2008, the Museum purchased a Type 47 Liquor License and established a DBA called Museum Beverage Services. Total costs related to the purchase equaled approximately \$102,000 and consisted of legal, escrow fees, and miscellaneous other costs. These costs were capitalized in accordance with the authoritative guidance and are included in long term other assets.

The useful life of an intangible asset is the period over which the asset is expected to contribute directly or indirectly to the future cash flows of the owner. As Management has determined that the license has an indefinite life, the Museum has not amortized the license. The Museum will perform an impairment analysis, as well as evaluate the useful life on an annual basis to determine whether events and circumstances continue to support an indefinite useful life and the carrying amount. There was no impairment as of June 30, 2012.

**Deferred Revenue** - Deferred revenue represents amounts collected in advance for exhibitions, membership fees, special events, and rental income. Such amounts are recognized as revenue in the period in which they are earned.

**Deferred Rent** - Rent expense is recorded on a straight-line basis over the term of the lease. The difference between rent expense and the amounts paid under the lease agreements is recorded as deferred rent and is included as a liability in the accompanying statements of financial position.

**Income Taxes** - The Museum is a not-for-profit organization and is exempt from federal and California income taxes under Section 501(c)(3) of the Internal Revenue Code and applicable state statutes. The Museum, however, may be subject to tax on income which is not related to its exempt purpose. The Museum had no unrelated business income tax for the year ended June 30, 2012.

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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At June 30, 2012, the federal statute of limitation remains open for the 2008 through 2012 years. The statute of limitations for the state income tax returns remains open for the 2007 through 2012 years.

**Use of Estimates** - The preparation of financial statements in conformity with U.S. 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 statement of financial position and the reported amounts of revenues and expenses during years presented. Actual results could differ from those estimates. Significant estimates used in preparing these financial statements include those assumed in computing the estimated future cash flow of charitable remainder trusts, pledges and grants receivables, and deferred liability calculations.

**Credit Risk** - The Museum invests in various types of marketable securities and money market funds, and has established guidelines relative to diversification and maturities that target certain safety and liquidity risk levels. These guidelines are periodically reviewed and modified to take advantage of trends in yields and interest rates.

The Museum invests in various investment securities, including U.S. government securities, corporate debt instruments, and corporate stocks. Investment securities, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the financial statements.

The Museum maintains cash balances at banks located in San Diego. Accounts at these institutions are secured up to the Federal Deposit Insurance Corporation limits. At times, balances may exceed federally insured limits. The Museum has not experienced any losses in such accounts. Management believes that the Museum is not exposed to any significant credit risk with respect to its cash and cash equivalents.

**Fair Value Measurements** - Authoritative guidance establishes a common definition for fair value to be applied to generally accepted accounting principles in the United States requiring use of fair value, establishes a framework of measuring fair value, and expands disclosures about such fair value measurements.

Fair value is defined as the hypothetical price (excluding transaction costs) that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value shall be determined based on the assumptions that market participants would use in pricing the asset or liability.

**Endowment Net Assets** - Authoritative guidance provides direction on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (“UPMIFA”). The State of California approved a version of UPMIFA in September 2008 with an effective date of January 1, 2009.

**Prior Year Information** - The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Museum’s audited financial statements for the year ended June 30, 2011, from which the summarized information was derived.

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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**2. INVESTMENTS**

Investments are carried at fair value based on quoted market prices and at June 30, 2012, consisted of the following:

Equity securities	\$ 27,358,749
Fixed income securities	7,388,150
	<u>\$ 34,746,899</u>

The Museum's investment activities for 2012 resulted in dividend and interest income of approximately \$857,000, net realized and unrealized loss on investments of approximately \$360,000 and total fees of approximately \$193,000.

**3. PLEDGES AND GRANTS RECEIVABLE**

As of June 30, 2012, the Museum has unconditional pledges and grants receivable which are due as follows:

Within one year	\$ 680,989
One to five years	791,167
Greater than five years	2,442,821
	<u>\$ 3,914,977</u>

Based on its history of collections and an assessment of existing receivables, management of the Museum believes that no allowance for doubtful pledges, grants, and other receivables is necessary at June 30, 2012. Pledges receivable from related parties totaled approximately \$1,349,000 at June 30, 2012.

**4. PROPERTY AND EQUIPMENT**

Property and equipment consisted of the following at June 30, 2012:

Buildings and leasehold improvements	\$ 35,375,632
Furniture and equipment	4,890,920
	<u>40,266,552</u>
Less accumulated depreciation	<u>(13,043,655)</u>
	27,222,897
Land	<u>7,466,552</u>
Property and equipment - net	<u>\$ 34,689,449</u>

Depreciation expense was approximately \$1,098,000 for 2012.

In July 2004, an unrelated party transferred title for land and a building for a third location to the Museum, the fair value of which was estimated to be \$6,771,000. In connection with the transfer, the Museum granted

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**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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the City of San Diego an option to acquire the land and building on or after July 31, 2091, or prior to that date if the Museum commits a default under the related transfer agreement.

Default includes failure to perform any substantive covenant, condition, or obligation of the Museum under the transfer agreement, including continuous operation of the property as a contemporary art museum.

**5. NOTES RECEIVABLE FROM OFFICERS**

At June 30, 2012, the Museum had a promissory note receivable from its CEO/executive director that had a balance of approximately \$8,000. The note provides for monthly payments of interest at a rate of 4.22% per annum with the principal due on the earlier of one year after the CEO/executive director's separation, the expiration of his current term of employment or in August 2020. The note is collateralized by a first trust deed on real property located in La Jolla, California. The Museum forgave approximately \$58,000 of the amount due under the note agreement in 2012, of which approximately \$50,000 related to principal and approximately \$8,000 to interest. Approximately \$353,000 in payments were received in 2012. The amounts forgiven have been included in general and administrative expenses.

Additionally, the Museum had a promissory note receivable from its CFO/deputy director which was paid off by the CFO/deputy director during the fiscal year. The note provided for monthly payments of principal and interest at a rate of 4.22% per annum, with final payment due in October 2020. The note was collateralized by a first trust deed on real property located in La Jolla, California. The Museum forgave approximately \$43,000 of the amount due under this note agreement in 2012, of which approximately \$30,000 related to principal and approximately \$13,000 to interest and has included this amount in general and administrative expenses. Approximately \$319,000 in payments were received in 2012.

**6. DEBT**

*Line of Credit* - The Museum has a line of credit agreement with a bank expiring in January 2013 that provides for borrowings up to \$1,000,000 at any one time at an interest rate of 3.25% per annum at June 30, 2012. The line of credit agreement is uncollateralized. At June 30, 2012, there was no outstanding balance under this agreement. There were draws and repayments of \$1,105,000 on the line during the fiscal year.

*Long-Term Debt* - In February 2012, the Museum refinanced a \$460,000 note with interest at 3.25% per annum. The note payable was paid in full in June 2012. The note was collateralized by the note receivable from the CEO/executive director, as well as the first trust deed on real property located in La Jolla, California, which serves as collateral for that note. The loan agreement included certain covenants, including a restriction on the Museum incurring additional indebtedness. The Museum was in compliance with these requirements as of June 30, 2012.

In December 2004, the Museum borrowed \$13,000,000 through the issuance of tax-exempt variable rate demand certificates of participation (the "Bonds") issued by the County of San Diego. The Bonds bear interest at a weekly interest rate determined by Westhoff, Cone & Holmstedt (the "Remarketing Agent"), which was 0.18% per annum at June 30, 2012. The next scheduled payment is November 1, 2017.

The Bonds mature on November 1, 2034, subject to prior redemption, and are secured by a \$9,750,000 (the "Stated Amount") irrevocable, direct-pay letter of credit (the "LC") issued by Northern Trust Bank (the

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**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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“Bank”) for the Museum, in the favor of the bondholders, which expires on February 3, 2016, unless extended. The Museum is required to have a letter of credit related to the Bonds through the maturity date.

The Museum pays to the Bank a LC fee based on a leverage ratio calculation. At June 30, 2012, the LC fee was equal to 0.75% per annum of the stated amount of the LC. LC fees are paid quarterly in advance, which commenced on February 2, 2011.

Furthermore, according to the terms of the LC the Museum has provided the Bank with a perfected first priority lien and security interest in the gross revenues of the Museum and each account in which the gross revenues are deposited.

The Museum must satisfy certain contractual covenants related to the Bonds that include, among others, meeting an annual liquidity requirement, maintaining its tax-exempt status under Section 501(c)(3) of the Internal Revenue Code, limiting capital expenditures and additional debt, and meeting annual financial reporting and audit requirements. The Museum was in compliance with these requirements as of June 30, 2012.

The proceeds of the Bonds were applied to the financing of the acquisition, construction, installation, improvement, renovation, furnishing, and equipping of new Museum galleries and other related facilities associated with the expansion project (collectively, “the Project”) in San Diego. The Project included renovating the historic Santa Fe Depot “baggage building” and constructing a new three-story contemporary structure.

In connection with the issuance of the Bonds, the Museum incurred approximately \$460,000 of certain directly related issuance expenses, which have been capitalized as debt issuance costs. These deferred financing costs are being amortized to interest cost over the life of the Bonds. Amortization of approximately \$15,000 was recognized in 2012.

Future minimum principal payments related to the bank loan and to the bonds are as follows:

<b>Years Ending June 30,</b>	
2013	\$ -
2014	-
2015	-
2016	-
2017	-
Thereafter	<u>6,950,000</u>
	6,950,000
Less current portion	<u>-</u>
	<u><u>\$ 6,950,000</u></u>

**7. FAIR VALUE MEASUREMENTS**

Authoritative guidance establishes a hierarchy for ranking the quality and reliability of the input information used to determine fair values, requiring that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
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Level 1: Unadjusted quoted market prices in active markets for identical assets or liabilities.

Level 2: Unadjusted quoted prices in active markets for similar assets or liabilities, unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, or inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3: Significant unobservable inputs for the asset or liability.

The following disclosures provide the fair value of financial instruments at June 30, 2012:

	<u>(Level 1)</u>	<u>(Level 2)</u>	<u>(Level 3)</u>	<u>Total</u>
Charitable Remainder Trusts	\$ -	\$ -	770,613	770,613
Common Stock Funds:				
Domestic:				
Large Cap	12,861,508	-	-	12,861,508
Mid Cap	1,337,799	-	-	1,337,799
Small Cap	1,362,070	-	-	1,362,070
International:				
International Developed	6,571,786	-	-	6,571,786
Emerging Markets	3,857,524	-	-	3,857,524
Fixed Income Funds:				
Government Agencies	6,341,454	-	-	6,341,454
Corporate Bond Funds	1,046,696	-	-	1,046,696
	<u>\$ 33,378,837</u>	<u>\$ -</u>	<u>\$ 770,613</u>	<u>\$ 34,149,450</u>

See Note 1 for a discussion of the fair value measurements of these assets.

For assets and liabilities measured at fair value on a recurring basis using Level 3 inputs during the year, authoritative guidance requires a reconciliation of the beginning and ending balances for each major category as follows:

	<u>Charitable Remainder Trusts</u>
Balance July 1, 2011	\$ 687,575
Unrealized gain	83,038
Balance June 30, 2012	<u>\$ 770,613</u>

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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**8. ENDOWMENT NET ASSETS**

In August 2008, the Financial Accounting Standards Board (“FASB”) issued authoritative guidance for endowments which provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (“UPMIFA”). The State of California approved a version of UPMIFA in September 2008, effective January 1, 2009.

Authoritative guidance requires the Museum to classify a portion of a donor-restricted endowment fund of perpetual duration as permanently restricted net assets. Specifically, the portion classified as permanently restricted shall be (a) the amount of the fund that must be retained permanently per explicit donor stipulations or (b) in the absence of such stipulations, the amount which the Museum’s governing board determines must be retained (preserved) permanently consistent with UPMIFA.

Authoritative guidance requires affirmation that the amount that is classified as permanently restricted net assets is not reduced by losses on investments of the fund or by the Museum’s appropriations from the fund unless required by the donor. Furthermore, the portion of the fund that is not classified as permanently restricted net assets must be classified as temporarily restricted net assets until appropriated for expenditure by the Museum. Such appropriation is deemed to occur upon the Museum’s governing board’s approval of expenditures in the current period. Once the appropriation for expenditure has occurred, the appropriated amount is reclassified to unrestricted net assets.

UPMIFA states that, absent explicit donor instructions to the contrary, assets in an endowment fund are donor-restricted assets until appropriated by the Museum. The Museum interprets this to mean that all earnings on a donor-restricted endowment gift are restricted assets. As such, in accordance with the authoritative guidance, such earnings are classified as temporarily restricted net assets (time restricted) until appropriated by the Museum.

UPMIFA became effective in California for endowment funds existing on or established after January 1, 2009. The law defines an endowment fund to mean an institutional fund (excluding assets that an institution designates as an endowment fund for its own use) that, under the terms of a gift instrument, is not wholly expendable by the institution on a current basis. The law establishes various factors for the Museum to consider in the management and investment of endowment funds, as well as various factors for the Museum to consider in its determination as to whether to appropriate or accumulate the endowment funds.

Upon adoption of UPMIFA the Museum interpreted the corpus of invested permanently restricted funds to be approximately \$39,058,000. The Museum considers the value of an endowment gift to be considered for appropriation under UPMIFA to be equal to the sum of the original gift (and any subsequent donations) plus accumulated investment earnings, less accumulated investment losses and appropriations for expenditure by the Museum at any point in time.

Previous California law restricted spending on donor-restricted endowment funds where the value of the fund fell below the “historic dollar value.” The historic dollar value represented the aggregate value of all contributions to an endowment fund at the time they were made. Absent explicit donor instructions to the contrary, the Museum interprets UPMIFA to have eliminated the historic dollar value limitation when considering endowment spending, instead providing guidelines for such spending (referred to as “appropriation” in UPMIFA). In accordance with UPMIFA, the Museum considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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- (1) The duration and preservation of the fund
- (2) The purposes of the Museum and the donor-restricted endowment fund
- (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) Other resources of the Museum
- (7) The investment policy of the Museum

The Board adopted a spending policy for permanently restricted endowment funds based on a rolling average of historical market values. In fiscal year 2009 the Board approved the annual use of approximately 5% of the endowment funds' calculated fair market value for the Museum's operations. The Board appropriated approximately \$1,601,000 from permanently restricted endowment funds in 2012 for operations. An additional board approved draw of \$786,000 was made to pay down bond debt in June 2012 and another \$812,000 was drawn to pay down bond debt in August 2012.

The Museum's endowment investment policy and strategy is to emphasize total return, that is, the aggregate return from capital appreciation and dividend and interest income. Within this framework specific investment objectives for endowment investments include liquidity, preservation of capital, preservation of purchasing power, and long-term growth of capital.

Occasionally, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the Museum to retain as a fund of perpetual duration. In accordance with the authoritative guidance, deficiencies of this nature are reported in unrestricted net assets in the year in which they occur. Deficiencies of this nature that are reported in unrestricted net assets were approximately \$5,991,000 as of June 30, 2012. Gains and income in subsequent years will be netted against this deficiency until the fair value is once again above the initial level. During 2012, approximately \$392,000 in gains and income on the endowments were netted against the loss classified in unrestricted net assets as of June 30, 2012.

The following is a composition of the Museum's endowment by net asset class in total and by type of endowment fund as of June 30, 2012:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Board-designated Funds	\$ 2,009,074	\$ -	\$ -	\$ 2,009,074
Donor-restricted Funds	(7,999,760)	98,109	39,058,378	31,156,727
	<u>\$ (5,990,686)</u>	<u>\$ 98,109</u>	<u>\$ 39,058,378</u>	<u>\$ 33,165,801</u>



**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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Changes in endowment net assets for the year ended June 30, 2012 are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment assets, June 30, 2011	\$ (6,211,963)	\$ 123,318	\$ 39,058,378	\$ 32,969,733
Interest and dividends, net	545,545	7,403	-	552,948
Net appreciation (realized gain)	63,926	1,494	-	65,420
Net appreciation (unrealized gain)	53,663	-	-	53,663
Net appreciation (unrealized loss)	(439,798)	(7,248)	-	(447,046)
Funds in	348,719	-	-	348,719
Funds in (board designated endowment)	2,009,074	-	-	2,009,074
Appropriations	(1,581,952)	(19,184)	-	(1,601,136)
Bond pay down	(777,900)	(7,674)	-	(785,574)
Endowment assets, June 30, 2012	<u>\$ (5,990,686)</u>	<u>\$ 98,109</u>	<u>\$ 39,058,378</u>	<u>\$ 33,165,801</u>

Note that the difference between the permanently restricted net assets presented in the Statement of Activities and the amount included in the table above relates to outstanding pledge receivables and settlement of CRT not invested as an endowment.

**9. TEMPORARILY RESTRICTED NET ASSETS**

Temporarily restricted net assets are available for the following purposes:

General operations and programs	\$ 3,909,109
21st Century building campaign	1,879,851
Accessions and exhibitions	1,472,384
Total	<u>\$ 7,261,344</u>

**10. PERMANENTLY RESTRICTED NET ASSETS**

Permanently restricted net assets are comprised of investments in perpetuity, the income from which is expendable for support of:

General operations and programs	\$ 38,868,807
Accessions and exhibitions	873,406
Total	<u>\$ 39,742,213</u>

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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**11. NET ASSETS RELEASED FROM RESTRICTIONS**

Net assets were released from donor restriction by board appropriation satisfying the restricted purposes specified by donors as follows:

21st Century building campaign	\$ 694,673
General operations and programs	1,065,044
Accessions and exhibitions	701,842
Total	<u>\$ 2,461,559</u>

**12. OPERATING LEASES**

In July 1992, the Museum entered into a ground lease agreement for property the Museum occupies in downtown San Diego. The term of the lease is 99 years and the annual lease payment is \$1.00. The Museum has agreed to comply with certain use and operating restrictions as defined in the lease agreement. The estimated fair value of the lease for 2012 is approximately \$226,000 per year based on rent for similar property in the area and is reflected as unrestricted contributions support and expense in the accompanying statement of activities.

The Museum leases storage space and equipment under non-cancelable operating leases. Certain of these leases include renewal and purchase options. Rent expense under these leases was approximately \$255,000, of which approximately \$98,000 was donated in 2012 and included in unrestricted contributions support.

Future minimum rental payments required under operating leases that have initial or remaining non-cancelable lease terms in excess of one year are as follows:

**Year Ending June 30,**

2013	\$ 128,888
2014	114,399
2015	112,491
2016	56,725
2017	-
Thereafter	-
Total	<u>\$ 412,503</u>

On February 1, 2006 (“Effective Date”), the Museum entered into an agreement with the National Rail Passenger Corporation (“Amtrak”) that allows Amtrak to occupy a portion of the David C. Copley Building (“Copley Building”). Although the agreement states that the \$850,000 payment received from Amtrak is a reimbursement for Amtrak’s agreed share of the costs of construction of the Copley Building, the Museum applied the applicable authoritative guidance to account for the payment as a lease. The term of the lease commenced on March 1, 2007 and expires on July 31, 2091. Rental income was approximately \$10,000 for 2012. Deferred rent revenue at June 30, 2012 is approximately \$792,000 and is included in deferred revenue on the statement of financial position.

**MUSEUM OF CONTEMPORARY ART SAN DIEGO**  
**NOTES TO FINANCIAL STATEMENTS**  
**AS OF AND FOR YEAR ENDED JUNE 30, 2012**

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**13. EMPLOYEE RETIREMENT PLAN**

The Museum has an employee retirement plan that is a defined contribution plan under which the Museum matches a percentage of the participants' contributions after one year of employment. The contributions are made in accordance with Section 403(b) of the Internal Revenue Code. Total employer contributions were approximately \$73,000 for 2012.

In 2008 the Museum set up qualified 457(b) plans and a 457(f) plan for two top executives. Employer contributions to these plans totaled approximately \$87,000 in 2012. The plans require the Museum to deposit employer contributions in a separate bank account each year. Assets contributed to the plans remain the sole property of the Museum until a covered employee is eligible to receive distributions.

**14. LITIGATION**

In the normal course of business, the Museum is occasionally named in various claims and litigations. It is the opinion of management that the outcome of any pending items will not materially affect the operations or the financial position of the Museum. Management is not aware of any lawsuits where the Museum is currently named.

**15. SUBSEQUENT EVENTS**

The Museum has evaluated subsequent events through November 8, 2012, which is the date the financial statements were available to be issued.

**SUPPLEMENTAL SCHEDULES  
FOR THE YEAR ENDED JUNE 30, 2012**

**Museum of Contemporary Art San Diego**  
**Schedule of Functional Expenses**  
**For the Year Ended June 30, 2012**

	Program Services								Support Services							Total
	Exhibitions	Publications	Curatorial	Permanent Collections, Circulation and Accessions	Events and Visitor Services	Education Performances Library	Museum Stores	Membership Support	Museum Beverage Service	PR and Marketing	Development	Special Events	General and Administrative	Building		
Salaries and employee benefits	\$ 427,048	\$ 5,762	\$ 456,243	\$ 208,268	\$ 395,756	\$ 157,914	\$ 71,424	\$ 239,909	\$ 6,527	\$ 215,073	\$ 300,235	\$ 8,847	\$ 1,169,013	\$ 164,107	\$ 3,826,126	
Accessions of art, net of deaccessions	-	-	-	583,500	-	-	-	-	-	-	-	-	-	-	583,500	
Advertising and marketing	-	17	-	-	4,533	-	-	-	-	48,317	-	3,813	-	-	56,680	
Bank service fees/Interest expense	410	-	20	11,440	5,544	413	5,503	14,089	2,693	-	-	30,009	135,786	-	205,907	
Amortization of Bond issuance fees	-	-	-	-	-	-	-	-	-	-	-	-	15,380	-	15,380	
Contract/Consulting services	237,078	3,200	67	59,072	21,958	23,015	304	20,845	113,024	57,766	21,181	275,996	43,706	299,250	1,176,462	
Computer materials/service	-	-	-	-	1,188	-	-	-	-	970	-	-	852	2,645	5,655	
Cost of sales	-	73,124	-	-	-	-	123,812	-	44,645	-	-	-	-	-	241,581	
Depreciation	-	-	-	-	-	-	-	-	-	-	-	-	-	1,097,883	1,097,883	
Food and entertainment	2,639	64	977	23	941	6,532	224	41,003	147	1,652	3,035	80,624	46,772	168	184,801	
Graphic design and printing	25,987	-	351	606	36	3,778	2	22,344	-	14,306	1,087	24,608	630	-	93,735	
Honoraria/artist fees	3,171	-	-	-	-	9,150	-	-	-	-	-	34,605	-	-	46,926	
Insurance	173	-	-	62,334	600	-	-	190	2,053	-	-	256	14,138	56,098	135,842	
Investment fee	2,524	-	-	9,308	-	9,567	-	-	-	-	-	-	171,831	-	193,230	
In-kind contributions	5,120	-	-	-	-	-	-	44,367	-	61,500	-	683,694	-	-	794,681	
Legal and accounting	-	-	-	11,226	50	12,795	-	-	-	-	-	-	81,679	-	105,750	
Loss on disposal of assets	-	-	-	-	-	-	-	-	-	-	-	-	-	2,517	2,517	
Membership, dues and subscriptions	-	-	1,670	5,786	26	20	-	1,809	-	2,825	3,019	-	22,131	248	37,534	
Miscellaneous	177	42,667	4,232	120	30	240	6,773	1,698	-	680	108	385	11,538	765	69,413	
Newsletter	-	-	-	-	-	-	-	-	-	36,465	-	-	-	-	36,465	
New employee search/staff training	375	-	15,171	1,365	435	1,522	416	907	-	765	1,338	-	3,763	270	26,327	
Participation fees	44,332	-	-	-	-	-	-	-	-	-	-	-	-	-	44,332	
Photography	8,507	-	33	1,409	-	982	-	2,701	-	955	-	4,861	-	-	19,448	
Postage	3	1,467	742	317	109	158	19	22,258	-	352	215	6,083	2,323	73	34,119	
Rentals	234,276	7,852	-	101,308	-	2,228	-	10,517	16,328	-	-	29,321	15,569	63,640	481,039	
Repairs and maintenance	-	-	-	2,678	336	-	-	-	-	-	-	-	885	81,222	85,121	
Restoration	34,216	-	-	4,751	-	-	-	-	-	-	-	2,370	-	-	41,337	
Shipping and crating	137,891	687	223	37,842	-	115	4,733	50	-	648	88	6,100	150	449	188,976	
Supplies and equipment	61,308	216	5,479	11,087	14,006	11,531	2,355	9,281	12,218	1,398	3,617	7,605	11,445	45,581	197,127	
Taxes	-	-	-	-	15,667	-	-	-	-	-	-	-	1,696	38,129	55,492	
Telephone	-	-	-	-	-	38	-	-	-	-	-	-	698	65,707	66,443	
Travel and accommodations	30,036	254	15,154	6,275	1,201	11,450	172	(2,553)	(106)	5,098	3,627	82	39,594	2,349	112,633	
Utilities	-	-	-	13,619	-	-	-	-	-	-	-	-	-	330,458	344,077	
	1,255,271	135,310	500,362	1,132,334	462,416	251,448	215,737	429,415	197,529	448,770	337,550	1,199,259	1,789,579	2,251,559	10,606,539	
Allocation of building expenses	\$ 1,403,617	\$ -	\$ 27,046	\$ 366,242	\$ 241,634	\$ 118,917	\$ 29,369	\$ 3,511	\$ -	\$ 6,446	\$ 23,211	\$ -	\$ 31,566	\$ (2,251,559)	-	
	\$ 2,658,888	\$ 135,310	\$ 527,408	\$ 1,498,576	\$ 704,050	\$ 370,365	\$ 245,106	\$ 432,926	\$ 197,529	\$ 455,216	\$ 360,761	\$ 1,199,259	\$ 1,821,145	\$ -	\$ 10,606,539	



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## **INDEPENDENT AUDITORS' REPORT ON ADDITIONAL INFORMATION**

To the Audit Committee of  
**Museum of Contemporary Art San Diego**

We have audited the financial statements of **Museum of Contemporary Art San Diego** (the "Museum") for the year ended June 30, 2012, and have issued our report thereon dated November 8, 2012. Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. The additional information on page 23 is presented for the purpose 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 our 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 taken as a whole.

*Mayer Hoffman McCann P.C.*

November 8, 2012

# MUSEUM OF CONTEMPORARY ART SAN DIEGO

## SCHEDULE OF BUDGETED AND ACTUAL EXPENDITURES OF CITY FUNDS SPECIAL PROMOTIONAL FUND AWARD FOR THE YEAR ENDED JUNE 30, 2012

COMMISSION FOR ARTS AND CULTURE, CITY OF SAN DIEGO BUDGET AND EXPENSES	<u>Budgeted</u>	<u>Actual</u>	<u>Total Funds</u>
<b>Expense Classification</b>			
All salaried personnel	\$ 3,809,490	\$ 3,628,625	\$ 65,000
Operating Expenses - nonpersonnel			
Advertising and marketing	173,582	180,560	50,000
Production and exhibition	1,329,227	1,241,967	144,234
Other (administrative, fundraising, stores, MBS)	2,062,568	2,075,144	-
Total operating expenses	<u>3,565,377</u>	<u>3,497,671</u>	<u>194,234</u>
Total expenses	<u>\$ 7,374,867</u>	<u>\$ 7,126,296</u>	<u>\$ 259,234</u>

NOTE: Budget and actual amounts are only a component of the Museum's operations and are not intended to reflect all of the operations of the Museum.