

**San Jose Museum of Art Association**

Financial Statements

June 30, 2018

(With Comparative Totals for 2017)



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## INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees  
San Jose Museum of Art Association  
San Jose, California

We have audited the accompanying financial statements of San Jose Museum of Art Association (a California nonprofit corporation) (the "Museum"), which comprise the statement of financial position as of June 30, 2018, and the related statements of activities, functional expenses, 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 San Jose Museum of Art Association as of June 30, 2018, 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.

## Report on Summarized Comparative Information

We have previously audited San Jose Museum of Art Association's 2017 financial statements, and our report dated October 19, 2017 expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2017, is consistent, in all material respects, with the audited financial statements from which it has been derived.

A handwritten signature in black ink that reads "Armanino LLP". The signature is written in a cursive, flowing style.

Armanino<sup>LLP</sup>  
San Jose, California

November 16, 2018

San Jose Museum of Art Association  
Statement of Financial Position  
June 30, 2018  
(With Comparative Totals for 2017)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2018 Total</u>	<u>2017 Total</u>
<b>ASSETS</b>					
Cash and cash equivalents	\$ 1,835,400	\$ 90,202	\$ -	\$ 1,925,602	\$ 2,181,472
Accounts receivable	57,881	5,219	-	63,100	86,281
Contributions receivable	62,330	1,230,222	-	1,292,552	1,520,674
Museum store inventory	68,948	-	-	68,948	71,057
Note receivable - related party	-	-	-	-	250,000
Deferred exhibition costs and prepaids	120,907	-	-	120,907	90,233
Investments	100,000	2,811,828	7,830,492	10,742,320	9,844,492
Property and equipment, net	6,483	-	-	6,483	8,401
Beneficial interest in perpetual trust	-	-	930,117	930,117	930,117
	-	-	930,117	930,117	930,117
Total assets	<u>\$ 2,251,949</u>	<u>\$ 4,137,471</u>	<u>\$ 8,760,609</u>	<u>\$ 15,150,029</u>	<u>\$ 14,982,727</u>
<b>LIABILITIES AND NET ASSETS</b>					
<b>Liabilities</b>					
Accounts payable	\$ 62,017	\$ -	\$ -	\$ 62,017	\$ 69,427
Accrued liabilities	374,846	-	-	374,846	207,795
Unearned revenue	129,036	-	-	129,036	132,770
Total liabilities	<u>565,899</u>	<u>-</u>	<u>-</u>	<u>565,899</u>	<u>409,992</u>
<b>Net assets</b>					
Unrestricted	1,686,050	-	-	1,686,050	1,713,911
Temporarily restricted	-	4,137,471	-	4,137,471	4,298,215
Permanently restricted	-	-	8,760,609	8,760,609	8,560,609
Total net assets	<u>1,686,050</u>	<u>4,137,471</u>	<u>8,760,609</u>	<u>14,584,130</u>	<u>14,572,735</u>
Total liabilities and net assets	<u>\$ 2,251,949</u>	<u>\$ 4,137,471</u>	<u>\$ 8,760,609</u>	<u>\$ 15,150,029</u>	<u>\$ 14,982,727</u>

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

San Jose Museum of Art Association  
Statement of Activities  
For the Year Ended June 30, 2018  
(With Comparative Totals for 2017)

	Unrestricted	Temporarily Restricted	Permanently Restricted	2018 Total	2017 Total
Operating support and revenue					
Contributions and grants	\$ 1,159,126	\$ 1,489,993	\$ -	\$ 2,649,119	\$ 2,489,798
Public programs	559,214	-	-	559,214	452,346
Other in-kind support	315,767	-	-	315,767	329,180
Museum store	222,761	-	-	222,761	224,920
Special events, net	202,097	-	-	202,097	195,621
Membership dues	173,230	-	-	173,230	190,393
Event rental income	54,300	-	-	54,300	59,600
Art class contracts and tuition	46,830	-	-	46,830	37,770
Other revenue	12,939	-	-	12,939	22,634
Net assets released from restriction	2,397,080	(2,397,080)	-	-	-
Total	<u>5,143,344</u>	<u>(907,087)</u>	<u>-</u>	<u>4,236,257</u>	<u>4,002,262</u>
In-kind rent	<u>2,340,000</u>	<u>-</u>	<u>-</u>	<u>2,340,000</u>	<u>1,872,000</u>
Total operating support and revenue	<u>7,483,344</u>	<u>(907,087)</u>	<u>-</u>	<u>6,576,257</u>	<u>5,874,262</u>
Operating expenses					
Program services					
Exhibitions	3,915,132	-	-	3,915,132	3,447,873
Education	1,718,491	-	-	1,718,491	1,299,013
Museum store	462,724	-	-	462,724	415,641
Total program services	<u>6,096,347</u>	<u>-</u>	<u>-</u>	<u>6,096,347</u>	<u>5,162,527</u>
Support services					
Management and general	645,583	-	-	645,583	540,367
Fundraising	724,356	-	-	724,356	669,906
Total support services	<u>1,369,939</u>	<u>-</u>	<u>-</u>	<u>1,369,939</u>	<u>1,210,273</u>
Total operating expenses	<u>7,466,286</u>	<u>-</u>	<u>-</u>	<u>7,466,286</u>	<u>6,372,800</u>
Change in net assets from operations	<u>17,058</u>	<u>(907,087)</u>	<u>-</u>	<u>(890,029)</u>	<u>(498,538)</u>
Non-operating activities					
Endowment investment income, net	-	750,154	-	750,154	1,202,543
Endowment contributions	-	-	200,000	200,000	200,000
Contributions for art collection items	-	543,668	-	543,668	202,995
General investment income, net	4,901	-	-	4,901	6,163
Depreciation and amortization	(1,918)	-	-	(1,918)	(2,723)
Net assets released from restriction - art acquisition	496,777	(496,777)	-	-	-
Net assets released from restriction - art acquisition endowment	50,702	(50,702)	-	-	-
Purchased art collection items	(575,244)	-	-	(575,244)	(228,752)
Separation payout	(20,137)	-	-	(20,137)	(260,982)
Total non-operating activities	<u>(44,919)</u>	<u>746,343</u>	<u>200,000</u>	<u>901,424</u>	<u>1,119,244</u>
Change in net assets	(27,861)	(160,744)	200,000	11,395	620,706
Net assets, beginning of year	<u>1,713,911</u>	<u>4,298,215</u>	<u>8,560,609</u>	<u>14,572,735</u>	<u>13,952,029</u>
Net assets, end of year	<u>\$ 1,686,050</u>	<u>\$ 4,137,471</u>	<u>\$ 8,760,609</u>	<u>\$ 14,584,130</u>	<u>\$ 14,572,735</u>

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

San Jose Museum of Art Association  
Statement of Functional Expenses  
For the Year Ended June 30, 2018  
(With Comparative Totals for 2017)

	Program Services				Support Services			2018 Total	2017 Total
	Exhibitions	Education	Museum store	Total Program Services	Management and General	Fundraising	Total Support Services		
Operating expenses									
Salaries and benefits									
Salaries and wages	\$ 1,145,309	\$ 542,732	\$ 100,245	\$ 1,788,286	\$ 246,280	\$ 341,346	\$ 587,626	\$ 2,375,912	\$ 2,233,901
Payroll taxes and benefits	202,066	87,271	17,757	307,094	44,263	71,447	115,710	422,804	368,801
Total salaries and benefits	<u>1,347,375</u>	<u>630,003</u>	<u>118,002</u>	<u>2,095,380</u>	<u>290,543</u>	<u>412,793</u>	<u>703,336</u>	<u>2,798,716</u>	<u>2,602,702</u>
In-kind rent	1,568,915	312,817	186,008	2,067,740	113,442	158,818	272,260	2,340,000	1,872,000
Outside services and security	273,605	134,461	-	408,066	106,865	10,546	117,411	525,477	355,585
Volunteer services	-	245,220	22,707	267,927	-	-	-	267,927	275,730
Travel	38,053	207,540	1,114	246,707	9,751	1,474	11,225	257,932	109,053
Marketing	155,895	-	-	155,895	6,649	-	6,649	162,544	145,132
Shipping and storage	158,638	203	115	158,956	-	-	-	158,956	163,121
Exhibition costs	140,644	1,337	-	141,981	-	1,882	1,882	143,863	124,687
Cost of goods sold	-	-	117,071	117,071	-	-	-	117,071	117,552
Printing and web design	16,553	54,635	37	71,225	2,283	23,357	25,640	96,865	47,013
Materials	38,071	53,809	-	91,880	3,878	-	3,878	95,758	89,932
Telephone and utilities	23,671	10,007	2,256	35,934	22,032	16,428	38,460	74,394	66,630
Catering	19,516	25,382	-	44,898	581	17,730	18,311	63,209	51,813
Miscellaneous	16,419	9,443	1,233	27,095	11,777	12,547	24,324	51,419	47,485
Equipment expenses	25,265	3,648	503	29,416	19,212	2,511	21,723	51,139	44,614
Software maintenance	20,588	-	1,141	21,729	3,407	17,941	21,348	43,077	44,268
Legal and accounting	-	-	-	-	42,758	-	42,758	42,758	38,905
Insurance	35,486	2,417	1,437	39,340	877	1,227	2,104	41,444	42,903
Bank charges	4,388	4,587	8,666	17,641	380	21,389	21,769	39,410	31,867
Office supplies and postage	12,059	2,939	2,223	17,221	8,820	8,223	17,043	34,264	29,761
In-kind support expense	16,466	16,200	-	32,666	-	15,174	15,174	47,840	53,450
Meetings and lunches	2,225	3,843	211	6,279	157	1,991	2,148	8,427	5,400
Recruiting	-	-	-	-	2,171	325	2,496	2,496	6,883
Conservation	1,300	-	-	1,300	-	-	-	1,300	6,314
Total operating expenses	<u>3,915,132</u>	<u>1,718,491</u>	<u>462,724</u>	<u>6,096,347</u>	<u>645,583</u>	<u>724,356</u>	<u>1,369,939</u>	<u>7,466,286</u>	<u>6,372,800</u>
Non-operating expenses									
Purchased art collection items	575,244	-	-	575,244	-	-	-	575,244	228,752
Depreciation and amortization	959	575	192	1,726	96	96	192	1,918	2,723
Separation payout	-	-	-	-	20,137	-	20,137	20,137	260,982
Total non-operating expenses	<u>576,203</u>	<u>575</u>	<u>192</u>	<u>576,970</u>	<u>20,233</u>	<u>96</u>	<u>20,329</u>	<u>597,299</u>	<u>492,457</u>
	<u>\$ 4,491,335</u>	<u>\$ 1,719,066</u>	<u>\$ 462,916</u>	<u>\$ 6,673,317</u>	<u>\$ 665,816</u>	<u>\$ 724,452</u>	<u>\$ 1,390,268</u>	<u>\$ 8,063,585</u>	<u>\$ 6,865,257</u>
Percentage of total	<u>55.7 %</u>	<u>21.3 %</u>	<u>5.7 %</u>	<u>82.7 %</u>	<u>8.3 %</u>	<u>9.0 %</u>	<u>17.3 %</u>	<u>100.0 %</u>	

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

San Jose Museum of Art Association  
Statement of Cash Flows  
For the Year Ended June 30, 2018  
(With Comparative Totals for 2017)

	<u>2018</u>	<u>2017</u>
Cash flows from operating activities		
Change in net assets	\$ 11,395	\$ 620,706
Adjustments to reconcile change in net assets to net cash used in operating activities		
Depreciation and amortization	1,918	2,723
Net realized gain on sale of investments	(193,810)	(625,386)
Net unrealized gain on investments	(221,046)	(294,021)
Contributions restricted for long-term purposes	(200,000)	(200,000)
Changes in operating assets and liabilities		
Accounts receivable	23,181	(11,006)
Contributions receivable	228,120	172,160
Museum store inventory	2,111	774
Deferred exhibition costs and prepaids	(30,674)	58,056
Accounts payable	(7,410)	20,480
Accrued liabilities	167,051	54,196
Unearned revenue	(3,734)	23,428
Net cash used in operating activities	<u>(222,898)</u>	<u>(177,890)</u>
Cash flows from investing activities		
Proceeds from sale or maturity of investments	1,080,987	1,303,002
Purchase of investments	(1,563,959)	(1,357,194)
Repayment of note receivable - related party	250,000	-
Net cash used in investing activities	<u>(232,972)</u>	<u>(54,192)</u>
Cash flows from financing activities		
Proceeds from contributions restricted for long-term purposes	200,000	200,000
Net cash provided by financing activities	<u>200,000</u>	<u>200,000</u>
Net decrease in cash and cash equivalents	(255,870)	(32,082)
Cash and cash equivalents, beginning of year	<u>2,181,472</u>	<u>2,213,554</u>
Cash and cash equivalents, end of year	<u>\$ 1,925,602</u>	<u>\$ 2,181,472</u>

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



San Jose Museum of Art Association  
Notes to Financial Statements  
June 30, 2018  
(With Comparative Totals for 2017)

1. ORGANIZATION

San Jose Museum of Art Association (the "Museum" or "SJMA") is a California nonprofit public benefit corporation incorporated in 1969. The San Jose Museum of Art reflects the diverse cultures and innovative spirit of Silicon Valley. Through its exhibitions, educational programs, scholarship, and collections, SJMA connects the present and the past and the art of the West Coast and the world. The Museum fosters awareness of artists' broad contributions to society; it engages audiences with the art of our time and the vitality of the creative process. SJMA also owns and operates a store located in the Museum.

The Museum's operations receive support from the City of San Jose through a facility subsidy, a program grant, and its donation of in-kind rent.

Exhibitions

Founded in 1969 by artists, SJMA is a modern and contemporary art museum located near the Plaza de César Chavez in downtown San José. The only art museum in the South Bay accredited by the American Alliance of Museums (AAM) and an invited member of the Association of Art Museums Directors (AAMD), SJMA offers a dynamic exhibition program of ten or more rotating exhibitions and attending public programs per year. SJMA presents the cutting-edge vision of California and Pacific Rim artists. Given its location in the heart of Silicon Valley, the Museum has a substantial commitment to showing and nurturing visionary work in new media: initiatives include an experimental gallery-as-laboratory for artists called "Beta Space," and the exhibition series "New Stories from the Edge of Asia." The Museum's talented curatorial staff creates thematic exhibitions drawn from its permanent collection of more than 2,500 works of art, and hosts exhibitions organized by significant California and national museums. Designed to appeal to audiences in San José and Silicon Valley, these exhibitions celebrate the work of groundbreaking, independent thinkers, and interject artists' voices into broader community discussions on topics from immigration to water politics.

San Jose Museum of Art Association  
Notes to Financial Statements  
June 30, 2018  
(With Comparative Totals for 2017)

1. ORGANIZATION (continued)

Education

The Museum is the largest provider of arts education in Santa Clara County, serving more than 40,000 school children per year. The Museum proudly offers a spectrum of educational programs that provide critical early exposure to the visual arts for tens of thousands of students in grades kindergarten through twelve, e.g. tours, workshops, in-class presentations, and curriculum guides. Initiatives such as the award-winning school programs “Let’s Look at Art,” which provides free docent presentations in the classroom, and the award-winning integrated visual arts residency “Sowing Creativity” which offers ten-week courses in art and science (3rd grade), art and math (4th grade), and art and engineering (5th grade), further distinguish the Museum as a leader in museum education. During the year ended June 30, 2018, the Museum received funding from the California Arts Council to provide free school tours to some 2,500 students in Title 1 schools. SJMA also offers sequential in-school artmaking workshops (often combined with museum tours); professional development opportunities for teachers; free family-oriented Community Days with hands-on activities and a variety of performances; Kids’ Summer Art Camp, weeklong adventures into art making that are linked to current exhibitions; and lectures, conversations, and symposia with artists that give the public close access to the creative process. In addition, adult programs include after-hours events that make the Museum a social hub downtown.

SJMA’s website enables access to the most current information, including educational materials, video interviews, curatorial essays and integrated social media participation. Web-based access to the collection has increased opportunities for students, scholars and the public to research the art and artists in the permanent collection since 2013, made easily accessible via mobile devices.

Museum store

The Museum Store is located off SJMA’s main lobby. This gift and book store carries mission-related products that are educational, foster creativity, and encourage the appreciation of art. The Museum Store also features custom products by area artists and craftsmen as well as merchandise relevant to the current exhibitions. The store is staffed by Museum employees as well as by an active contingent of longtime volunteers.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting and financial statement presentation

The financial statements of San Jose Museum of Art Association have been prepared on the accrual basis of accounting.

In accordance with generally accepted accounting principles, the Museum reports its financial position and activities in three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

San Jose Museum of Art Association  
Notes to Financial Statements  
June 30, 2018  
(With Comparative Totals for 2017)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of accounting and financial statement presentation (continued)

- *Unrestricted net assets* - include those assets over which the Board of Trustees has discretionary control in carrying out the operations of the Museum. Under this category, the Museum maintains an operating fund, plus any net assets designated by the Board for specific purposes.
- *Temporarily restricted net assets* - include contributions received from donors that are restricted for specific purposes or for subsequent periods. When a donor restriction expires, temporarily restricted net assets are classified to unrestricted net assets and reported in the statement of activities as net assets released from restriction.
- *Permanently restricted net assets* - include those assets which are subject to a non-expiring donor restriction, such as endowments.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of support, revenue and expenses during the period. Accordingly, actual results could differ from those estimates.

Summarized financial information

The financial statements include certain prior-year summarized comparative information in total but not by net asset class or functional expense categories. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Museum's financial statements for the year ended June 30, 2017, from which the summarized information was derived.

Cash and cash equivalents

Cash and cash equivalents include highly liquid investments and investments with a maturity of three months or less. The Museum maintains its cash in bank deposit accounts which, at times, may exceed Federally insured limits. The Museum has not experienced any losses in such accounts. Management believes it is not exposed to any significant risk on cash accounts.

Museum store inventory

Museum store inventory is valued at the lower of cost or net realizable value and consists primarily of books and other education and exhibition-related items held for sale.

San Jose Museum of Art Association  
Notes to Financial Statements  
June 30, 2018  
(With Comparative Totals for 2017)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments

Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the statement of financial position. Unrealized gains and losses are included in the change in net assets. Investment income and gains restricted by a donor are reported as increases in temporarily restricted net assets. When donor restrictions are met (either by passage of time or by use), temporarily restricted net assets are classified to unrestricted net assets and reported in the statement of activities as net assets released from restriction.

Fair value measurements

Fair value is defined as "the price 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."

A hierarchy has been established to prioritize the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest ranking to fair values determined using unadjusted quoted prices in active markets for identical assets (Level 1) and the lowest ranking to fair values determined using methodologies and models with unobservable inputs (Level 3). Observable inputs are those that market participants would use in pricing the asset based on market data obtained from sources independent of the Museum. Unobservable inputs reflect the Museum's assumption about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The fair value hierarchy is categorized into three levels based on the inputs as follows:

- *Level 1* - Values are unadjusted quoted prices for identical assets and liabilities in active markets accessible at the measurement date.
- *Level 2* - Inputs include quoted prices for similar assets or liabilities in active markets, quoted prices from those willing to trade in markets that are not active, or other inputs that are observable or can be corroborated by market data for the term of the instrument. Such inputs include market interest rates and volatilities, spreads and yield curves.
- *Level 3* - Certain inputs are unobservable (supported by little or no market activity) and significant to the fair value measurement. Unobservable inputs reflect the Museum's best estimate of what hypothetical market participants would use to determine a transaction price for the asset or liability at the reporting date.

San Jose Museum of Art Association  
Notes to Financial Statements  
June 30, 2018  
(With Comparative Totals for 2017)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Permanent art collection

The collection consists of twentieth and twenty-first century artwork, including paintings, sculptures, installations, new media, photography, drawings and prints, acquired through purchase or contribution. The collection is not recognized as an asset in the statement of financial position. Each work of art is inventoried and cared for, and activities verifying the collection's integrity are performed continuously. Purchases of art are recorded as non-operating decreases in the unrestricted net assets in the year in which items are acquired. Contributed collection items are not reflected in the financial statements. Proceeds from any deaccessions or insurance recoveries are required to be used to acquire other works of art.

Accounts and contributions receivable

The Museum considers all accounts and contributions receivable to be fully collectible; accordingly, no allowance for doubtful accounts is considered necessary.

Property and equipment

Property and equipment are recorded at cost or estimated fair value for donated items. Purchases of individual items of property and equipment with a cost greater than \$3,000 are capitalized. In addition, items with individual costs exceeding \$2,500 with a total invoice cost of \$8,000 are capitalized. The cost of repairs and maintenance which do not improve or extend the lives of the respective assets are expensed as incurred. Depreciation is computed on the straight-line method based on the estimated useful lives of the assets, which range from 5 to 10 years. Depreciation is charged to the activity benefiting from the use of the property or equipment.

Impairment of long-lived assets

The Museum reviews property and equipment for impairment whenever events or changes in circumstances indicate that the carrying value of the property and equipment may not be recoverable. Recoverability is measured by a comparison of the carrying amount of the asset to future net cash flows, undiscounted and without interest, expected to be generated by the asset. If assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds the fair value of the asset. For the years ended June 30, 2018 and 2017, there were no events or changes in circumstances indicating that the carrying amount of the property and equipment may not be recoverable.

Accrued vacation

Accrued vacation represents vacation earned, but not taken as of June 30, 2018 and 2017, and is included in "accrued liabilities" in the statement of financial position. The accrued vacation balance as of June 30, 2018 and 2017, was \$103,086 and \$90,013, respectively.

San Jose Museum of Art Association  
Notes to Financial Statements  
June 30, 2018  
(With Comparative Totals for 2017)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue recognition

The Museum recognizes support and revenue on the accrual basis of accounting. Revenue from grants which have been classified as "exchange transactions" and program fees are recognized as revenue in the period in which the service is provided.

Unearned revenue

Membership dues received in advance are deferred and recognized as revenue over the periods to which the dues relate. Unearned revenue also includes amounts received for exhibits and events that will be presented in a future period.

Contributions

Contributions are recognized when the donor makes a pledge to give that is, in substance, an unconditional promise. Contributions are recorded as unrestricted, temporarily restricted, or permanently restricted depending on the nature of donor restrictions. Restricted contributions are reported as increases in restricted net assets. When the restriction is met the amount is shown as a reclassification of restricted net assets to unrestricted net assets.

In-kind rent and other in-kind support

In-kind rent is valued based on current prevailing downtown San Jose rent rates. Donated equipment and other donated goods are recorded at their estimated fair value as of the date of the donation. Contributed services, which require a specialized skill and which the Museum would have paid for if not donated, are recorded at the estimated fair value at the time the services are rendered. The estimated value of in-kind rent and other in-kind support is disclosed in Note 13.

Functional expense allocation

Indirect functional expenses are allocated to program and support services based on an analysis of salary dollars, headcount, and space utilized.

Income tax status

San Jose Museum of Art Association is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code and state income taxes under Section 23701(d) of the California Revenue Taxation Code. However, income from certain activities not directly related to the Museum's tax-exempt purpose is subject to taxation as unrelated business income. In addition, the Museum qualifies for the charitable contribution deduction under Section 170(b)(1)(A) of the Internal Revenue Code and has been classified as an organization that is not a private foundation under Section 509(a)(1) of the Internal Revenue Code.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Uncertainty in income taxes

Generally accepted accounting principles provide accounting and disclosure guidance about positions taken by an organization in its tax returns that might be uncertain. Management has considered its tax positions and believes that all of the positions taken by the Museum in its federal and state exempt organization tax returns are more likely than not to be sustained upon examination.

The Museum files information returns in the U.S. federal jurisdiction and state of California. The Museum's federal returns for the years ended June 30, 2015, and beyond remain subject to possible examination by the Internal Revenue Service. The Museum's California returns of the tax years ended June 30, 2014, and beyond remain subject to possible examination by the Franchise Tax Board.

Advertising costs

The Museum's policy is to expense advertising costs as the costs are incurred. Advertising expenses for the years ended June 30, 2018 and 2017, totaled \$131,955 and \$121,701, respectively.

Subsequent events

Management of the Museum has evaluated events and transactions subsequent to June 30, 2018, for potential recognition or disclosure in the financial statements. The Museum did not have subsequent events that required recognition or disclosure in the financial statements for the fiscal year ended June 30, 2018. Subsequent events have been evaluated through the date the financial statements became available to be issued, November 16, 2018.

Liquidity management

As of June 30, 2018, the Museum has unrestricted cash of \$1,835,400. During the year ended June 30, 2018, the Museum incurred a change in unrestricted net assets from operations of \$27,861 and had negative cash flows from operating activities of \$222,898. To date, the Museum has been funded primarily by contributions and program revenue. The Museum's ultimate success is dependent upon its ability to maintain program revenue and fundraise. The financial statements do not include any adjustments to reflect possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

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3. CONTRIBUTIONS RECEIVABLE

Contributions receivable consist of the following:

	2018	2017
Programs and other	\$ 1,292,552	\$ 1,533,787
	1,292,552	1,533,787
Less: discounts to net present value	-	(13,113)
	\$ 1,292,552	\$ 1,520,674

As of June 30, 2018, \$1,292,552 of contributions receivable is expected to be collected in less than one year and \$0 is expected to be collected in one to five years. The Museum periodically evaluates the collectability of its contributions receivable based on historical experience. Uncollectible contributions are expected to be insignificant; therefore, an allowance for doubtful accounts has not been recorded as of June 30, 2018 and 2017.

Unconditional promises to give, which are not expected to be collected until after the year contributed, are reflected in the accompanying financial statements as contributions receivable and support in the appropriate net asset category. For promises expected to be collected in more than one year a present value discount is estimated based on the risk free rate (appropriate U.S. Treasury Bond Rate) at the time of the promise as adjusted for credit and other donor specific risks. The risk-adjusted discount rate on contributions receivable as of June 30, 2018, ranged between 1.8% and 2.9%.

4. NOTE RECEIVABLE - RELATED PARTY

Note receivable - related party consist of the following:

	2018	2017
Note receivable	\$ -	\$ 250,000



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4. NOTE RECEIVABLE - RELATED PARTY (continued)

In November 2009, the Museum entered into a secured note receivable with an officer of the Museum in the amount of \$250,000 for the purpose of purchasing a primary residence within the San Jose, California Metropolitan area. The note bore a fixed interest rate of 1.5%, but for income reporting purposes, the interest benefit was computed and reported to the Internal Revenue Service as part of the officer's benefit package. The maturity date of this note receivable was amended in connection with the separation agreement entered into with the officer in January 2017. Under the terms of the initial agreement, the note matured at the earlier of the date which is (i) six months after the effective date of the termination of the officer's employment by the Museum, or (ii) the date on which the officer ceases to use the primary residence as her principal or primary residence, or (iii) the date on which the officer closes escrow on a sale or otherwise effects a transfer or conveyance of the primary residence. Under the terms of the separation agreement, all unpaid principal and accrued and unpaid interest under the note receivable was received during the year ended June 30, 2018. Interest receivable on the note totaled \$0 and \$28,500 as of June 30, 2018 and 2017, respectively. Interest earned on the note totaled \$2,188 and \$3,750 for years ended June 30, 2018 and 2017, respectively.

5. INVESTMENTS

All of the following investments are classified as Level 1 investments (see Note 2). The fair value of investments as of June 30, was as follows:

	<u>2018</u>	<u>2017</u>
Unrestricted		
Equity securities	\$ 57,907	\$ -
Mutual funds	29,479	-
Fixed income securities	12,614	-
Total unrestricted	<u>100,000</u>	<u>-</u>
Temporarily restricted		
Temporarily restricted portion - unappropriated	<u>2,811,828</u>	<u>2,414,000</u>
Total temporarily restricted	<u>2,811,828</u>	<u>2,414,000</u>
Permanently restricted		
Equity securities	6,207,293	5,897,750
Mutual funds	3,288,265	2,679,560
Fixed income securities	1,146,762	1,267,182
Less: temporarily restricted portion - unappropriated	<u>(2,811,828)</u>	<u>(2,414,000)</u>
Total permanently restricted	<u>7,830,492</u>	<u>7,430,492</u>
Total	<u>\$ 10,742,320</u>	<u>\$ 9,844,492</u>

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5. INVESTMENTS (continued)

Investment earnings consist of the following:

	2018	2017
Net realized and unrealized gain	\$ 414,856	\$ 919,407
Interest and dividends	270,452	219,166
Distribution from beneficial interest in perpetual trust	69,747	70,133
	\$ 755,055	\$ 1,208,706

6. PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	2018	2017
Computer and media equipment	\$ 745,768	\$ 745,768
Leasehold improvements	613,310	613,310
Software	190,216	190,216
Furniture and fixtures	161,002	161,002
	1,710,296	1,710,296
Less: accumulated depreciation and amortization	(1,703,813)	(1,701,895)
	\$ 6,483	\$ 8,401

Depreciation and amortization expense for the years ended June 30, 2018 and 2017 was \$1,918 and \$2,723, respectively.

As detailed in Note 13 - in-kind rent and other in-kind support, the City of San Jose provides facilities for the Museum at no charge to the Museum. Improvements to the building made by the Museum have been recorded as leasehold improvements.

7. BENEFICIAL INTEREST IN PERPETUAL TRUST

In 1997, the Museum received a conditional promise to give from a foundation in the form of a challenge grant towards the Museum's endowment campaign. Under the challenge grant, the Museum was to receive the rights to future earnings on funds contributed by the foundation to an independent trustee. The trustee's responsibilities are to hold and invest the funds in perpetuity and pay the Museum a percentage of the annual income, on a total revenue basis, earned on the donated amount. In December 2002, the foundation notified the Museum that the campaign goal was met.

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7. BENEFICIAL INTEREST IN PERPETUAL TRUST (continued)

As of June 30, 2018, the Museum has recognized \$930,117 in permanently restricted net assets, representing the present value of the estimated future earnings to be received on the funds held by the trustee. The Museum's interest in the trust is classified as a Level 3 asset (see Note 2). The present value of estimated future earnings was determined using an average rate of return, net of trustee fees of 4% and discount rates of 3% to 6%. The valuation has not changed from year to year and the balance has been consistently reported at \$930,117. The actual fair value of the underlying assets in the perpetual trust at June 30, 2018, was \$1,471,516.

8. LINE OF CREDIT

The Museum renewed its \$500,000 unsecured line of credit with Heritage Bank on January 21, 2017. The line of credit bears interest commensurate with the bank's prime rate plus 0.5% (5.50% and 4.75% at June 30, 2018 and 2017, respectively). The line of credit expires on January 21, 2019. The Museum is required to comply with certain financial and reporting covenants under the terms of the line of credit agreement. As of June 30, 2018 and 2017, the Museum was in compliance with the reporting covenants. There were no amounts outstanding under the line of credit as of June 30, 2018 or 2017.

9. EMPLOYEE BENEFIT PLANS

The Museum makes contributions to a defined contribution 403(b) retirement plan for employees who have completed one year of service, and who have worked at least 1,000 hours during that year. Pension expense for the years ended June 30, 2018 and 2017, was \$81,329 and \$71,305, respectively.

The Museum had an incentive compensation plan covering certain key employees, which was replaced by the defined contribution 403(b) plan. Annual contributions to the plan were determined by the Executive Committee of the Board of Trustees.

10. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following:

	2018	2017
Endowment accumulated earnings - unappropriated	\$ 2,745,999	\$ 2,479,824
Exhibitions and education programs	619,577	1,268,720
Time restriction	503,295	344,075
Gala	268,600	196,672
Director's fund	-	5,413
Art acquisitions	-	3,511
	\$ 4,137,471	\$ 4,298,215

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10. TEMPORARILY RESTRICTED NET ASSETS (continued)

Temporarily restricted net assets released from restriction during the year were as follows:

	2018	2017
Exhibitions and education programs	\$ 1,281,523	\$ 1,190,313
Non-operating art acquisitions	547,479	248,727
Endowment appropriations for operations	483,979	498,676
Time restriction	356,865	125,000
Gala	269,300	284,873
Director's fund	5,413	-
	\$ 2,944,559	\$ 2,347,589

11. PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets consist of the following:

	2018	2017
Endowment funds	\$ 7,830,492	\$ 7,630,492
Beneficial interest in perpetual trust	930,117	930,117
	\$ 8,760,609	\$ 8,560,609

12. ENDOWMENT

San Jose Museum of Art Association's endowment consists of two individual funds (see Note 11). Its endowment includes donor-restricted endowment funds. As required by Generally Accepted Accounting Principles (GAAP), net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

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12. ENDOWMENT (continued)

Interpretation of relevant law

The Board of Trustees of San Jose Museum of Art Association has interpreted the California version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, San Jose Museum of Art Association 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 Museum in a manner consistent with the standard of prudence prescribed by the California version of UPMIFA. In accordance with the California version of UPMIFA, the Museum 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 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 policies of the Museum

Funds with deficiencies

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the permanently restricted net assets balance. There were no deficiencies of this nature that would be required to be reported in unrestricted net assets as of June 30, 2018 and 2017.

Investment return objectives, risk parameters and strategies

The primary objectives of the Fund are to support the operations of the Museum over time, while preserving the Fund's inflation-adjusted asset value. The current investment goals are to achieve average long-term total returns on assets (net of fees) that are at least 5.5% greater than the current annual inflation rate (as measured by the Consumer Price Index for All Urban Consumers, Not Seasonally Adjusted, or if that Index is discontinued, the most similar then existing Index), at acceptable risk levels.

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12. ENDOWMENT (continued)

Investment return objectives, risk parameters and strategies (continued)

A portfolio such as this, with a long-term investment time horizon, should hold a larger percentage of its assets in high-quality equities than in fixed-income securities. The short-term volatility of the return from stocks dictates that a percentage of the assets are invested in fixed-income securities and alternative investments that have low correlations with performance of equities, to provide an element of stability to the portfolio's return.

Performance of the investment strategy is monitored by comparing returns to a properly weighted, blended benchmark. Appropriate benchmark indices for evaluation of investment performance shall be selected in consultation with the Fund's investment manager(s). Current benchmarks are: domestic large-cap, S&P500; domestic mid-cap, S&P400; domestic small-cap, S&P600; international equities, MSCI World x U.S.; fixed income, Barclay's Bond Index; cash equivalents, and 3-month US Treasury Bill.

The Board understands that in order to seek to achieve the Fund's investment objectives, it must allocate Fund assets to diverse asset classes. Furthermore, the Board understands that, in general, assets with the highest potential for investment returns also have the highest investment risk.

Spending policy

San Jose Museum of Art Association shall maintain records of the initial contributed value of endowment gifts, and shall not expend any portion of the initial contributed value of any endowment gift subject to these Policies.

The Museum may expend any portion of the net income and/or growth in asset value of an endowment gift, which exceeds its initial contributed value, in such amounts as the Board determines. The Board of Trustees can at its discretion approve distributions from the Fund to support the operations of the Museum up to the amount of 5% of the Fund's principal balance per year if: a) such distributions do not conflict with the intent of any donors; and (b) such distributions do not result in a decline in the initial contributed value balance of the Fund. Only under exceptional circumstances should distributions greater than 5% be considered. Any such larger distributions must (a) meet the same guidelines outlined above, and (b) must also be approved by the full Board. The current distribution policy is to budget distributions for a new fiscal year at no more than 5% of the rolling-average for the eight quarters prior to the end of the previous calendar year.

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12. ENDOWMENT (continued)

Endowment composition

Endowment net asset composition by type of fund as of June 30, 2018, is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Board-designated endowment funds	\$ 100,000	\$ -	\$ -	\$ 100,000
Donor-restricted endowment funds	<u>-</u>	<u>2,745,999</u>	<u>8,760,609</u>	<u>11,506,608</u>
	<u>\$ 100,000</u>	<u>\$ 2,745,999</u>	<u>\$ 8,760,609</u>	<u>\$11,606,608</u>

Endowment net asset composition by type of fund as of June 30, 2017, is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	<u>\$ -</u>	<u>\$ 2,479,824</u>	<u>\$ 8,560,609</u>	<u>\$11,040,433</u>

Changes in endowment net assets for the fiscal year ended June 30, 2018, is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance, June 30, 2017	<u>\$ -</u>	<u>\$ 2,479,824</u>	<u>\$ 8,560,609</u>	<u>\$11,040,433</u>
Investment return				
Interest and dividends	-	265,551	-	265,551
Net realized gain	-	193,810	-	193,810
Net unrealized gain	<u>-</u>	<u>221,046</u>	<u>-</u>	<u>221,046</u>
Total investment return	-	680,407	-	680,407
Board-designated contributions	100,000	-	-	100,000
Contributions	-	-	200,000	200,000
Distribution from beneficial interest in perpetual trust	-	69,747	-	69,747
Amount appropriated for expenditure - operating	<u>-</u>	<u>(483,979)</u>	<u>-</u>	<u>(483,979)</u>
Balance, June 30, 2018	<u>\$ 100,000</u>	<u>\$ 2,745,999</u>	<u>\$ 8,760,609</u>	<u>\$11,606,608</u>

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12. ENDOWMENT (continued)

Endowment composition (continued)

Changes in endowment net assets for the fiscal year ended June 30, 2017, is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance, June 30, 2016	\$ -	\$ 1,775,957	\$ 8,360,609	\$10,136,566
Investment return				
Interest and dividends	-	213,003	-	213,003
Net realized gain	-	294,021	-	294,021
Net unrealized loss	-	625,386	-	625,386
Total investment return	-	1,132,410	-	1,132,410
Contributions	-	-	200,000	200,000
Distribution from beneficial interest in perpetual trust	-	70,133	-	70,133
Amount appropriated for expenditure	-	(498,676)	-	(498,676)
Balance, June 30, 2017	<u>\$ -</u>	<u>\$ 2,479,824</u>	<u>\$ 8,560,609</u>	<u>\$11,040,433</u>

13. IN-KIND RENT AND OTHER IN-KIND SUPPORT

The City of San Jose provides facilities for the Museum, the Museum's store, and administrative offices at no charge to the Museum under the terms and conditions of a fifty-five year agreement dated June 1988. The estimated fair value of rent for these facilities was \$2,340,000 and \$1,872,000 for the years ended June 30, 2018 and 2017, respectively. These amounts have been determined by an independent real estate professional and were recorded as support and expenses in the statement of activities for each of the years ended June 30, 2018 and 2017, respectively.

Donated services are recognized as contributions at their fair value, if the services (a) create or enhance non-financial assets or (b) require specialized skills, are performed by individuals possessing those skills, and would otherwise be purchased by the Museum if not provided by donations. Donated services and supplies of \$315,767 and \$329,180 have been recognized as in-kind support in the statement of activities for the years ended June 30, 2018 and 2017, respectively.

In addition, a substantial number of corporations and individual volunteers have donated significant amounts of time and performed a variety of tasks related to the Museum's program operations and fundraising campaigns, which do not meet the criteria for recognition as donated services. Accordingly, no amounts have been recognized for these services in the accompanying financial statements.



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13. IN-KIND RENT AND OTHER IN-KIND SUPPORT (continued)

The following in-kind contributions received by the Museum were as follows:

	2018	2017
In-kind rent	<u>\$ 2,340,000</u>	<u>\$ 1,872,000</u>
Other in-kind support		
Volunteer services	267,927	275,730
Museum parking spaces	32,400	27,000
Cloud subscription services	15,000	15,000
Pro bono professional services	440	11,450
	<u>315,767</u>	<u>329,180</u>
Special events in-kind support		
Special event auction items to be sold	199,295	124,366
	<u>199,295</u>	<u>124,366</u>
	<u>\$ 2,855,062</u>	<u>\$ 2,325,546</u>

14. CONCENTRATIONS

The Museum had contributions receivable from Board members totaling \$399,875 and \$706,791 at June 30, 2018 and 2017, respectively. Contribution support for the years ended June 30, 2018 and 2017, included \$1,164,680 and \$465,475, respectively, received from Board members.