

Financial Statements

Palm Springs Art Museum, Inc.

September 30, 2016 and 2015

Maryanov Madsen Gordon & Campbell
CERTIFIED PUBLIC ACCOUNTANTS - A Professional Corporation

INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
Palm Springs Art Museum, Inc.

We have audited the accompanying financial statements of Palm Springs Art Museum, Inc., (a California nonprofit corporation), which comprise the statements of financial position as of September 30, 2016 and 2015, and the related statements of activities and changes in net assets and cash flows for the years 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits 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 auditors' 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.

To the Board of Trustees of
Palm Springs Art Museum, Inc.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Palm Springs Art Museum, Inc. as of September 30, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Maryann Madsen Gordon & Campbell

Palm Springs, California
February 24, 2017

PALM SPRINGS ART MUSEUM, INC.

STATEMENTS OF FINANCIAL POSITION
SEPTEMBER 30, 2016 AND 2015

<u>ASSETS</u>	<u>2016</u>	<u>2015</u>
Cash and cash equivalents - unrestricted	\$ 196,531	\$ 346,153
Cash and cash equivalents - proceeds from deaccessioned art sales restricted for art purchases	268,265	1,804
Cash and cash equivalents - restricted for Edwards Harris Center renovations	-	2,304
Cash and cash equivalents - restricted for endowment	1,544,005	892,436
Investments	14,433,531	14,924,995
Accounts and interest receivable	10,007	271,213
Grants receivable	20,000	25,978
Pledges/bequests receivable, net of allowance of \$12,000 and \$12,000, respectively	4,003,965	5,708,486
Inventories	240,828	252,598
Prepaid expenses and deposits	347,997	585,536
Charitable remainder trusts receivable	2,318,893	2,235,408
Collections	-	-
Land, buildings, and equipment, net of accumulated depreciation	15,693,587	15,068,228
Construction in progress	37,474	22,576
	<u>39,115,083</u>	<u>40,337,715</u>
Total assets	<u>\$ 39,115,083</u>	<u>\$ 40,337,715</u>
<u>LIABILITIES AND NET ASSETS</u>		
Accounts payable and accrued liabilities	\$ 613,426	\$ 671,529
Line of credit	1,350,000	1,010,000
Deferred revenue	250,002	585,700
	<u>2,213,428</u>	<u>2,267,229</u>
Total liabilities	<u>2,213,428</u>	<u>2,267,229</u>
NET ASSETS		
Unrestricted	8,368,204	8,211,458
Temporarily restricted	5,459,805	6,045,575
Permanently restricted	23,073,646	23,813,453
	<u>36,901,655</u>	<u>38,070,486</u>
Total net assets	<u>36,901,655</u>	<u>38,070,486</u>
	<u>\$ 39,115,083</u>	<u>\$ 40,337,715</u>

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

PALM SPRINGS ART MUSEUM, INC.

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS
YEAR ENDED SEPTEMBER 30, 2016

	Unrestricted Fund	Temporarily Restricted Fund	Permanently Restricted Fund	Total All Funds
OPERATING REVENUES AND OTHER SUPPORT				
Contributions and grants	\$ 3,949,406	\$ 1,662,914	\$ 27,632	\$ 5,639,952
Admissions	830,469	-	-	830,469
Memberships	973,804	18,810	-	992,614
Fundraising events	77,928	-	-	77,928
Exhibits and programs	562,032	22,755	-	584,787
Endowment support for current activities	1,160,603	16,641	-	1,177,244
Museum store	906,522	-	-	906,522
Facility use fees	322,347	-	-	322,347
Other	23,650	-	-	23,650
Satisfaction of program restrictions	<u>2,864,186</u>	<u>(1,864,186)</u>	<u>(1,000,000)</u>	<u>-</u>
Total operating revenues and other support	<u>11,670,947</u>	<u>(143,066)</u>	<u>(972,368)</u>	<u>10,555,513</u>
OPERATING EXPENSES				
Program services	7,368,071	-	-	7,368,071
Management and general	1,563,877	-	-	1,563,877
Fundraising and membership	<u>1,458,333</u>	<u>-</u>	<u>-</u>	<u>1,458,333</u>
Total operating expenses	<u>10,390,281</u>	<u>-</u>	<u>-</u>	<u>10,390,281</u>
CHANGES IN NET ASSETS BEFORE DEPRECIATION	1,280,666	(143,066)	(972,368)	165,232
DEPRECIATION	<u>775,996</u>	<u>-</u>	<u>-</u>	<u>775,996</u>
CHANGES IN NET ASSETS FROM OPERATING EXPENSES	<u>504,670</u>	<u>(143,066)</u>	<u>(972,368)</u>	<u>(610,764)</u>
NON-OPERATING REVENUES AND EXPENSES				
Investment return more (less) than endowment support for current activities	(273,587)	126,253	-	(147,334)
Investment management fees	(79,516)	(12,799)	-	(92,315)
Proceeds (loss) from sale of collections	-	(265,525)	272,650	7,125
Purchases of collections	-	-	(409,028)	(409,028)
Change in value - charitable remainder trusts	5,179	-	78,306	83,485
Satisfaction of program restrictions	<u>-</u>	<u>(290,633)</u>	<u>290,633</u>	<u>-</u>
CHANGES IN NET ASSETS FROM NON-OPERATING ACTIVITIES	<u>(347,924)</u>	<u>(442,704)</u>	<u>232,561</u>	<u>(558,067)</u>
CHANGES IN NET ASSETS	<u>\$ 156,746</u>	<u>\$ (585,770)</u>	<u>\$ (739,807)</u>	<u>\$ (1,168,831)</u>
NET ASSETS, beginning of year (as restated)	\$ 8,211,458	\$ 6,045,575	\$ 23,813,453	\$ 38,070,486
CHANGE IN NET ASSETS	<u>156,746</u>	<u>(585,770)</u>	<u>(739,807)</u>	<u>(1,168,831)</u>
NET ASSETS, end of year	<u>\$ 8,368,204</u>	<u>\$ 5,459,805</u>	<u>\$ 23,073,646</u>	<u>\$ 36,901,655</u>

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

PALM SPRINGS ART MUSEUM, INC.

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS
YEAR ENDED SEPTEMBER 30, 2015

	Unrestricted Fund	Temporarily Restricted Fund	Permanently Restricted Fund	Total All Funds
OPERATING REVENUES AND OTHER SUPPORT				
Contributions and grants	\$ 3,553,993	\$ 2,989,607	\$ 64,511	\$ 6,608,111
Admissions	855,769	-	-	855,769
Memberships	1,080,036	90,780	-	1,170,816
Fundraising events	59,842	-	-	59,842
Exhibits and programs	439,866	16,752	-	456,618
Endowment support for current activities	1,065,415	56,361	-	1,121,776
Museum store and auction sales	1,305,831	4,682	-	1,310,513
Facility use fees	259,419	-	-	259,419
Other	12,450	-	-	12,450
Satisfaction of program restrictions	<u>3,532,205</u>	<u>(3,532,205)</u>	<u>-</u>	<u>-</u>
Total operating revenues and other support	<u>12,164,826</u>	<u>(374,023)</u>	<u>64,511</u>	<u>11,855,314</u>
OPERATING EXPENSES				
Program services	7,861,678	-	-	7,861,678
Management and general	1,501,151	-	-	1,501,151
Fundraising and membership	<u>1,853,821</u>	<u>-</u>	<u>-</u>	<u>1,853,821</u>
Total operating expenses	<u>11,216,650</u>	<u>-</u>	<u>-</u>	<u>11,216,650</u>
CHANGES IN NET ASSETS BEFORE DEPRECIATION	948,176	(374,023)	64,511	638,664
DEPRECIATION	<u>699,960</u>	<u>-</u>	<u>-</u>	<u>699,960</u>
CHANGES IN NET ASSETS FROM OPERATING EXPENSES	<u>248,216</u>	<u>(374,023)</u>	<u>64,511</u>	<u>(61,296)</u>
NON-OPERATING REVENUES AND EXPENSES				
Investment return more (less) than endowment support for current activities	(1,394,093)	(113,257)	-	(1,507,350)
Investment management fees	(77,310)	(13,585)	-	(90,895)
Proceeds from sale of collections	-	246,894	-	246,894
Purchases of collections	-	-	(822,500)	(822,500)
Change in value - charitable remainder trusts	2,505	-	(34,303)	(31,798)
Satisfaction of program restrictions	<u>527,117</u>	<u>(527,117)</u>	<u>-</u>	<u>-</u>
CHANGES IN NET ASSETS FROM NON-OPERATING ACTIVITIES	<u>(941,781)</u>	<u>(407,065)</u>	<u>(856,803)</u>	<u>(2,205,649)</u>
CHANGES IN NET ASSETS (as restated)	<u>\$ (693,565)</u>	<u>\$ (781,088)</u>	<u>\$ (792,292)</u>	<u>\$ (2,266,945)</u>
NET ASSETS, beginning of year	\$ 8,905,023	\$ 6,826,663	\$ 24,605,745	\$ 40,337,431
CHANGE IN NET ASSETS (as restated)	<u>(693,565)</u>	<u>(781,088)</u>	<u>(792,292)</u>	<u>(2,266,945)</u>
NET ASSETS, end of year	<u>\$ 8,211,458</u>	<u>\$ 6,045,575</u>	<u>\$ 23,813,453</u>	<u>\$ 38,070,486</u>

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

PALM SPRINGS ART MUSEUM, INC.

STATEMENT OF CASH FLOWS
YEAR ENDED SEPTEMBER 30, 2016

	<u>Total All Funds</u>
CHANGES IN NET ASSETS	\$ (1,168,831)
Adjustments to reconcile change in net assets to net cash used by operating activities:	
Depreciation	775,996
Donated real estate	(1,020,000)
Unrealized (gain) loss on investment transactions	(666,257)
Unrealized (gain) loss on charitable remainder trusts	(83,485)
(Increase) decrease in assets:	
Accounts and interest receivable	261,206
Grants receivable	5,978
Pledges/bequests receivable	1,704,521
Inventories	11,770
Prepaid expenses and deposits	237,539
Increase (decrease) in liabilities:	
Accounts payable and accrued liabilities	(58,103)
Deferred revenue	(335,698)
Net cash used by operating activities	<u>(335,364)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:	
Purchase of fixed assets	(381,355)
Increase in construction in progress	(14,898)
Purchase of investments	(4,845,571)
Sale of investments	<u>6,003,292</u>
Net cash provided by investing activities	<u>761,468</u>
CASH FLOWS FROM FINANCING ACTIVITIES:	
Advances from line of credit	1,800,000
Repayments on line of credit	<u>(1,460,000)</u>
Net cash provided by financing activities	<u>340,000</u>
Net increase in cash and cash equivalents	766,104
Cash and cash equivalents at beginning of year	<u>1,242,697</u>
Cash and cash equivalents at end of year	<u>\$ 2,008,801</u>
CASH AND CASH EQUIVALENTS CONSISTS OF:	
Unrestricted	\$ 196,531
Restricted	<u>1,812,270</u>
	<u>\$ 2,008,801</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOWS INFORMATION	
Interest paid - expense	<u>\$ 26,661</u>

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

PALM SPRINGS ART MUSEUM, INC.

STATEMENT OF CASH FLOWS
YEAR ENDED SEPTEMBER 30, 2015

	<u>Total All Funds</u>
CHANGES IN NET ASSETS	\$ (2,266,945)
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation	699,960
Unrealized (gain) loss on investment transactions	747,612
Unrealized (gain) loss on charitable remainder trusts	31,798
(Increase) decrease in assets:	
Accounts and interest receivable	(262,090)
Grants receivable	14,022
Pledges/bequests receivable	2,771,464
Inventories	(73,927)
Prepaid expenses and deposits	317,751
Deferred compensation asset	161,820
Increase (decrease) in liabilities:	
Accounts payable and accrued liabilities	(1,397,115)
Deferred compensation liability	(161,820)
Deferred revenue	179,594
Net cash provided by operating activities	<u>762,124</u>
CASH FLOWS FROM INVESTINGS ACTIVITIES:	
Purchase of fixed assets	(4,318,484)
Decrease in construction in progress	3,509,212
Purchase of investments	(9,912,146)
Sale of investments	<u>8,840,459</u>
Net cash used by investing activities	<u>(1,880,959)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:	
Advances from line of credit	2,232,111
Repayments on line of credit	<u>(2,692,111)</u>
Net cash used by financing activities	<u>(460,000)</u>
Net decrease in cash and cash equivalents	(1,578,835)
Cash and cash equivalents at beginning of year	<u>2,821,532</u>
Cash and cash equivalents at end of year	<u>\$ 1,242,697</u>
CASH AND CASH EQUIVALENTS CONSISTS OF:	
Unrestricted	\$ 346,153
Restricted	<u>896,544</u>
	<u>\$ 1,242,697</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOWS INFORMATION	
Interest paid - expense	<u>\$ 43,307</u>

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

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Organization

The Palm Springs Art Museum, Inc. (the "Museum") was incorporated in the state of California on October 13, 1938, as a nonprofit corporation. At its founding, the Museum focused on the natural sciences. By the late 1950's, primarily through gifts from trustees and bequests from area residents, the Museum had acquired a modest collection of modern artworks in addition to its significant holdings of regional native American cultural artifacts. In the early 1970's, the Museum relinquished control of its 230-acre wildlife sanctuary in Palm Desert, to a new entity called "The Living Desert". In 1976, the Museum moved to a new facility on Museum Drive and continued a dual focus on art and the natural sciences, as well as performing arts in the 430-seat Annenberg Theater. In 1996, art became a more dominant focus with the bequest of Steve Chase's extensive collection of art and design objects, as well as funds to add the Steve Chase wing, which expanded the Museum Drive facility to 132,000 square feet. In 2004, the Board of Trustees (the "Board") shifted the focus of the Museum from a multi-disciplinary museum to a world-class art museum with a vibrant performing arts program. Natural history and science collections were distributed to appropriate institutions around the Coachella Valley, most notably the Living Desert.

The Museum expanded beyond its Museum Drive facility with the bequest of Albert Frey's iconic home "Frey House II" to the Museum in 1999. In 2012, the Museum opened an additional exhibition and education facility in Palm Desert in an 8,400 square foot, Silver LEED-certified building named "The Galen", which is surrounded by the four-acre Faye Sarkowsky Sculpture Garden. In 2014, the Museum renovated a 10,775 square foot classic midcentury modern commercial bank building in downtown Palm Springs and opened it as the Palm Springs Art Museum Architecture and Design Center, Edwards Harris Pavilion.

As one of the leading cultural institutions in the Coachella Valley, the Museum continues to expand its collections of Native American and Mesoamerican art, Western art, international modern and contemporary art, contemporary glass, photography and video, and architecture and design, presenting exhibitions, educational programs, and performing arts.

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Fund Accounting and Description of Funds

To ensure observance of limitations and restrictions placed on the use of resources available to the Museum, the accounts of the Museum are maintained in accordance with the principles of fund accounting. This is the procedure by which resources for various purposes are classified for accounting and reporting purposes into funds established according to their nature and purpose. Separate accounts are maintained for each fund; however, in the accompanying financial statements, funds that have similar characteristics have been combined into fund groups as follows:

The Unrestricted Fund represents all resources over which the Board has discretionary control for use in operating the Museum, as well as all land, buildings, and equipment of the Museum.

The Temporarily Restricted Fund represents those resources that are received with temporary stipulations that limit the use of the donated assets. When a restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

The Permanently Restricted Fund represents funds that are subject to permanent restriction by the donor requiring that the principal be invested and only the income be used for unrestricted purposes.

Contributions

Contributions, including unconditional promises to give (pledges), are recorded upon the date of donation or the promise to give. All contributions are available for unrestricted use unless specifically restricted by the donor. Conditional promises to give are recognized when the conditions on which they depend are substantially met. Unconditional promises to give are reported at net realizable value if at the time the promise is made payment is expected to be received in one year or less. Unconditional promises that are expected to be collected in more than one year are reported at fair value initially and in subsequent periods, in accordance with generally accepted accounting principles. These unconditional promises to give are discounted using the risk-free rate of return for the applicable time period, which management has determined ranges from 0.33% to 1.46%. Contribution receivables are reported net of the discount against long-term receivables in the notes to the financial statements.

Allowance for Doubtful Accounts

The Museum uses the allowance method to account for doubtful pledges and accounts.

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Membership Dues

Membership dues are recorded as revenue in the year the dues apply.

Cash Equivalents

The Museum considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Investments

The Museum carries investments in marketable securities with readily determinable fair values and all investments in debt securities at their fair values in the statement of financial position. Unrealized gains and losses are included in the change in net assets in the accompanying statement of activities.

Inventories

Inventories are stated at the lower of cost or market, with cost determined using the first-in, first-out method.

Collections

The Museum's collections comprise more than 11,300 objects and works of art including sculptures, paintings, drawings, graphics, photographs, ceramics, and contemporary glass; Native American baskets, weavings, pottery and artifacts; Mesoamerican artifacts; and architectural drawings and archives. In addition, it includes the Stephen Willard Photography Archives and the Bill Anderson Photographic Archives, totaling more than 50,000 images and archival materials. The collections are maintained for public exhibition, education, research, and the furtherance of public service rather than for financial gain. The Museum's collections, acquired through donations and through purchases, are not recognized as assets in the accompanying financial statements. Purchases of collection items are recorded as decreases in the appropriate net asset classification in the year of acquisition. Contributed collection items are not reflected in the financial statements. Proceeds from the sale of art are recorded as increases in the appropriate net asset classification in the year of sale and are reserved for the acquisition of works of art.

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Land, Buildings and Equipment

Land, buildings and equipment are recorded at cost, or in the case of donated items, at estimated value on the date of donation. Maintenance and repairs are expensed when incurred. The costs of betterments or improvements which are greater than \$5,000 and materially extend the useful lives of the assets are capitalized. Proceeds from the sale of fixed assets are recorded in the unrestricted fund. Depreciation is provided using the straight-line method over estimated useful lives. Construction in progress is recorded as construction occurs. Upon completion of a capital project the asset is placed in service and depreciation begins.

Charitable Remainder Trusts

Assets under charitable remainder trust wherein the Museum is not the trustee are recorded as contributions receivable from remainder trust and contributions revenue in the period in which the trust is created. The Museum's beneficial interest is measured by the present value of estimated future distribution expected to be received by the Museum. The accretion of the discount, revaluation of the present value of the estimated future payments to the beneficiaries, and changes in actuarial assumptions are recorded separately in the statement of activities.

Contributed Services

A substantial number of unpaid volunteers have made significant contributions of their time to Museum programs, operations and fundraising activities. The value of donated volunteer services is not reflected in the accompanying financial statements since no objective basis is available to measure the value of such services.

Income Taxes

The Museum is exempt from federal income and California franchise taxes under Section 501(c)(3) of the Internal Revenue Code ("IRC") and Section 23701(d) of the State Revenue and Taxation Code, respectively.

The Museum's policy is to record income tax related interest and penalties in operating expenses. For the year ended September 30, 2016, there was no interest or penalties expense recorded and no accrued interest or penalties.

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes (Continued)

The Museum's Forms 990, Return of Organization Exempt from Income Tax, are subject to examination by the Internal Revenue Service, generally for three years after they are filed. The Museum's Forms 199, California Exempt Organization Annual Information Return, are subject to examination by the Franchise Tax Board, generally for four years after they are filed. Management has reviewed tax positions for open years and has determined that a provision for uncertain tax positions is not required.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Fair Value of Financial Instruments

U.S. generally accepted accounting principles ("GAAP") have established a framework to measure fair value, and defined the required disclosures about fair value measurements. Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 820, *Fair Value Measurements and Disclosures*, favors the use of market-based information over entity-specific information. The standard prescribes a three-level hierarchy for fair value measurements based on the transparency of information, such as the pricing source, used in the valuation of an asset as of the measurement date.

Investments measured and reported at fair value are classified and disclosed in one of the following categories. There have been no changes in the techniques and inputs used at September 30, 2016 and 2015.

Level I Inputs - Quoted prices are available in active markets for identical investments as of the reporting date.

Level II Inputs - Pricing inputs are available in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.

Level III Inputs - Pricing inputs are unobservable and determination of fair value requires significant management judgment or estimation.

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Functional Allocation of Expenses

The costs of providing various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Measure of Operations

The Museum includes in its measure of operations all revenue and expenses that are integral to its programs and supporting activities. The measure of operations includes investment income according to the Museum's spending policy, as detailed in Note 1. The measure of operations excludes investment return in excess of/less than amounts made available for current support, purchase and sale of museum collection items and releases of net assets from restrictions related to non-operating items.

Advertising Costs

Advertising costs are expensed as incurred by the Museum. Total advertising costs for the years ended September 30, 2016 and 2015 were \$246,795 and \$240,179, respectively.

Reclassifications

Certain accounts in the prior-year financial statements have been reclassified for comparative purposes to conform to the presentation in the current-year financial statements.

Subsequent Events

Subsequent events have been evaluated through February 24, 2017, which is the date the financial statements were available to be issued.

NOTE 1: VALUATION OF INVESTMENTS

The majority of the investments are managed by the Museum's investment portfolio managers in accordance with the Museum's investment policies and objectives, therefore the investment mix changes frequently and investments are regularly bought and sold to meet the objectives of the investments.

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 1: VALUATION OF INVESTMENTS (Continued)

Investments at September 30, 2016 and 2015, stated at fair value, using Level I inputs, based on quoted market prices are summarized as follows:

	<u>Total All Funds</u>	
	<u>2016</u>	<u>2015</u>
Common stock	\$ 5,736,348	\$ 5,131,015
Exchange-traded funds	1,735,375	2,966,227
Mutual funds	1,225,913	1,769,046
Government securities	305,708	211,194
Corporate bonds	1,728,603	1,297,650
Certificates of deposit	3,005,825	2,657,906
Real assets	224,771	364,880
Complimentary strategic investments	<u>470,988</u>	<u>527,077</u>
Total investments	14,433,531	14,924,995
Cash held in brokerage accounts	<u>1,544,005</u>	<u>892,436</u>
Total brokerage balance	<u>\$15,977,536</u>	<u>\$15,817,431</u>

The Board approved and budgeted for \$1,177,244 and \$512,000 for endowment support of current operations for the years ended September 30, 2016 and 2015, respectively. During fiscal year 2015, the Board approved \$609,776 of additional endowment support for the year ended September 30, 2015. The approved and budgeted spending rate for current operations is described in Note 14. The following schedule summarizes the investment return and its classification in the statement of activities.

	<u>2016</u>		
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Dividends and interest	\$ 313,181	\$ 50,472	\$ 363,653
Net realized and unrealized gains	573,835	92,422	666,257
Investment management fees	<u>(79,516)</u>	<u>(12,799)</u>	<u>(92,315)</u>
Total return on investments	807,500	130,095	937,595
Investment return budgeted for current operations	<u>(1,160,603)</u>	<u>(16,641)</u>	<u>(1,177,244)</u>
Investment return more (less) than endowment support and investment management fees	<u>\$ (353,103)</u>	<u>\$ 113,454</u>	<u>\$ (239,649)</u>

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 1: VALUATION OF INVESTMENTS (Continued)

	2015		
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Dividends and interest	\$ 307,865	\$ 54,173	\$ 362,038
Net realized and unrealized losses	(636,543)	(111,069)	(747,612)
Investment management fees	<u>(77,310)</u>	<u>(13,585)</u>	<u>(90,895)</u>
Total return on investments	(405,988)	(70,481)	(476,469)
Investment return budgeted for current operations	(455,639)	(56,361)	(512,000)
Additional endowment draw	<u>(609,776)</u>	<u>-</u>	<u>(609,776)</u>
Investment return less than endowment support and investment management fees	<u>\$(1,471,403)</u>	<u>\$ (126,842)</u>	<u>\$(1,598,245)</u>

NOTE 2: UNCONDITIONAL PROMISES TO GIVE

Unconditional promises to give are due to be paid as follows:

	Total All Funds	
	<u>2016</u>	<u>2015</u>
Pledges, grants, and bequests receivable in less than one year	\$ 2,036,106	\$ 2,242,769
Pledges, grants, and bequests receivable in one to five years	1,342,247	2,875,195
Pledges, grants, and bequests receivable in more than five years	<u>735,337</u>	<u>735,337</u>
Total unconditional promises to give	4,113,690	5,853,301
Less unamortized discount	(77,725)	(106,837)
Less allowance for doubtful pledges	<u>(12,000)</u>	<u>(12,000)</u>
	<u>\$ 4,023,965</u>	<u>\$ 5,734,464</u>
Balance consists of the following:		
Grants receivable	\$ 20,000	\$ 25,978
Pledges/bequests receivable	<u>4,003,965</u>	<u>5,708,486</u>
	<u>\$ 4,023,965</u>	<u>\$ 5,734,464</u>

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 2: UNCONDITIONAL PROMISES TO GIVE (Continued)

The table below presents information about changes in unconditional promises to give for the years ended September 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Beginning balance	\$ 5,734,464	\$ 8,519,950
New promises to give	341,845	288,909
Payments	<u>(2,052,344)</u>	<u>(3,074,395)</u>
Ending balance	<u>\$ 4,023,965</u>	<u>\$ 5,734,464</u>

NOTE 3: CHARITABLE REMAINDER TRUSTS

The Museum is the beneficiary of three charitable remainder trusts that are administered by unrelated third parties. A charitable remainder trust provides for the payments of distributions to the grantor or other designated beneficiaries over the trust's term (usually the designated beneficiary's lifetime). At the end of the trust's term, the remaining assets are available for the Museum's use.

The portion of the trust attributable to the present value of the future benefits to be received by the Museum was recorded in the statement of activities in the period the trust was established. On an annual basis, the Museum revalues the present value of the future benefits to be received by the Museum based on actuarial assumptions. Valuations are based on the donor's life expectancy and a discount rate of 4.8%. The charitable remainder trusts are stated at fair value using Level III inputs based on the present value of future benefits to be received by the Museum which was estimated to be \$2,318,893 and \$2,235,408 at September 30, 2016 and 2015, respectively. These amounts are reported as contributions receivable in the statements of financial position.

The table below presents information about the changes in the contribution receivable-charitable remainder trusts, which are measured at fair value on a recurring basis using significant unobservable inputs:

	<u>2016</u>	<u>2015</u>
Beginning balance	\$ 2,235,408	\$ 2,267,206
Change in value of beneficial interest	<u>83,485</u>	<u>(31,798)</u>
Ending balance	<u>\$ 2,318,893</u>	<u>\$ 2,235,408</u>

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 4: COLLECTIONS

The following amounts are the purchase price, or the fair market value, at the time of the gift to the Museum at September 30:

	<u>2016</u>	<u>2015</u>
Art	\$62,706,267	\$61,123,919
Anthropology	1,893,698	1,893,698
Reserve	2,776,155	2,775,955
Frey House	519,552	416,158
Library, archives and other items	734,007	297,957
Items held for deaccession	<u>460,833</u>	<u>246,433</u>
	<u>\$69,090,512</u>	<u>\$66,754,120</u>

Collection items consist of art objects that are held for educational and curatorial purposes. Each of the items is cataloged, preserved, kept unencumbered, and cared for. Activities verifying their existence and assessing their condition are performed continuously. Collection items acquired either through purchase or donation are not capitalized. Purchases of collection items are recorded as decreases in unrestricted net assets if purchased with unrestricted assets and as decreases in temporarily restricted or permanently restricted net assets if purchased with donor-restricted assets. Contributions of collection items are not recognized in the statement of activities. Proceeds from deaccessions or insurance recoveries are reflected in the statement of activities based on the absence or existence and nature of donor-imposed restrictions.

The fair market values of the works acquired through contributions were \$1,961,615 (unaudited) and \$5,330,313 (unaudited) during the years ended September 30, 2016 and 2015, respectively.

Proceeds from the sale of deaccessioned items were \$272,650 and \$246,894, for the years ended September 30, 2016 and 2015, respectively. Collections purchased were \$409,028 and \$822,500 during the years ended September 30, 2016 and 2015, respectively.

As part of a plan approved by the Board in June 2005, works of art not deemed to be strategic were deaccessioned from the collection. It was agreed by the Board that deaccessioning proceeds would be credited to the art acquisition account. The Board also approved the use of net cash surpluses in the art acquisition account to repay external debt for a limited time, and that the borrowings from the account would be repaid over time. The deaccessioning procedures were discussed with the American Association of Museums and with the Accreditation Committee in February 2007, and such practices confirmed by such organizations as being appropriate and consistent with "best practices".

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 4: COLLECTIONS (Continued)

Funds were then borrowed from the Art Acquisition account to repay the Museum's external debts. As of September 30, 2016 and 2015, a balance of \$831,000 remains to be reimbursed to the Art Acquisition account as funds become available. Commencing in 2007, it was determined by the Board that any new deaccessioned funds raised by the Museum would be maintained in a segregated account and would be strictly for the acquisition of works of art. As of September 30, 2016, all proceeds from the sale of new deaccessioned art were either expended for the purchase of art or remain in the segregated account.

NOTE 5: EMPLOYEE BENEFIT PLANS

The Museum sponsors a 401(k) retirement plan covering substantially all employees who are at least 21 years of age and have one year of service. The plan provides for both employer and employee contributions. Safe harbor employer contributions are made to the plan based on 3% of each employee's eligible compensation. Additionally, the Museum contributes a discretionary match covering specified eligible employees after one year of service. Employer contributions are made to the plan based on 1% of each employee's eligible compensation. Employer contributions to the plan for the years ended September 30, 2016 and 2015 were \$92,356 and \$92,311, respectively.

In January 2008, the Museum established a deferred compensation plan under section 457(f) of the IRC. The plan covers certain employees of the Museum. Employer contributions to the plan are made in accordance with the plan agreement. Contributions to the plan were \$0 for the years ended September 30, 2016 and 2015, with a balance of \$0 for the years ended September 30, 2016 and 2015.

NOTE 6: LAND, BUILDINGS, AND EQUIPMENT

Land, buildings, and equipment are summarized as follows at September 30:

	<u>Total All Funds</u>	
	<u>2016</u>	<u>2015</u>
Land	\$ 1,798,000	\$ 1,798,000
Buildings and improvements	21,993,723	20,916,431
Equipment and furnishings	6,729,150	6,405,087
Site development	<u>160,431</u>	<u>160,431</u>
	30,681,304	29,279,949
Less accumulated depreciation	<u>(14,987,717)</u>	<u>(14,211,721)</u>
	<u>\$ 15,693,587</u>	<u>\$ 15,068,228</u>

Buildings are depreciated over estimated useful lives ranging from 25 to 50 years. Building improvements, equipment, and furnishings are depreciated over estimated useful lives ranging from four to 10 years.

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 7: CONSTRUCTION IN PROGRESS

Marks Vault Conversion

During the year ended September 30, 2016, the Museum has expended \$28,724 on the conversion of the Marks Vault. The project is estimated to be completed in March 2017.

Museum Lobby Renovation

During the year ended September 30, 2016, the Museum has expended \$8,750 on the renovation of the Museum lobby. The project is estimated to be completed in February 2017.

NOTE 8: LINE OF CREDIT

The Museum has a business line of credit with Wells Fargo Bank in the amount of \$3,000,000 secured by a first trust deed on the land and buildings and a maturity date of March 15, 2017. The line of credit bears a variable interest rate of the LIBOR rate plus 3.25%. For the years ended September 30, 2016 and 2015, the total rate was 4.00%. The balance on the line of credit was \$1,350,000 and \$1,010,000 as of September 30, 2016 and 2015, respectively.

NOTE 9: DEFERRED REVENUE

Deferred revenue is comprised of prepayments for future program fees, memberships, and museum events. At September 30, 2016 and 2015 the deferred revenue balance was \$250,002 and \$585,700, respectively.

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 10: ASSETS RELEASED FROM RESTRICTIONS

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors. The total assets released from restriction were as follows:

	<u>2016</u>	<u>2015</u>
Restrictions accomplished:		
<u>Operating</u>		
Architecture and Design Center	\$ 404,447	\$ 955,479
Time restrictions	438,239	2,355,838
Program completion and other	1,021,500	220,888
Donor changed restriction	<u>1,000,000</u>	<u>-</u>
Total – Operating	<u>\$ 2,864,186</u>	<u>\$ 3,532,205</u>
<u>Non-Operating</u>		
Fixed asset purchases	\$ -	\$ 527,117
Collection purchases	<u>290,633</u>	<u>-</u>
Total – Non-Operating	<u>\$ 290,633</u>	<u>\$ 527,117</u>

NOTE 11: LEASE COMMITMENTS

The Museum leases certain office equipment under operating lease agreements expiring at various dates through the year 2022. The Museum also rents storage space under month to month agreements.

Minimum required future rental payments under leases as of September 30, 2016 are:

<u>Years Ending September 30</u>	<u>Amount</u>
2017	\$ 31,506
2018	31,213
2019	21,237
2020	4,087
Thereafter	<u>1,842</u>
	<u>\$ 89,885</u>

Rental expenses for those leases were \$59,050 and \$51,474 for the years ended September 30, 2016 and 2015, respectively.

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 12: COMMITMENTS

On November 1, 2010, the Museum signed a 5-year lease with an option to renew for 5 consecutive 5-year periods for the former Visitor's Center in Palm Desert, at the rate of \$1/year, to be called the Palm Springs Art Museum - Palm Desert. This agreement was renewed on August 27, 2015 for another 5 years.

NOTE 13: CONCENTRATION OF CREDIT RISK

The Museum maintains its cash accounts at Wells Fargo Bank. Those accounts may have exceeded the amount guaranteed by the Federal Deposit Insurance Corporation ("FDIC") up to \$250,000, during the fiscal year.

The Museum also maintains accounts with TD Ameritrade, Goldman Sachs, and Wells Fargo. The accounts contain cash and securities and sometimes exceed the amount guaranteed by the Securities Investor Protection Corporation ("SIPC") which is \$500,000 for securities and cash (including a limit of \$250,000 for cash only). Accounts held in the same capacity are combined for purposes of the SIPC protection limits. Each investment company maintains insurance to guarantee the Museum's balances in excess of the amounts on deposit or invested.

NOTE 14: DONOR DESIGNATED FUNDS

The Museum's endowment consists of funds established for a variety of purposes. Its endowment consists solely of donor-restricted funds. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absences of donor-imposed restrictions.

The Board has interpreted 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.

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 14: DONOR DESIGNATED FUNDS (Continued)

As a result of this interpretation, the Museum classified 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 funds that is not classified in permanently restricted net assets may be 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 UPMIFA. In accordance with UPMIFA, the Museum considers the following factors in making a determination to appropriate or accumulate donor-restricted funds: (1) the duration and preservation of the various funds, (2) the purposes of the donor-restricted funds, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments (6) other resources of the Museum, and (7) the Museum's investment policies.

During the year ended September 30, 2016, a donor released the restriction on her \$1,000,000 payment to the Museum's current operating budget. The donor's initial 2013 pledge amount of \$5,000,000 was originally permanently restricted.

Distribution Policy

The Museum has a policy of appropriating for distribution, approved annually by the finance committee, 4%-5% of investable assets based on a 12-quarter trailing average through the preceding fiscal year in which the distribution is planned. The distribution rate was temporarily set at 7% for a three year period which included 2016 and 2015, and will extend through 2017, after which the distribution rate is expected to return to the historic level of 4%-5%. It is the expectation that, over time, the total return from investments will exceed the endowment's distribution rate, thus allowing for growth of the endowment portfolio. In establishing this policy, the Museum considered the long-term expected return on its investment assets, the nature and duration of the individual endowment funds, some of which must be maintained in perpetuity because of donor-imposed restrictions, and the possible effects of inflation.

Continued

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 14: DONOR DESIGNATED FUNDS (Continued)

Donor designated net asset composition by type of fund as of September 30, 2016 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total All Funds</u>
Donor Restricted Endowment Funds	<u>\$ (1,712,771)</u>	<u>\$ 258,959</u>	<u>\$ 22,388,986</u>	<u>\$ 20,935,174</u>
Changes in endowment net assets as of September 30, 2016 are as follows:				
Endowment net assets, beginning of year	\$ (2,359,668)	\$ 17,065	\$ 23,813,453	\$ 21,470,850
Contributions	-	-	27,632	27,632
Donor changed restriction	1,000,000	-	(1,000,000)	-
Investment income	313,181	50,410	-	363,591
Net appreciation (depreciation)	573,835	92,422	78,306	744,563
Management fees and other expenses	(79,516)	(12,799)	-	(92,315)
Proceeds (loss) from sale of collections	-	(265,525)	272,650	7,125
Purchases of collections	-	-	(409,028)	(409,028)
Satisfaction of program restrictions	-	(290,633)	290,633	-
Amounts appropriated for draws	<u>(1,160,603)</u>	<u>(16,641)</u>	<u>-</u>	<u>(1,177,244)</u>
Endowment net assets, end of year	<u>\$ (1,712,771)</u>	<u>\$ (425,701)</u>	<u>\$ 23,073,646</u>	<u>\$ 20,935,174</u>

Donor designated net asset composition by type of fund as of September 30, 2015 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total All Funds</u>
Donor Restricted Endowment Funds	<u>\$ (2,359,668)</u>	<u>\$ 17,065</u>	<u>\$ 23,813,453</u>	<u>\$ 21,470,850</u>
Changes in endowment net assets as of September 30, 2015 are as follows:				
Endowment net assets, beginning of year	\$ (1,415,382)	\$ 424,130	\$ 24,605,745	\$ 23,614,493
Contributions	-	-	64,511	64,511
Investment income	307,865	54,173	-	362,038
Net appreciation (depreciation)	(636,543)	(111,069)	(34,303)	(781,915)
Management fees and other expenses	(77,310)	(13,585)	-	(90,895)
Proceeds from sale of collections	-	246,894	-	246,894
Purchases of collections	-	-	(822,500)	(822,500)
Satisfaction of program restrictions	527,117	(527,117)	-	-
Amounts appropriated for budgeted draw	<u>(1,065,415)</u>	<u>(56,361)</u>	<u>-</u>	<u>(1,121,776)</u>
Endowment net assets, end of year	<u>\$ (2,359,668)</u>	<u>\$ 17,065</u>	<u>\$ 23,813,453</u>	<u>\$ 21,470,850</u>

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 15: NET ASSETS RESTATEMENT

In the prior year, the 2015 investment return budgeted for current operations was incorrectly allocated between unrestricted and temporarily restricted funds and purchases of collections were incorrectly grouped with temporarily restricted funds. During 2016, these amounts were presented in the proper net asset fund. The restatement increased unrestricted and temporarily restricted fund net assets by \$56,361 and \$766,139, respectively, and decreased permanently restricted fund net assets by \$822,500 as previously reported at September 30, 2015. The restatement had no impact on net assets in total.

PALM SPRINGS ART MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS
SEPTEMBER 30, 2016 AND 2015

NOTE 16: UNRESTRICTED EXPENSES

Expenses incurred for the year ended September 30, 2016:

	Program Services	Management & General	Fundraising & Membership	Total
Salaries	\$ 3,021,129	\$ 857,959	\$ 691,879	\$ 4,570,967
Payroll taxes and employee benefits	574,654	148,365	133,932	856,951
Exhibits and program events	1,438,507	74,583	229,816	1,742,906
Interest, insurance and other fees	244,977	77,197	905	323,079
Utilities	240,777	62,793	33,230	336,800
Professional services	443,278	193,812	108,503	745,593
Costs of sales (store and auctions)	444,984	-	-	444,984
Printing and photography	125,641	25,157	48,093	198,891
Repair and maintenance	336,133	82,316	27,783	446,232
Advertising	197,413	36	49,346	246,795
Postage and delivery	126,932	6,536	51,775	185,243
Supplies	117,593	20,520	21,950	160,063
Miscellaneous	56,053	14,603	61,121	131,777
	<u>\$ 7,368,071</u>	<u>\$ 1,563,877</u>	<u>\$ 1,458,333</u>	<u>\$ 10,390,281</u>

Expenses incurred for the year ended September 30, 2015:

	Program Services	Management & General	Fundraising & Membership	Total
Salaries	\$ 2,996,181	\$ 775,242	\$ 652,030	\$ 4,423,453
Payroll taxes and employee benefits	552,354	138,495	120,437	811,286
Exhibits and program events	1,672,142	88,763	322,798	2,083,703
Interest, insurance and other fees	239,994	105,392	21,731	367,117
Utilities	283,998	75,469	39,784	399,251
Professional services	342,420	150,611	223,276	716,307
Costs of sales (store and auctions)	513,742	-	-	513,742
Printing and photography	137,768	22,669	123,096	283,533
Repair and maintenance	380,713	87,148	38,479	506,340
Advertising	180,591	5,369	54,219	240,179
Postage and delivery	223,417	7,768	66,386	297,571
Supplies	152,855	26,949	36,933	216,737
Miscellaneous	185,503	17,276	154,652	357,431
	<u>\$ 7,861,678</u>	<u>\$ 1,501,151</u>	<u>\$ 1,853,821</u>	<u>\$ 11,216,650</u>