

# Financial Report



June 30, 2017



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## ***INDEPENDENT AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS***

Board of Trustees  
The San Diego Society of Natural History  
San Diego, California

We have audited the accompanying financial statements of the San Diego Society of Natural History (a nonprofit organization), which comprise the statement of financial position as of June 30, 2017, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

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

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risk 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 principles used and the reasonableness of significant estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the San Diego Society of Natural History as of June 30, 2017, 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 the San Diego Society of Natural History's June 30, 2016, financial statements, and our report dated September 22, 2016, 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, 2016, is consistent, in all material respects, with the audited financial statements from which it has been derived.

### **Other Matter**

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The Income/Expense Statement, City of San Diego TOT Funds on page 16 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.



WEST RHODE & ROBERTS

San Diego, California  
September 28, 2017

**THE SAN DIEGO SOCIETY OF NATURAL HISTORY**  
**STATEMENT OF FINANCIAL POSITION**  
**June 30, 2017**  
*(With Summarized Financial Information for June 30, 2016)*

	2017	2016 (Note 14)
<b>ASSETS</b>		
Cash and cash equivalents	\$ 2,055,454	\$ 2,855,487
Receivables	1,752,168	1,866,428
Prepaid expenses and other assets	318,098	455,197
Investments	17,328,880	15,568,444
Beneficial interest in charitable remainder trust	5,316,378	4,987,984
Beneficial interest in perpetual trust	2,323,541	2,284,453
Property, equipment, and leasehold improvements, net	21,151,313	22,155,840
Collections and exhibits	1	1
Total assets	<b>\$ 50,245,833</b>	<b>\$ 50,173,834</b>
<b>LIABILITIES AND NET ASSETS</b>		
Liabilities:		
Accounts payable and accrued expenses	\$ 1,245,095	\$ 1,291,512
Note payable	99,386	525,000
Deferred revenue	123,740	113,951
Total liabilities	1,468,221	1,930,463
Commitments		
Net assets:		
Unrestricted	21,168,727	22,536,860
Temporarily restricted	10,251,861	8,393,574
	31,420,588	30,930,434
Permanently restricted:		
Museum endowments	13,201,330	13,313,480
Beneficial interest in perpetual trust	2,323,541	2,284,453
Endowments held by others	1,832,153	1,715,004
	17,357,024	17,312,937
Total net assets	48,777,612	48,243,371
Total liabilities and net assets	<b>\$ 50,245,833</b>	<b>\$ 50,173,834</b>

**THE SAN DIEGO SOCIETY OF NATURAL HISTORY**

**STATEMENT OF ACTIVITIES**

**Year Ended June 30, 2017**

**(With Summarized Financial Information for the Year Ended June 30, 2016)**

	Unrestricted			Restricted		Total	2016 (Note 14)
	Operations	Depreciation	Total Unrestricted	Temporarily Restricted	Permanently Restricted		
<b>OPERATING SUPPORT AND REVENUE</b>							
Admissions and exhibit ticket sales	\$ 3,119,029	\$ -	\$ 3,119,029	\$ -	\$ -	\$ 3,119,029	\$ 3,359,082
Contributions	373,407	-	373,407	2,434,641	5,000	2,813,048	6,951,469
Contracts	2,232,424	-	2,232,424	-	-	2,232,424	2,364,382
Government grants	854,674	-	854,674	-	-	854,674	708,953
Other	503,955	-	503,955	-	-	503,955	444,171
Memberships	404,251	-	404,251	-	-	404,251	440,202
Education	279,708	-	279,708	-	-	279,708	234,436
Net assets released from restrictions:							
Satisfaction of restrictions (Note 10)	3,021,415	-	3,021,415	(2,924,982)	(96,433)	-	-
Total operating support and revenue	<u>10,788,863</u>	<u>-</u>	<u>10,788,863</u>	<u>(490,341)</u>	<u>(91,433)</u>	<u>10,207,089</u>	<u>14,502,695</u>
<b>OPERATING EXPENSES</b>							
Exhibitions	3,753,516	625,198	4,378,714	-	-	4,378,714	4,779,808
Science and research	3,062,617	351,235	3,413,852	-	-	3,413,852	3,505,820
Education/public programs	932,630	277,977	1,210,607	-	-	1,210,607	1,248,269
Membership	128,068	10,035	138,103	-	-	138,103	189,643
Management and general	999,301	130,459	1,129,760	-	-	1,129,760	1,225,164
Institutional advancement	947,963	20,071	968,034	-	-	968,034	996,815
Communications and public relations	862,732	55,194	917,926	-	-	917,926	1,076,424
Total operating expenses	<u>10,686,827</u>	<u>1,470,169</u>	<u>12,156,996</u>	<u>-</u>	<u>-</u>	<u>12,156,996</u>	<u>13,021,943</u>
Operating revenue and support in excess of expenses	<u>102,036</u>	<u>(1,470,169)</u>	<u>(1,368,133)</u>	<u>(490,341)</u>	<u>(91,433)</u>	<u>(1,949,907)</u>	<u>1,480,752</u>
<b>INVESTMENT GAINS (LOSSES)</b>							
Investment income	-	-	-	681,258	80,771	762,029	430,769
Net realized and unrealized gain (loss)	-	-	-	1,667,370	54,749	1,722,119	(699,599)
Total investment gains (losses)	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,348,628</u>	<u>135,520</u>	<u>2,484,148</u>	<u>(268,830)</u>
Change in net assets	102,036	(1,470,169)	(1,368,133)	1,858,287	44,087	534,241	1,211,922
NET ASSETS AT BEGINNING OF YEAR	<u>46,518,092</u>	<u>(23,981,232)</u>	<u>22,536,860</u>	<u>8,393,574</u>	<u>17,312,937</u>	<u>48,243,371</u>	<u>47,031,449</u>
NET ASSETS AT END OF YEAR	<u>\$ 46,620,128</u>	<u>\$ (25,451,401)</u>	<u>\$ 21,168,727</u>	<u>\$ 10,251,861</u>	<u>\$ 17,357,024</u>	<u>\$ 48,777,612</u>	<u>\$ 48,243,371</u>

**THE SAN DIEGO SOCIETY OF NATURAL HISTORY**  
**STATEMENT OF CASH FLOWS**  
**Year Ended June 30, 2017**  
**(With Summarized Financial Information for the Year Ended June 30, 2016)**

	2017	2016 (Note 14)
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in net assets	\$ 534,241	\$ 1,211,922
Adjustments to reconcile change in net assets to net cash from operating activities:		
Depreciation	1,470,169	1,395,890
Amortization	-	-
Allowance for uncollectability and discounts	144,273	6,729
Contributions restricted for endowments	(44,087)	(2,687,755)
Contributed stock	-	(568,359)
Realized and unrealized gain on investments	(1,722,119)	699,599
Beneficial interest in charitable remainder trust	(367,482)	223,989
Change in operating assets and liabilities:		
Receivables	(30,013)	1,933,298
Prepaid expenses and other assets	137,099	257,938
Accounts payable and accrued expenses	(46,417)	(474,865)
Deferred revenue	9,789	(23,819)
Net cash provided by operating activities	85,453	1,974,567
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net (purchase) proceeds of investments	(38,317)	(2,109,124)
Purchase of property and equipment	(465,642)	(2,893,151)
Net cash used in investing activities	(503,959)	(5,002,275)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Contributions restricted for endowments	44,087	2,687,755
Payment on line of credit	-	(215,128)
Proceeds from note payable	-	525,000
Payments of notes payable	(425,614)	-
Net cash (used in) provided by financing activities	(381,527)	2,997,627
Change in cash and cash equivalents	(800,033)	(30,081)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	2,855,487	2,885,568
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 2,055,454	\$ 2,855,487
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Cash paid for interest	\$ 15,305	\$ 2,300

## **Note 1. Organization and Significant Accounting Policies**

### **Organization and Activities**

The San Diego Natural History Museum (the Museum) was founded in 1874 and operates with a mission to *interpret the natural world through research, education and exhibits; to promote understanding of the evolution and diversity of southern California and the peninsula of Baja California; and to inspire in all a respect for nature and the environment.* Major Museum program areas include:

#### **Public Programs**

The Museum occupies a 150,000-square-foot facility that has public access to exhibitions on five floors, a 3-D giant-screen theater, and education classrooms. In January 2015, the Museum dedicated a new permanent exhibition, *Coast to Cactus in Southern California*, which is designed to take visitors through Southern California's patchwork of diverse habitats, home to the most bio-diverse flora and fauna found anywhere in the contiguous United States, and the greatest number of endangered species. *Coast to Cactus* teaches students and all visitors about the importance of biodiversity and at the same time encourage environmental awareness. This exhibition complements their first permanent exhibition, *Fossil Mysteries*, which takes visitors through a 75-million-year timeline, from the age of dinosaurs to the Ice Ages, to experience the prehistory of southern California and Baja California. Combined, these two exhibitions will give visitors a true sense of place: from the geologic and paleontological past to the biological present and how they both inform the future.

#### **Education Programs**

Through the Environmental Science Education Center, the Museum offers programs for lifelong learning, from pre-school through senior adults in the United States and Mexico. Education programs are offered in the Museum, in schools and other community locations, as well as outdoors locations throughout the region, to a total of 30,000 participants annually. The range of K-12 programs includes Common Core Standards based hands-on science workshops which are enlivened by encased and touchable natural specimens.

#### **The Biodiversity Research Center of the Californias (BRCC)**

For 140 years, the Museum has served as a leader for the preservation and interpretation of scientific specimens that document the biodiversity of our area. As the research and collections of the Museum, BRCC continues this legacy by publishing high-quality scientific research on southern California and Baja California. BRCC focuses on the biology, ecology, paleontology, and geology of this region and houses nearly 7.4 million research specimens. Through collections-based research, BRCC promotes the understanding of the evolution and diversity of southern California and the peninsula of Baja California. Our research and publications are fundamentally region-oriented, collection-based, and driven by evolutionary hypotheses.

### **Significant Accounting Policies**

**Method of Accounting** – The financial statements of the Museum have been prepared utilizing the accrual basis of accounting.

**Basis of Presentation** – The Museum reports information regarding its financial position and activities in three classes of net assets – unrestricted, temporarily restricted, and permanently restricted - based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Museum and changes therein are classified and reported as follows:

Unrestricted net assets - Net assets that are not subject to any donor-imposed stipulations.

Temporarily restricted net assets - Net assets subject to donor-imposed restrictions on their use that may be met either by actions of the Museum or the passage of time.

Permanently restricted net assets - Net assets subject to donor-imposed restrictions requiring that the principal be maintained permanently by the Museum. Generally, the donors permit the Museum to use all or part of the income earned for either general or donor-specified purposes.

## Revenue Recognition

Contributions – Contributions are recognized as revenue when they are unconditionally pledged or when all conditions have been met.

The Museum reports contributions as temporarily restricted if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted revenues are reclassified to unrestricted revenues and reported in the statement of activities as revenues released from restrictions. Contributions with donor restrictions requiring the principal gift to be held in perpetuity are reported as permanently restricted. The income and net gains earned from such assets is generally restricted to the purpose designated by the donor. This recognition is in accordance with the Financial Accounting Standards Board (FASB) Accounting Standards Codification No. 958-605.

Contributions of service are recognized if the services received (a) create or enhance non-financial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. The Museum reports such contributions at their estimated fair value when received. During the year ended June 30, 2017, no contributions of services were recorded.

Government Grants – The policy of the Museum is to recognize the revenue to the extent of eligible costs incurred, up to the maximum subcontract or grant amount.

Scientific Grants and Contracts – The Museum recognizes revenue as services are provided.

Admissions and Education – The Museum records revenue when goods or services are provided.

Memberships – The Museum recognizes revenue at the time of renewal.

Exhibition Costs – Exhibition costs are usually expensed when incurred; however, traveling exhibition costs included in prepaid expense are expensed over the term of the exhibition.

Traveling exhibitions are exhibitions in which the Museum may charge an additional fee in excess of the normal admission price. The Museum recognizes revenue when earned and expenses are recognized over the term of the exhibition. During the year ended June 30, 2017, the Museum hosted traveling exhibitions, *Animals in Motion and Ultimate Dinosaurs*, to which it charged an additional fee in excess of the normal general admission price.

**Cash and Cash Equivalents** – The Museum considers all cash accounts that are not subject to withdrawal restrictions or penalties, and certificate of deposits with an original maturity date of less than 90 days to be cash equivalents.

**Grants and Contracts Receivable** – All receivables are reviewed for collectability and reserves for uncollectible amounts are recorded based on the estimated collectability. Accounts are written off against the allowance for doubtful accounts when deemed uncollectible. Management has determined that an allowance of \$55,000 is needed for the year ended June 30, 2017.

**Pledges Receivable** – Pledges receivable are unconditional promises received and are recorded when the promise to contribute is made. The Museum provides an allowance for estimated uncollectible amounts at the time the pledges are recorded. The provision for uncollectible pledges is based, among other things, on the Museum's past collection experience and the changes in the current economic conditions. Pledges receivable with payment terms in excess of one year have been discounted using an interest rate of 5%. Amortization of the discounts related to pledges receivable are recognized over the period of the promise as contribution revenue. Management has determined that an allowance of \$100,000 is needed for the year ended June 30, 2017.

**Investments** – Investments in debt and equity securities with readily determinable fair values are reported at fair values. Net realized and unrealized gains or losses are reflected as increases or decreases in unrestricted net assets, unless the use is restricted by the donor.

*THE SAN DIEGO SOCIETY OF NATURAL HISTORY*  
*NOTES TO FINANCIAL STATEMENTS*

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Under the Museum's bylaws, the Board of Trustees Finance and Investment Committees have overall responsibility for the establishment of policies and general governance related to investments of the Museum.

**Beneficial Interest in Charitable Remainder Trusts** – The Museum is the beneficiary of charitable remainder trusts, which provide for payments of distributions to designated beneficiaries over the trusts' terms (usually the designated beneficiary's lifetime). At the end of a trust's term, the remaining assets are available to the Museum for the purpose specified by the donor.

Assets held in the charitable remainder trusts are managed by donor designated trustees, and are not accessible by the Museum until the end of the trusts' terms. The assets are recorded as temporarily restricted contributions at their present value, calculated by the trustee using risk-free interest rates over the estimated period until the Museum is to receive an irrevocable right to the assets.

**Beneficial Interests in Perpetual Trusts** – The Museum is named as beneficiary on a perpetual trust held by a third party. This is an arrangement in which the donor established and funds a trust that is administered by an outside third party. Under the terms of the trust, the Museum has the right to receive the income earned on the trust's assets in perpetuity, but never receives the assets held in trust. The trust is recorded as permanently restricted net assets.

**Pooled Income Funds** – Included in investments are pooled income funds, which are held at a bank. During the life of the donors, income from the pooled funds is distributed to the donors. Upon the donor's death, the principal is to be distributed to the Museum. A discount to present value is recorded and the net amount is included in temporarily restricted net assets.

**Physical Facilities** – The Museum constructed the original building and the expansion it occupies. After completion, the Museum transferred the title to the City of San Diego (the City). The Museum occupies the building under a 35-year lease agreement with the City expiring in 2033, which permits the Museum use of the structure at no charge. Under the terms of the lease, the City is responsible for the maintenance of the exterior of the building.

In accordance with accounting principles generally accepted in the United States of America (US GAAP), the original value of the building is to be reflected in the Museum's financial statements. However, if the building had been reported at its fair market value at the date the agreement with the City originally commenced, it would have been fully depreciated in prior years. Therefore, it is not reflected in the accompanying statement of financial position. The cost of construction to expand and renovate the original building has been capitalized in the statement of financial position as leasehold improvements and is being amortized over the life of the lease.

The agreement with the City also provides for the Museum's free use of the land in Balboa Park on which the structure is situated. No amounts have been reflected in the financial statements for use of the land, as no objective basis is available to measure its value.

**Property, Equipment and Leasehold Improvements** – Property, equipment and leasehold improvements are carried at cost for items purchased or improvements made, or fair value at the date of the gift for donated items. Items which cost or have a fair value at the date of the gift of \$5,000 or more are capitalized. Depreciation is provided using the straight-line method over the estimated useful lives of the assets. Improvements are depreciated over 30 years. Furniture and equipment are depreciated over 5 to 20 years.

**Collections** – The Museum houses over seven million natural history specimens in collections dating back as far as the 1870s. Specimens include plants, birds, mammals, insects, reptiles, amphibians, marine invertebrates, fossils, and minerals mainly from the Western United States and Baja California, Mexico. In addition, the Museum's library includes some 25,000 titles in 56,000 volumes with many significant and rare volumes on natural history. The Museum's collections are expensed when acquired. In accordance with the practice generally followed by museums, the value of the collections housed by the Museum are excluded from the financial statements and are reflected on the statements of financial position at the nominal value of \$1. Contributed collections are not reflected in the financial statements. There were no proceeds from deaccessions during the year ended June 30, 2017.

**Advertising Costs** – Advertising costs are expensed as incurred.

**Functional Allocation of Expenses** – The costs of providing the 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.

**Use of Estimates** – The preparation of financial statements, in conformity with US GAAP, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of support, revenue, and expenses during the reporting period. Actual results could differ from those estimates.

**Income Tax Status** – The Museum is exempt from federal income tax pursuant to Section 501(c)(3) of the Internal Revenue Code and is also exempt from state income tax. The Financial Accounting Standards Board (FASB) issued Accounting Standards Codification No. 740-10, *Accounting for Uncertainties in Income Taxes*, which sets a minimum threshold for financial statement recognition of the benefit of a tax position taken or expected to be taken in a tax return. The Museum has reviewed its positions for all open tax years and has determined that it has no uncertain tax positions requiring accrual or disclosure.

**Subsequent Events** – Subsequent events are events or transactions that occur after the statement of financial position date but before financial statements are available to be issued. The Museum recognizes in the financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at that date, including the estimates inherent in the process of preparing financial statements. The Museum's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of financial position, but arose after that date and before the financial statements are available to be issued.

The Museum has evaluated subsequent events through September 28, 2017, which is the date the financial statements are available for issuance, and concluded that there were no events or transactions that needed to be disclosed.

## **Note 2. Concentration of Credit Risk**

Financial instruments, which potentially subject the Museum to credit risk, consist primarily of cash, receivables, and investments.

**Cash** – The Museum maintains its cash in bank accounts, which at times may exceed federally insured limits. The Museum has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk related to cash.

**Pledges Receivable** – Pledges receivable include charitable remainder trusts, which are exposed to various risks such as interest rates and donor life expectancies. Changes in the near term are not expected to materially affect the amounts reported in the financial statements. Pledges are subject to credit risk.

**Investments** – The Museum maintains its short-term investments in several different instruments with various investment firms. Marketable securities are exposed to various risks, such as interest rate, market, and credit risk. It is reasonably possible, given the level of risk associated with marketable securities that changes in the near term could materially affect the amount reported in the financial statements.

## **Note 3. Fair Value Measurements**

Due to the short-term nature of cash equivalents, receivables, prepaid expenses, accounts payable and deferred revenue, fair value approximates carrying value. In accordance with Financial Accounting Standards Board Codification No. 820 (FASB ASC 820), fair value is defined as the price that the Museum would receive upon selling an asset or transferring a liability in an orderly transaction to an independent buyer in the principal or most advantageous market of the asset.

*THE SAN DIEGO SOCIETY OF NATURAL HISTORY  
NOTES TO FINANCIAL STATEMENTS*

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FASB ASC 820 also establishes a three-tier hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs and to establish the classification of fair value measurements for disclosure purposes. Inputs refer broadly to the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available.

The standard describes three-tier hierarchy of inputs that may be used to measure fair value as follows:

**Level 1:** Quoted prices of identical assets or liabilities in active markets.

**Level 2:** Significant other observable inputs other than Level 1 prices (such as quoted prices for similar assets or liabilities, interest rates, prepayment speeds and credit risk).

**Level 3:** Significant unobservable inputs that reflect the Museum's own assumptions in determining the fair value of assets.

Assets and liabilities measured at fair value on a recurring basis are summarized below:

	Fair Value Measurements at June 30, 2017, Using:			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
<u>Assets</u>				
Investments, general	\$ 15,367,070	\$ 129,657	\$ -	\$ 15,496,727
Beneficial interest in charitable remainder trust	-	5,316,378	-	5,316,378
Beneficial interest in perpetual trust	-	2,323,541	-	2,323,541
Funds held at San Diego Foundation	-	1,832,153	-	1,832,153
	<u>\$ 15,367,070</u>	<u>\$ 9,601,729</u>	<u>\$ -</u>	<u>\$ 24,968,799</u>

The fair value of a financial instrument is 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. Fair value is best determined based upon quoted market prices. The Museum has investments which are based upon quoted market prices at June 30, 2017. The Museum also has a beneficial interest in a perpetual trust and charitable remainder trust which is based upon significant inputs as performed by their respective trustee.

The management of the Museum is responsible for making the fair value measurements and disclosures in the financial statements. As part of fulfilling this responsibility, the management of the Museum has established an accounting and financial reporting process for determining the fair value measurements and disclosures, which identifies and adequately supports the valuation methods and assumptions used and ensures that the presentation of the fair value measurement is in accordance with US GAAP.

THE SAN DIEGO SOCIETY OF NATURAL HISTORY  
NOTES TO FINANCIAL STATEMENTS

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**Note 4. Investments**

Investments, at fair value, consist of:

	<u>Total</u>
Equity mutual funds	\$ 11,589,719
Bond mutual funds	3,770,545
Funds held at San Diego Foundation	1,832,153
Pooled income fund	121,657
Other	8,000
Money market funds	6,806
	<u>\$ 17,328,880</u>

**Note 5. Receivables**

Receivables consist of:

Due in less than one year	
Contracts	\$ 545,927
Pledges	363,370
General	294,347
Grants	36,927
Less allowance for doubtful accounts	<u>(155,000)</u>
	<u>1,085,571</u>
Due in one to five years	
Pledges	399,307
Charitable remainder trusts	469,914
Less discounts to net present value at 4%	<u>(202,624)</u>
	<u>666,597</u>
Total receivables	<u>\$ 1,752,168</u>

**Note 6. Property, Equipment, and Leasehold Improvements**

Property, equipment, and leasehold improvements consist of:

Leasehold improvements	\$ 38,906,946
Furniture, fixtures, and equipment	7,175,051
Construction in progress	301,161
Capital lease equipment	<u>219,547</u>
	46,602,705
Less accumulated depreciation	<u>(25,451,392)</u>
	<u>\$ 21,151,313</u>

Depreciation expense was \$1,470,169 for the year ended June 30, 2017.

**Note 7. Note Payable**

In March 2016, the Museum entered into a note payable agreement with First Republic Bank that allows the Museum to borrow up to \$900,000 at the rate of 3.5% per annum. As of June 30, 2017, the Museum had \$99,386 outstanding on the loan. The loan is interest only through March 9, 2019, at which time the principal is due.

THE SAN DIEGO SOCIETY OF NATURAL HISTORY  
 NOTES TO FINANCIAL STATEMENTS

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**Note 8. Commitments**

**Operating Leases** – The Museum leases copier equipment under two lease agreements expiring on or before June 2020.

In addition, the Museum entered into an agreement to lease warehouse space under a lease agreement expiring in June 2023.

Future minimum lease payments required under the operating lease agreements are as follows:

<u>Years Ending June 30,</u>	<u>Operating Leases</u>
2018	\$ 101,604
2019	104,712
2020	107,964
2021	88,320
2022	91,176
Thereafter	94,824
	<u>\$ 588,600</u>

For the year ended June 30, 2017, lease expense for these leases totaled approximately \$117,831.

**Employment Contracts** – The Museum has an employment contract with the CEO for an annual salary through June 30, 2019.

**Note 9. Restricted Net Assets**

Temporarily restricted net assets consists of:

Charitable remainder trusts	\$ 5,611,668
Endowment over corpus	2,570,873
Legacy campaign	1,036,891
Science, research and education	910,771
Pooled income funds*	121,658
	<u>\$ 10,251,861</u>

\*The Museum maintains a pooled income fund at Union Bank of California. The fund is reported at its June 30, 2017, net present value.

Permanently restricted net assets consist of endowments, the income from which is expendable for:

Endowments held at the Museum	
Science, research and education	\$ 7,008,868
General operations	4,309,611
CEO Endowment	2,000,000
	<u>13,318,479</u>
Beneficial interest in perpetual trust	<u>2,323,541</u>
Endowments held at San Diego Foundation	1,715,004
	<u>\$ 17,357,024</u>

**Note 10. Net Assets Released from Restriction**

Net assets were released for the following purposes:

Temporarily restricted	
Legacy campaign	\$ 890,334
Special projects campaign	875,416
Science, research and education	569,419
Endowment funds released	<u>589,813</u>
	<u>2,924,982</u>
Permanently restricted	
Distribution from perpetual trust	<u>96,433</u>
	<u>\$ 3,021,415</u>

**Note 11. Endowment**

The Museum follows the standards codified in FASB ASC 958-205-65, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds*, which provides guidance on the net asset classification of donor-restricted endowment funds for a not-for-profit organization that is subject to an enacted version of the 2006 UPMIFA. The endowment includes only donor-restricted endowment funds.

**Interpretation of Relevant Law** – The Board of Directors of the Museum 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. As a result of this interpretation, the Museum 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 UPMIFA. The Museum considers endowed funds its general endowment, beneficial interest in a perpetual trust and funds that are held at community foundations.

**Endowment Investment and Spending Policies** – The Museum has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Museum must hold in perpetuity. The Museum expects its endowment funds, over time, to provide an average rate of return.

The investment objectives for the Endowment’s assets are to earn long-term returns that match or exceed annual income requirements of the San Diego Natural History Museum, to provide for asset growth at a rate in excess of the rate of inflation, to diversify the Endowment’s assets in order to reduce the risk of wide swings in market value from year-to-year, or of incurring large losses, and to achieve investment results over the long-term that compare favorably with those of other endowments and of appropriate market indexes. The committee uses a return objective which is measured over a full market cycle (5 years), and is expected to outperform a custom index which reflects the target asset allocation of the portfolio. The 5 year custom index was 7.5% as of June 30, 2017.

The Museum has a policy of appropriating for distribution each year 4.5% of its endowment fund’s average value over the previous three calendar years. In establishing this policy, the Museum considered the long-term expected return on its endowment. This is consistent with the Museum’s objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

THE SAN DIEGO SOCIETY OF NATURAL HISTORY  
 NOTES TO FINANCIAL STATEMENTS

Donor-restricted endowment net asset composition as of June 30, 2017, is as follows:

**Changes in Endowment Net Assets  
 for the Fiscal Year Ended June 30, 2017**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ -	\$ 812,058	\$ 17,312,937	\$ 18,124,995
Investment return:				
Investment income	-	681,258	80,771	762,029
Net appreciation (depreciation)	(1) -	1,667,370	54,749	1,722,119
Total investment return	-	2,348,628	135,520	2,484,148
Appropriation of assets for expenditure	-	(589,813)	(96,433)	(686,246)
Contributions	-	-	5,000	5,000
Endowment net assets, end of year	<u>\$ -</u>	<u>\$ 2,570,873</u>	<u>\$ 17,357,024</u>	<u>\$ 19,927,897</u>

(1) Includes realized and unrealized gains and losses, and other fees or expenses

**Note 12. Retirement Plan**

**Defined Contribution Plan** – The Museum has a defined contribution plan. The plan provides for voluntary employee contributions and employer contributions. Generally, all employees regularly scheduled to work at least 20 hours per week are eligible to participate in the Plan. An eligible employee may elect to make voluntary employee contributions to the Plan at any time after employment commences. For the year ended June 30, 2017, the Museum made matching contributions of \$44,042.

**Note 13. Contingencies**

**Grants and Contracts** – The Museum has grants and contracts with government agencies which are subject to audit. No provision has been made for any liabilities that may arise from such audits since the amounts, if any, cannot be determined. Management believes that any liability which may result from these audits would not have a material impact on the Museum's financial statements.

**Note 14. June 30, 2016 Financial Information**

The financial statements include certain prior year summarized comparative information in total, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Museum's financial statements for the year ended June 30, 2016, from which the summarized information was derived.

**THE SAN DIEGO SOCIETY OF NATURAL HISTORY**  
**SUPPLEMENTARY INFORMATION**  
**INCOME/EXPENSE STATEMENT, CITY OF SAN DIEGO TOT FUNDS**  
**Year Ended June 30, 2017**

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<b>EXPENSE CLASSIFICATION</b>	Budget	Actual	TOT Funds
Operating income	\$ 24,773,783	\$ 10,207,089	\$ 593,753
Operating expense	(24,773,783)	(12,156,996)	(593,753)
Net income	\$ -	\$ (1,949,907)	\$ -



**REPORT ON COMPLIANCE WITH THE REQUIREMENTS OF THE CITY OF SAN DIEGO COMMISSION  
FOR ARTS AND CULTURE ALLOCATIONS PROGRAM**

Board of Trustees  
The San Diego Society of Natural History

We have audited, in accordance with auditing standards generally accepted in the United States of America, the statement of financial position of the San Diego Society of Natural History (the Museum) as of June 30, 2017, and the related statements of activities and cash flows for the year then ended, and have issued our report thereon dated September 28, 2017.

In connection with our audit, nothing came to our attention that caused us to believe that the San Diego Society of Natural History failed to comply with the requirements of the City of San Diego Commission for Arts and Culture Allocations Program. However, our audit was not directed primarily toward obtaining knowledge of such non-compliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Museum's non-compliance with the requirements of the City of San Diego Commission for Arts and Culture Allocations Program.

This report is intended solely for the information and use of the Board of Trustees and management of the San Diego Society of Natural History, and the City of San Diego Commission for Arts and Culture Allocations Program, and is not intended to be and should not be used by anyone other than these specified parties.

*West Rhode & Roberts*

WEST RHODE & ROBERTS

San Diego, California  
September 28, 2017