

ARIZONA-SONORA DESERT MUSEUM, INC.

YEAR ENDED SEPTEMBER 30, 2016

ARIZONA-SONORA DESERT MUSEUM, INC.

YEAR ENDED SEPTEMBER 30, 2016

CONTENTS

	Page
Independent auditors' report	1 - 2
Financial statements:	
Statement of financial position	3
Statement of activities	4
Statement of cash flows	5
Notes to financial statements	6 - 20
Supplementary information to financial statements:	
Schedule of functional expenses	21

Independent Auditors' Report

Board of Trustees and Management
Arizona-Sonora Desert Museum, Inc.
Tucson, Arizona

We have audited the accompanying financial statements of Arizona-Sonora Desert Museum, Inc. (Museum) which comprise the statement of financial position as of September 30, 2016, 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 U.S. generally accepted accounting principles; 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 audit. We conducted our audit in accordance with U.S. generally accepted auditing standards established by the AICPA Auditing Standards Board. 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 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 Museum'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 Museum'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 Arizona-Sonora Desert Museum, Inc. as of September 30, 2016, and the changes in its net assets and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

Report on Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information on page 21 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 U.S. generally accepted auditing standards. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Beach Fleishman PC

Tucson, Arizona
January 25, 2017

ARIZONA-SONORA DESERT MUSEUM, INC.

STATEMENT OF FINANCIAL POSITION

SEPTEMBER 30, 2016

	Unrestricted				Temporarily Restricted	Permanently Restricted	Total
	Operating	Capital Asset Fund	Operating Reserve	Total Unrestricted			
ASSETS							
Cash and cash equivalents	\$ 583,424	\$ -	\$ -	\$ 583,424	\$ -	\$ -	\$ 583,424
Estates and pledges receivable, net	318,425	-	147,118	465,543	196,690	-	662,233
Other receivables	135,966	-	-	135,966	-	-	135,966
Inventory	253,467	-	-	253,467	-	-	253,467
Due from (to) other net asset groups	1,109,571	-	(1,043,648)	65,923	213,543	(279,466)	-
Investments	9,760	-	3,585,098	3,594,858	1,201,543	4,284,154	9,080,555
Beneficial interest in perpetual trust	-	-	-	-	-	130,057	130,057
Assets held in charitable trusts	-	-	-	-	415,178	-	415,178
Other assets	42,049	-	-	42,049	-	-	42,049
Property and equipment, net	-	13,289,712	-	13,289,712	151,482	-	13,441,194
Total assets	\$ 2,452,662	\$13,289,712	\$ 2,688,568	\$18,430,942	\$ 2,178,436	\$ 4,134,745	\$24,744,123
LIABILITIES AND NET ASSETS							
Liabilities:							
Accounts payable	\$ 143,765	\$ -	\$ -	\$ 143,765	\$ -	\$ -	\$ 143,765
Accrued liabilities	463,652	-	449	464,101	2,880	-	466,981
Unearned revenue	84,198	-	-	84,198	-	-	84,198
Deferred revenue, membership dues	370,778	-	-	370,778	-	-	370,778
Capital leases payable	11,107	-	-	11,107	-	-	11,107
Total liabilities	1,073,500	-	449	1,073,949	2,880	-	1,076,829
Commitments and contingencies							
Net assets:							
Unrestricted:							
Undesignated	1,379,162	-	-	1,379,162	-	-	1,379,162
Invested in property and equipment	-	13,289,712	-	13,289,712	-	-	13,289,712
Designated for long-term reserves	-	-	2,688,119	2,688,119	-	-	2,688,119
	1,379,162	13,289,712	2,688,119	17,356,993	-	-	17,356,993
Temporarily restricted	-	-	-	-	2,175,556	-	2,175,556
Permanently restricted	-	-	-	-	-	4,134,745	4,134,745
Total net assets	1,379,162	13,289,712	2,688,119	17,356,993	2,175,556	4,134,745	23,667,294
Total liabilities and net assets	\$ 2,452,662	\$13,289,712	\$ 2,688,568	\$18,430,942	\$ 2,178,436	\$ 4,134,745	\$24,744,123

See notes to financial statements.

ARIZONA-SONORA DESERT MUSEUM, INC.

STATEMENT OF ACTIVITIES

YEAR ENDED SEPTEMBER 30, 2016

	Unrestricted			Temporarily Restricted	Permanently Restricted	Total
	Operating	Capital Asset Fund	Operating Reserve			
Revenues and other support:						
Admissions	\$ 3,345,800	\$ -	\$ -	\$ 3,345,800	\$ -	\$ 3,345,800
Concessions rental	412,371	-	-	412,371	-	412,371
Museum food services rental	115,049	-	-	115,049	-	115,049
Facilities rental	51,884	-	-	51,884	-	51,884
Membership	1,715,174	-	-	1,715,174	-	1,715,174
Contributions	1,241,256	-	481,463	1,722,719	1,756,089	3,488,376
Grant revenue	212,423	-	-	212,423	-	212,423
Special events, net	129,706	-	-	129,706	28,046	157,752
Education	213,893	-	-	213,893	154,435	368,328
Publications	29,967	-	-	29,967	-	29,967
Investment income:						
Interest and dividends	2,010	-	55,584	57,594	17,913	162,632
Net investment gain (loss)	(9,041)	-	170,288	161,247	(9,817)	466,043
Investment fees	(7,995)	-	(13,934)	(21,929)	(5,577)	(45,670)
Other	153,152	(4,907)	-	148,245	-	148,245
Net assets released from restrictions/reserves	1,019,104	254,806	25,000	1,298,910	(1,298,910)	-
Total revenues and other support	<u>8,624,753</u>	<u>249,899</u>	<u>718,401</u>	<u>9,593,053</u>	<u>642,179</u>	<u>10,628,374</u>
Expenses:						
Program services:						
Facilities	2,176,622	1,079,191	-	3,255,813	-	3,255,813
Visitor services	406,782	-	-	406,782	-	406,782
Summer Saturday evenings	20,675	-	-	20,675	-	20,675
Animal interpretive collections	203,518	-	-	203,518	-	203,518
Raptor Free Flight	216,872	-	-	216,872	-	216,872
Botany	540,330	-	-	540,330	-	540,330
Herpetology and invertebrate zoology	501,640	-	-	501,640	-	501,640
Mammalogy and ornithology	697,112	-	-	697,112	-	697,112
Publications	24,430	-	-	24,430	-	24,430
Center for Sonoran Desert Studies	1,043,786	-	-	1,043,786	-	1,043,786
Design and planning	235,559	-	-	235,559	-	235,559
Art Institute	629,410	-	-	629,410	-	629,410
General collections	181,651	-	-	181,651	-	181,651
Supporting services:						
Administration	499,105	13,171	-	512,276	-	512,276
Finance	474,025	-	-	474,025	-	474,025
Marketing	355,909	-	-	355,909	-	355,909
Fundraising:						
Development and membership	583,463	300	70,584	654,347	-	654,347
Total expenses	<u>8,790,889</u>	<u>1,092,662</u>	<u>70,584</u>	<u>9,954,135</u>	<u>-</u>	<u>9,954,135</u>
Change in net assets before transfers	<u>(166,136)</u>	<u>(842,763)</u>	<u>647,817</u>	<u>(361,082)</u>	<u>642,179</u>	<u>674,239</u>
Operating support provided from designated funds	171,000	-	(171,000)	-	-	-
Other transfers	-	794,341	(391,508)	402,833	(140,723)	(262,110)
	<u>171,000</u>	<u>794,341</u>	<u>(562,508)</u>	<u>402,833</u>	<u>(140,723)</u>	<u>(262,110)</u>
Change in net assets	4,864	(48,422)	85,309	41,751	501,456	674,239
Net assets, beginning of year	1,374,298	13,338,134	2,602,810	17,315,242	1,674,100	22,993,055
Net assets, end of year	<u>\$ 1,379,162</u>	<u>\$13,289,712</u>	<u>\$ 2,688,119</u>	<u>\$17,356,993</u>	<u>\$ 2,175,556</u>	<u>\$23,667,294</u>

See notes to financial statements.

ARIZONA-SONORA DESERT MUSEUM, INC.

STATEMENT OF CASH FLOWS

YEAR ENDED SEPTEMBER 30, 2016

Cash flows from operating activities:	
Change in net assets	\$ 674,239
Adjustment to reconcile change in net assets to net cash provided by operating activities:	
Depreciation and amortization	1,079,041
Net unrealized gains on investments	(417,383)
Net realized gains on investments	(48,660)
Amortization of discount on pledges receivable	(98)
Loss on disposal of assets	4,907
Contributions received for long-term purposes	(491,031)
Changes in operating assets and liabilities:	
Estates and pledges receivable	(313,177)
Other receivables	(82,230)
Inventory	7,751
Other assets	1,547
Accounts payable	8,726
Accrued liabilities	(131,928)
Unearned revenue	19,442
Deferred revenue, membership dues	5,195
Total adjustments	<u>(357,898)</u>
Net cash provided by operating activities	<u>316,341</u>
Cash flows from investing activities:	
Proceeds from sales and redemptions of investments	599,944
Purchases of investments	(905,304)
Purchases of property and equipment	<u>(789,868)</u>
Net cash used in investing activities	<u>(1,095,228)</u>
Cash flows from financing activities:	
Repayments on capital lease obligation	(37,002)
Proceeds from contributions for long-term purposes	<u>491,031</u>
Net cash provided by financing activities	<u>454,029</u>
Net decrease in cash and cash equivalents	(324,858)
Cash and cash equivalents, beginning	<u>908,282</u>
Cash and cash equivalents, ending	<u>\$ 583,424</u>

See notes to financial statements.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED SEPTEMBER 30, 2016

1. Organization and summary of significant accounting policies:

Organization:

The Arizona-Sonora Desert Museum, Inc. (the Museum) is an independent natural history institution in Tucson, Arizona. The Museum operates as a nonprofit, educational corporation supported by admission, membership dues and contributions, which come primarily from the private sector.

Financial statement presentation:

The Museum reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets and permanently restricted net assets. Resources are reported for accounting purposes in separate classes of net assets based on the existence or absence of donor-imposed restrictions. In the accompanying financial statements, net assets that have similar characteristics have been combined into similar categories as follows:

- Unrestricted - Net assets that are not subject to donor-imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of the Board of Trustees or may otherwise be limited by contractual agreements with outside parties.
- Temporarily restricted - Net assets whose use by the Museum is subject to donor-imposed stipulations that can be fulfilled by actions of the Museum pursuant to those stipulations or that expire through the passage of time.
- Permanently restricted - Net assets that are subject to donor-imposed stipulations that assets be maintained permanently by the Museum. The donors of these assets permit the Museum to use all or part of the investment return from these assets on continuing operations, which may be subject to certain restrictions.

Accounting estimates:

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (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 reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recognition of donor-restricted contributions:

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset classes. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restriction.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

1. Organization and summary of significant accounting policies (continued):

Recognition of donor-restricted contributions (continued):

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

Revenue recognition:

The Museum recognizes revenue earned on government grant and cooperative contracts as exchange transactions utilizing the percentage-of-completion method measured by the cost-to-cost method or level-of-effort method, as applicable. The percentage complete is estimated based upon the percentage that the incurred costs on each grant bears to the estimated total costs of the grant.

Revenue and costs on grants are subject to revision throughout the terms of the grants and required adjustments, if any, are made in the period in which the revisions become known.

Unearned revenue represents advance payments received for educational classes and other activities offered by the Museum.

The Museum sells annual memberships entitling the purchaser to unlimited admission during the year. Fees for membership dues are recognized ratably and in the fiscal year to which the membership applies.

Cash and cash equivalents:

Cash and cash equivalents include securities with an original purchased maturity of three months or less. Cash and cash equivalents received with donor-imposed stipulations restricting the use of the cash to long-term purposes and cash designated for long-term purposes are classified as investments.

The Museum maintains deposit accounts, certificates of deposit and money market funds with various institutions. At times, such investments may be in excess of the FDIC and SBIC insurance limits; however, management does not believe it is exposed to any significant credit risk on cash and cash equivalents.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

1. Organization and summary of significant accounting policies (continued):

Estates and pledges receivable:

Unconditional promises to give are recognized as revenues at their estimated net realizable value when notice of the promise is received. Conditional promises to give are recognized only when the conditions on which they depend are substantially met and the pledges become unconditional. Promises to give that are collectible over future periods are discounted to their net present value. The provision for uncollectible pledges is based on management's estimate of current economic factors, applied as a percentage to gross revenues. Promises to give are periodically reviewed for collectibility and written off to the provision at the time of such determination.

Inventory:

Inventory consists primarily of supplies and publications and is stated at cost on a first-in, first-out basis. Minerals included in inventory are held for sale and are stated at the lower of average cost or net realizable value.

Investments:

Investments in equity securities with readily determinable fair values and all investments in debt securities are valued at their fair values in the statement of financial position. Donated investments are recorded at their fair value at the date of gift. Investment gains and losses are included in the change in net assets in the accompanying statement of activities as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor-imposed stipulation or by law.

Realized gains or losses on disposition of investments are recorded on a trade date basis using the specific identification method. The fair value of investment securities is estimated based upon the last trade price on a national securities exchange or in the over-the-counter market. If no trade price is reported for the measurement date, the fair value is estimated based upon the current bid price at the close of business on the measurement date.

Property and equipment:

Property and equipment are stated at cost or, if acquired by gift, at estimated fair market value at the date of donation. Depreciation is computed on the straight-line method over the estimated useful lives of the related assets which range from 3 to 30 years. Maintenance, repairs and minor renewals are expensed as incurred while expenditures for additions and improvements with a useful life greater than 3 years are capitalized. Contributions of cash that must be used to acquire property and equipment are reported as temporarily restricted support. The Museum reports expirations of donor restrictions when the acquired assets are placed in service as instructed by the donor. The Museum reclassifies temporarily restricted net assets to unrestricted net assets at that time.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

1. Organization and summary of significant accounting policies (continued):

Property and equipment (continued):

Property and equipment under capital lease is stated at cost or the assets' net present value of future lease payments at the date of the lease. Amortization is provided using the straight-line method over the estimated useful lives of the assets, or lease term, and is included with depreciation expense.

Pima County owns the land and some permanent structures on which the Museum is located. The Museum has a lease with Pima County, which entitles the Museum to exclusive right and use of the land and to operate the properties as a museum of natural history. The lease expires on September 30, 2028, with an option to renew for an additional 25 years under the same terms. Although the lease provides that the title to the Museum's property and exhibits is vested with the County, such assets are recorded on the books of the Museum to reflect the Museum's responsibility for management of these assets. The fair value of the leased premises has not been reported in the financial statements of the Museum.

Collections:

The collections, which were acquired through purchases and contributions since the Museum's inception, are not recognized as assets on the statement of financial position. Purchases of collection items are recorded as decreases in unrestricted net assets in the year in which the items are acquired, or as decreases in temporarily or permanently restricted net assets if the assets used to purchase the items are restricted by donors. Contributed collection items are not reflected in the financial statements. Proceeds from de-accessions or insurance recoveries are reflected as increases in the appropriate net asset classes.

Contributed services:

Contributed services are reported as contribution revenue and as assets or expenses only if the services create or enhance a non financial asset or:

- Would typically need to be purchased by the Museum if such services had not been contributed,
- Require specialized skills, and
- Are provided by individuals possessing those skills.

Many individuals volunteer their time and perform a variety of tasks that assist the Museum. During 2016, approximately 200 docents contributed over 77,000 hours in interpretive and educational programs on Museum grounds and in southern Arizona communities. In addition, over 500 other volunteers contributed approximately 65,000 hours in serving as clerical and library aides, greeters, botany and geology assistants, and in various other capacities. No amounts have been recorded in the financial statements for contributed services from docents and other volunteers as the criteria specified above were not met.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

1. Organization and summary of significant accounting policies (continued):

Fair value measurements:

Fair value is defined as the price to sell an asset or transfer a liability between market participants as of the measurement date. Fair value measurements assume the asset or liability is exchanged in an orderly manner; the exchange is in the principal market for that asset or liability (or in the most advantageous market when no principal market exists); and that the market participants are independent, knowledgeable, able and willing to transact an exchange. The provisions also clarify that the reporting entity's nonperformance risk (credit risk) should be considered in valuing liabilities.

Accounting standards establish a framework for measuring fair value by creating a hierarchy for observable independent market inputs and unobservable market assumptions and expands disclosures about fair value measurements. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). Considerable judgment is required in interpreting market data used to develop the estimates of fair value. Accordingly, the estimates presented in the financial statements are not necessarily indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions and estimation methodologies may have a material effect on the estimated fair value.

The Museum applies provisions for fair value measurements and disclosures related to certain alternative investments that permit the use of a qualifying investment's net asset value per share to estimate fair value.

Program expense allocations:

Expenses that can be identified with a specific program are charged directly to the program according to their natural expense classification. Costs incurred that share a common purpose are allocated to programs based upon their percentage of employees or square foot usage depending upon the nature of the expense.

Advertising:

Advertising costs are expensed as incurred. Total advertising expense was \$208,572 for 2016.

Tax exempt status:

The Museum is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. The Museum is also exempt from state income taxes. Accordingly, no provision is made for income taxes in the financial statements. Income from certain activities not directly related to the Museum's tax-exempt purpose, however, may be subject to taxation as unrelated business taxable income (UBTI). Management is not aware of any matters which would cause the Museum to jeopardize its tax-exempt status and there are no activities subject to UBTI.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

1. Organization and summary of significant accounting policies (continued):

Tax exempt status (continued):

GAAP requires management to perform an evaluation of all tax positions taken or expected to be taken in the course of preparing the Museum's tax returns to determine whether the tax positions meet a "more likely than not" standard of being sustained under examination by the applicable taxing authorities. This evaluation is required to be performed for all open tax years, as defined by the various statutes of limitations, for federal and state purposes.

The Museum is only subject to income taxes on UBTI as applicable. As a result, the Museum is required to file informational returns for federal and state purposes and, if it has UBTI, federal and state income tax returns. Management has performed its evaluation of tax positions taken on all open tax returns and has determined that there were no positions taken that do not meet the "more likely than not" standard.

From time to time, the Museum may be subject to penalties and interest assessed by various taxing authorities, which are classified as administration expenses, if they occur.

Subsequent events:

The Museum's management has evaluated the events that have occurred subsequent to September 30, 2016 through January 25, 2017, the date that the financial statements were available to be issued. Management has no responsibility to update these financial statements for events and circumstances occurring after this date.

2. Estates and pledges receivable:

The Museum accounts for contributions to be made in future years as unconditional promises in the year the promise is made. Long-term pledges receivable are discounted to their present value with rates ranging from 0.10% to 0.17%.

At September 30, 2016, the amounts receivable as a result of these promises are as follows:

<u>Year ending</u> <u>September 30,</u>	
2017	\$ 602,396
2018	24,500
2019	24,500
2020	<u>11,000</u>
	662,396
Less allowance for uncollectible pledges	-
Less unamortized discount to present value	<u>163</u>
	<u>\$ 662,233</u>

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

2. Estates and pledges receivable (continued):

Estates and pledges receivable are due from various private estates, foundations, businesses and individuals. Estates and pledges receivable from the Board of Trustees totaled \$90,089 as of September 30, 2016. Four donors comprised 84% of estates and pledges receivable at September 30, 2016.

3. Investments:

Investments carried at fair value are comprised of the following amounts at September 30, 2016:

Exchange traded funds	\$ 1,776,112
Money market funds and cash equivalents	103,172
Mutual funds	5,954,142
Strategy and private equity	<u>1,247,129</u>
	<u>\$ 9,080,555</u>

Net investment gain for the year ended September 30, 2016 is as follows:

Net realized gains on investments	\$ 48,660
Net unrealized gains on investments	<u>417,383</u>
	<u>\$ 466,043</u>

In addition to the resources set aside to fund capital and special projects, the Board of Trustees designated a portion of unrestricted net assets as a long-term reserve to serve a function similar to an endowment. The amount in the long-term reserve was \$3,585,098 at September 30, 2016.

4. Beneficial interest in perpetual trust:

The Museum is the beneficiary of the J. Benton Trust (the Trust). The Trust is a perpetual trust administered by a financial institution for the sole benefit of the Museum. Distributions from the Trust are restricted for the care of the Museum's animal collections. The unrealized gain on Trust assets for the year ended September 30, 2016 was \$3,533 and is included in net investment gain in the statement of activities. As of September 30, 2016, the trust assets had a value of \$130,057.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

5. Assets held in charitable trusts:

The Museum is the remainder beneficiary of an irrevocable trust agreement with a market value of \$671,246 as of September 30, 2016. The trust assets are held in money market accounts and U.S. treasury notes monitored by the trustee. Income earned on trust assets is paid to designated income beneficiaries in an amount not less than \$35,000 per year. Upon the death of the income beneficiaries, the Museum will receive the remaining value of the trust's assets. The value of the trust agreement is recorded in the accompanying financial statements based upon the estimated present value of the trust assets to be received by the Museum. The assets are discounted annually at 3.41% over a 13-year period, which represents the remaining life expectancy of the income beneficiaries. These assets had a value of \$415,178 as of September 30, 2016.

The discount rate on the Museum's interest in the above irrevocable trust agreement is based on the September 30, 2016 U.S. Treasury Bill rate corresponding to the estimated life expectancy of the trust beneficiaries.

6. Fair value measurements:

At September 30, 2016, the fair value of assets measured on a recurring basis is as follows:

	<u>Fair value</u>	<u>Quoted prices (level 1)</u>	<u>Significant other observable inputs (level 2)</u>	<u>Significant unobservable inputs (level 3)</u>
Exchange traded funds:				
Equity securities	\$ 657,838	\$ 657,838	\$ -	\$ -
Exchange traded notes	553,729	553,729	-	-
Fixed income securities	564,545	564,545	-	-
Mutual funds:				
Bond funds	3,167,483	3,167,483	-	-
Stock funds	2,786,659	2,786,659	-	-
Other funds	1,247,129	1,247,129	-	-
Money market funds and cash equivalents	<u>103,172</u>	<u>103,172</u>	<u>-</u>	<u>-</u>
Total investments	<u>9,080,555</u>	<u>9,080,555</u>	<u>-</u>	<u>-</u>
Beneficial interest in perpetual trust	130,057	-	130,057	-
Assets held in charitable trusts	<u>415,178</u>	<u>-</u>	<u>415,178</u>	<u>-</u>
	<u>\$ 9,625,790</u>	<u>\$ 9,080,555</u>	<u>\$ 545,235</u>	<u>\$ -</u>

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

6. Fair value measurements (continued):

The preceding table is based on the following hierarchy of observable independent market inputs and unobservable market assumptions:

Level 1 – Inputs represent unadjusted quoted prices for identical assets or liabilities exchanged in active markets.

Level 2 – Inputs include directly or indirectly observable inputs other than Level 1 inputs such as quoted prices for similar assets or liabilities exchanged in active or inactive markets; quoted prices for identical assets or liabilities exchanged in inactive markets; other inputs that are considered in fair value determinations of the assets or liabilities, such as interest rates and yield curves that are observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks and default rates; and inputs that are derived principally from or corroborated by observable market data.

Level 3 – Inputs include unobservable inputs used in the measurement of assets and liabilities. The Museum is required to use its own assumptions regarding unobservable inputs because there is little, if any, market activity in the assets or liabilities or related observable inputs that can be corroborated at the measurement date. Measurements of nonexchange traded derivative contract assets and liabilities are primarily based on valuation models, discounted cash flow models or other valuation techniques that are believed to be used by market participants. Unobservable inputs require the Museum to make certain projections and assumptions about the information that would be used by market participants in pricing assets or liabilities.

The investment's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

A reconciliation of assets measured at fair value on a recurring basis with the use of significant unobservable inputs (Level 3) from October 1, 2015 to September 30, 2016 is as follows:

	<u>Hedge fund</u>
Balance at October 1, 2015	\$ 664,274
Realized losses included in change in net assets	(13,873)
Sales	<u>(650,401)</u>
Balance at September 30, 2016	<u>\$ -</u>

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

6. Fair value measurements (continued):

The following is a description of the valuation methodologies used for assets measured at fair value:

The fair value of the Museum's exchange trade funds, mutual funds, and money market funds are valued at the closing price reported in the active market on which the individual securities are traded (Level 1), which represents the net asset value of shares held by the Museum at year end.

The fair value of the Museum's other funds, which consists of investments in Fidelity Absolute Access Fund 1 and Directional Access TEI Fund, are valued at the net asset value published on an exchange monthly (Level 1). Redemptions occur semi-annually at net asset value by contract.

The Museum invests in hedge funds. The Funds operated as a "Fund-of-Funds," investing, either directly or indirectly, in a group of funds or other pooled investment vehicles ("Sub-Funds") managed by investment advisers selected by the Fund's investment manager. The Funds seek to provide investors with exposure to alternative investment strategies by investing in diversified markets and instruments. Investments in Sub-Funds are valued at fair value, as determined by Fidelity Investments (Fidelity). In determining the fair value of each Sub-Fund, Fidelity will take into account the estimated net asset value of such Sub-Fund provided to the Funds by the Sub-Fund itself, as well as any other considerations that may, in Fidelity's judgment, increase or decrease such estimated value (Level 3). Accordingly, because of the inherent uncertainty of these valuations, these estimated values may differ significantly from the values that could have been used had a readily available market for the investments existed, and the differences could be material. Cash equivalents are valued at cost, which approximates fair value. The Funds charge various administrative and management fees as defined in the Fund administration agreements. The Sub-Fund investments are subject to various redemption restrictions with typical redemption notice periods ranging from five to 90 days. During 2016, the Museum liquidated its investment in the hedge funds.

7. Property and equipment:

	<u>Pima County</u>	<u>Museum</u>	<u>Total</u>
Land held for investment	\$ -	\$ 226,500	\$ 226,500
Buildings and improvements	34,402,795	-	34,402,795
Furniture, equipment and vehicles	-	2,974,367	2,974,367
Construction in progress	-	158,754	158,754
Total property and equipment	<u>34,402,795</u>	<u>3,359,621</u>	<u>37,762,416</u>
Less accumulated depreciation	<u>21,752,428</u>	<u>2,568,794</u>	<u>24,321,222</u>
Property and equipment, net	<u>\$ 12,650,367</u>	<u>\$ 790,827</u>	<u>\$13,441,194</u>

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

8. Collections:

The Museum's collections consist substantially of living and nonliving natural history objects related to the Museum's interpretive region (the Sonoran Desert and adjacent habitats). Collections are held for educational, research, scientific and curatorial purposes. With the exception of certain free-living organisms, collections are catalogued, preserved and cared for, and activities verifying their existence and assessing their condition are performed continuously.

Objects are de-accessioned according to their value and replaceability. Living plants and animals for which there is no foreseeable future need are donated to other accredited institutions. No significant collection items were de-accessioned during the year ended September 30, 2016.

9. Line of credit:

The Museum has entered into a one-year agreement with Northern Trust for a \$250,000 revolving line of credit (the "Agreement") through May 2017. The Agreement requires monthly interest only payments with any remaining principal balance due upon termination of the Agreement. Interest is calculated at the overnight LIBOR rate plus 2.75%. The overnight LIBOR rate at September 30, 2016 was 0.41989%. At September 30, 2016, there was no outstanding balance on the line. The line of credit is collateralized by a security interest in the Museum's general intangibles, accounts receivable and pledges receivable.

10. Capital leases payable:

The Museum leases equipment under capital leases having a cost of \$229,573 and accumulated amortization of \$190,126. Future minimum lease payments under the capitalized equipment leases as of September 30, 2016 is \$11,432, including interest of \$325, for the year ended September 30, 2017.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

11. Temporarily restricted net assets:

Temporarily restricted net assets were restricted for the following as of September 30, 2016:

Art Institute	\$ 216,794
Aquarium	12,904
Collections	135,464
Education	632,707
Facilities and exhibits	134,836
Other miscellaneous programs	258,443
Science	234,230
Time restrictions	550,178
	<u>\$ 2,175,556</u>

12. Permanently restricted net assets:

At September 30, 2016, permanently restricted net assets are restricted for investment in perpetuity, the income from which is expendable to support the following:

Animal care (perpetual trust)	\$ 130,057
Any museum activities	2,540,688
Art Institute	1,241,958
ASDM docent endowment	1,675
ASDM sustainability campaign	46,540
Earth Science	60,918
Education	55,892
Research	57,017
	<u>\$ 4,134,745</u>

13. Endowment and operating reserve:

The Museum's endowment and operating reserve consists of an individual fund established for a variety of purposes. The endowment includes both donor-restricted funds and as required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

13. Endowment and operating reserve (continued):

Interpretation of relevant law:

The Board of Trustees of the Museum has interpreted Arizona's version (titled the "Management of Charitable Funds Act" (the Act)) 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, 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 the Act.

Changes in endowment and operating reserves for the year ended September 30, 2016 are as follows:

	<u>Operating reserve</u>	<u>Donor temporarily restricted</u>	<u>Donor permanently restricted</u>	<u>Total</u>
Endowment and operating reserve, October 1, 2015	\$ 2,602,810	\$ 551,470	\$ 4,003,713	\$ 7,157,993
Investment return:				
Investment income	55,584	17,913	87,125	160,622
Net realized losses	(52,849)	(4,132)	(116,427)	(173,408)
Net unrealized gains (losses)	<u>223,137</u>	<u>(5,685)</u>	<u>431,040</u>	<u>648,492</u>
Total investment return	225,872	8,096	401,738	635,706
Contributions	481,463	-	9,568	491,031
Appropriation/transfer of assets for expenditures	(562,508)	-	(262,110)	(824,618)
Operating support provided from designated funds	25,000	-	-	25,000
Administrative fees and expenses	<u>(84,518)</u>	<u>(5,577)</u>	<u>(18,164)</u>	<u>(108,259)</u>
Endowment and operating reserve, September 30, 2016	<u>\$ 2,688,119</u>	<u>\$ 553,989</u>	<u>\$ 4,134,745</u>	<u>\$ 7,376,853</u>

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

13. Endowment and operating reserve (continued):

Funds with deficiencies:

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or the Act requires to retain as a fund of perpetual duration. In accordance with GAAP, such deficiencies are to be reported in unrestricted net assets. As of September 30, 2016, there were no deficiencies of this nature.

Return objectives and risk parameters:

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 or for a donor-specified period(s) as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the appropriate blended investment indexes while assuming a moderate level of investment risk. The Museum expects its endowment funds over time to provide an average real rate of return of approximately 5.5% annually. Actual returns in any given year may vary from this amount.

Strategies employed for achieving objectives:

To satisfy its long-term rate-of-return objectives, the Museum relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Museum targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending policy and how the investment objectives relate to spending policy:

The Museum has a policy of appropriating for distribution each year up to 5.5% of its permanently restricted endowment and board designated endowment funds' average fair value over the three fiscal year-ends preceding the fiscal year in which the distribution is planned. In establishing this policy, the Museum considered the long-term expected return on its endowment. Historically, the Museum has spent less than the 5.5%. This is consistent with the Museum's objective to maintain 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. Management of the Museum reports this as a transfer out.

14. Contingent rentals:

The Museum receives rent based upon a percentage of the gross sales from a gift shop and restaurant located on the Museum premises. Contingent rentals earned for the year ended September 30, 2016 totaled \$527,420 and are reported as concessions rental and museum food services.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2016

15. Retirement plan:

The Museum has established a voluntary retirement plan (the "Plan") under Section 403(b) of the Internal Revenue Code. Employees with 1,000 hours or more of annual service are eligible to participate in the Plan. Eligible employees may contribute to the Plan not to exceed statutory limits. Once an employee has completed two years of eligible service, the Museum matches employee contributions up to three percent of their annual compensation to the Plan. Participants may invest all contributions in any of several options offered by the Reliance Advisory Portfolio Collective Trusts managed by the StanCorp Investment Advisers, Inc. The Museum's contribution to the Plan for the year ended September 30, 2016 was \$80,230.

16. Functional expenses:

Program services	\$ 7,957,578
Supporting services	1,342,210
Fundraising	<u>654,347</u>
	<u>\$ 9,954,135</u>

17. Concentrations:

Substantially all nonmanagement employees of the Museum are subject to a three-year collective bargaining agreement with United Food and Commercial Workers Union Local 99 that expires on September 30, 2017.

18. Related party transactions:

During 2016, the Museum received approximately \$241,000 of cash contributions and \$8,000 of in-kind contributions from certain board members.

The Museum also paid approximately \$13,000 to the spouse of an employee for services performed and approximately \$30,000 to a company owned by an employee's spouse for services performed.

19. Contingencies:

From time to time, the Museum may be involved in legal proceedings in the ordinary course of business operations. In management's opinion, upon consultation with legal counsel, there is no current litigation that will materially affect the Museum's financial statements.

ARIZONA-SONORA DESERT MUSEUM, INC.

SCHEDULE OF FUNCTIONAL EXPENSES

YEAR ENDED SEPTEMBER 30, 2016

	Program services	Supporting services	Fundraising	Total expenses
Accounting fees	\$ 30,426	\$ 5,035	\$ 1,439	\$ 36,900
Advertising	43,651	160,641	4,280	208,572
Animal expense	321,412	-	-	321,412
Conferences, conventions and meetings	16,623	25,843	3,719	46,185
Depreciation and amortization	1,079,041	-	-	1,079,041
General insurance	92,910	8,343	206	101,459
Information technology	44,847	6,921	1,977	53,745
Legal fees	24,173	4,000	1,143	29,316
Maintenance and repair	156,306	-	-	156,306
Occupancy	424,273	879	-	425,152
Office expenses	408,602	32,099	163,351	604,052
Other employee benefits	577,730	96,100	43,485	717,315
Other expenses	287,566	31,319	25,655	344,540
Other fees for services	459,294	118,778	57,423	635,495
Payroll taxes	313,952	59,666	24,642	398,260
Pension plan contributions	56,437	17,708	6,085	80,230
Salaries and wages	3,561,024	774,296	320,768	4,656,088
Travel	59,311	582	174	60,067
	<u>\$ 7,957,578</u>	<u>\$ 1,342,210</u>	<u>\$ 654,347</u>	<u>\$ 9,954,135</u>