

Audited Financial Statements



JAPANESE AMERICAN NATIONAL MUSEUM

June 30, 2016 and 2015

Quigley & Miron

Suite 1660
3550 Wilshire Boulevard
Los Angeles, California 90010

Telephone: (213) 639-3550
Facsimile: (213) 639-3555

Suite 700
1999 South Bascom Avenue
Campbell, California 95008

Telephone: (408) 614-0100
Facsimile: (213) 639-3555

Independent Auditor's Report

Board of Trustees
Japanese American National Museum
Los Angeles, California

We have audited the accompanying financial statements of Japanese American National Museum (National Museum), a nonprofit organization, which comprise the statements of financial position as of June 30, 2016 and 2015, and the related statements of activities, functional expenses, 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 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

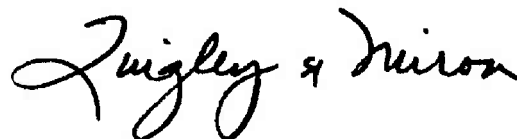
Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

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



**Japanese American National Museum
Statements of Financial Position
June 30, 2016 and 2015**

	<u>2016</u>	<u>2015</u>
Assets		
Cash and cash equivalents	\$ 722,798	\$ 1,854,489
Restricted cash: gift annuities	53,386	51,813
Inventories, net	371,369	408,641
Pledges and grants receivable, net—Note 2	389,472	604,225
Investments—Note 3	12,433,551	13,137,957
Land held for investment	36,000	36,000
Beneficial interest in split-interest arrangements—Note 4	1,851,873	2,165,991
Building and land lease—Note 6	8,015,905	8,078,594
Historic Building—Note 6	5,318,252	5,522,985
Other assets	268,315	206,999
Property and equipment, net—Note 7	21,059,720	21,604,483
Capitalized bond issuance costs, net	141,945	170,333
Artifact collection—Note 1		
Total Assets	<u>\$ 50,662,586</u>	<u>\$ 53,842,510</u>
Liabilities and Net Assets		
Liabilities		
Accounts payable and accrued expenses	\$ 636,005	\$ 740,776
Notes and bonds payable—Note 8	3,407,500	3,977,500
Gift annuities and planned giving liabilities	231,420	269,001
Total Liabilities	4,274,925	4,987,277
Net Assets		
Unrestricted	20,649,121	21,947,324
Temporarily restricted—Note 9	16,807,358	18,019,028
Permanently restricted—Note 10	8,931,182	8,888,881
Total Net Assets	<u>46,387,661</u>	<u>48,855,233</u>
Total Liabilities and Net Assets	<u>\$ 50,662,586</u>	<u>\$ 53,842,510</u>

See notes to financial statements.

**Japanese American National Museum
Statement of Activities
Year Ended June 30, 2016**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Support				
Contributions and grant income	\$ 1,134,846	\$ 422,792	\$ 42,347	\$ 1,599,985
Contribution of use of Historic Building and land	895,888			895,888
Valuation of beneficial interest in split-interest arrangements		(274,918)	(46)	(274,964)
Membership fees	649,672			649,672
Special events, net—Note 11	956,796			956,796
Revenue				
Admissions	226,842			226,842
Museum store, net of cost of goods sold of \$298,696	142,975			142,975
Dividend and interest income	14,764	406,987		421,751
Realized and unrealized gain on investments	31,609	(230,978)		(199,369)
Rental income	381,592			381,592
Other revenue	206,641			206,641
Total Support and Revenue Before Reclassifications	4,641,625	323,883	42,301	5,007,809
Reclassifications				
Net assets released from restrictions	1,535,553	(1,535,553)		
Total Support and Revenue After Reclassifications	6,177,178	(1,211,670)	42,301	5,007,809
Expenses				
Program services	5,569,612			5,569,612
Management and general	1,244,948			1,244,948
Fundraising and development	660,821			660,821
Total Expenses	7,475,381			7,475,381
Change in Net Assets	(1,298,203)	(1,211,670)	42,301	(2,467,572)
Net Assets at Beginning of Year	21,947,324	18,019,028	8,888,881	48,855,233
Net Assets at End of Year	\$ 20,649,121	\$ 16,807,358	\$ 8,931,182	\$ 46,387,661

See notes to financial statements.

**Japanese American National Museum
Statement of Activities
Year Ended June 30, 2015**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Support				
Contributions and grant income	\$ 1,640,811	\$ 732,661	\$ 20,000	\$ 2,393,472
Contribution of use of Historic Building and land	912,114			912,114
Valuation of beneficial interest in split-interest arrangements		(135,100)	59,306	(75,794)
Membership fees	825,141			825,141
Special events, net—Note 11	1,127,855			1,127,855
Revenue				
Admissions	1,145,233			1,145,233
Museum store, net of cost of goods sold of \$622,791	670,049			670,049
Dividend and interest income	68,851	304,431		373,282
Realized and unrealized gain on investments	56,598	27,389		83,987
Rental income	412,321			412,321
Other revenue	196,453			196,453
Total Support and Revenue Before Reclassifications	7,055,426	929,381	79,306	8,064,113
Reclassifications				
Net assets released from restrictions	1,367,933	(1,367,933)		
Total Support and Revenue After Reclassifications	8,423,359	(438,552)	79,306	8,064,113
Expenses				
Program services	5,978,925			5,978,925
Management and general	1,199,516			1,199,516
Fundraising and development	880,953			880,953
Total Expenses	8,059,394			8,059,394
Change in Net Assets	363,965	(438,552)	79,306	4,719
Net Assets at Beginning of Year	21,583,359	18,457,580	8,809,575	48,850,514
Net Assets at End of Year	<u>\$ 21,947,324</u>	<u>\$ 18,019,028</u>	<u>\$ 8,888,881</u>	<u>\$ 48,855,233</u>

See notes to financial statements.

**Japanese American National Museum
Statement of Functional Expenses
Year Ended June 30, 2016**

	Program Services	Management and General	Fundraising and Development	Total
Expenses				
Salaries	\$ 1,505,353	\$ 482,904	\$ 409,824	\$ 2,398,081
Payroll taxes	109,413	36,520	29,021	174,954
Other employee benefits	199,879	59,453	37,172	296,504
Total Personnel Expenses	1,814,645	578,877	476,017	2,869,539
Facility and parking rental	1,175,184	66,092	33,959	1,275,235
Contracted services	525,712	148,922	29,256	703,890
Depreciation	749,206	33,629	19,315	802,150
Utilities	363,416	13,365	10,728	387,509
Supplies, materials, and equipment	234,334	23,819	14,862	273,015
Professional fees	237,407	155,058	35,723	428,188
Postage and delivery	43,499	4,032	2,871	50,402
Travel, meetings, and memberships	126,933	73,596	14,605	215,134
Telephone	105,939	12,928	3,708	122,575
Insurance	57,028	48,064	1,435	106,527
Interest	57,086	20,634	1,472	79,192
Bank and merchant fees	26,952	35,887	7,003	69,842
Advertising	21,086	2,823	4,878	28,787
Taxes, licenses, permits, and fees	28,873	4,736	3,735	37,344
Other expenses	2,312	22,486	1,254	26,052
Total Expenses	\$ 5,569,612	\$ 1,244,948	\$ 660,821	\$ 7,475,381

See notes to financial statements.

**Japanese American National Museum
Statement of Functional Expenses
Year Ended June 30, 2015**

	Program Services	Management and General	Fundraising and Development	Total
Expenses				
Salaries	\$ 1,461,567	\$ 402,437	\$ 396,997	\$ 2,261,001
Payroll taxes	106,535	28,222	26,075	160,832
Other employee benefits	171,476	45,465	24,154	241,095
Total Personnel Expenses	1,739,578	476,124	447,226	2,662,928
Facility and parking rental	1,180,330	68,079	33,931	1,282,340
Contracted services	835,148	137,477	94,080	1,066,705
Depreciation	672,853	29,287	19,863	722,003
Utilities	393,614	20,961	11,620	426,195
Supplies, materials, and equipment	312,248	40,122	47,014	399,384
Professional fees	293,444	169,750	143,757	606,951
Postage and delivery	110,948	3,754	7,239	121,941
Travel, meetings, and memberships	101,237	88,680	32,296	222,213
Telephone	85,822	13,432	3,107	102,361
Insurance	76,162	57,186	2,009	135,357
Interest	69,145	11,118	2,041	82,304
Bank and merchant fees	66,103	29,837	28,300	124,240
Advertising	25,094	3,260	1,531	29,885
Taxes, licenses, permits, and fees	12,689	22,832	5,999	41,520
Other expenses	4,510	27,617	940	33,067
Total Expenses	\$ 5,978,925	\$ 1,199,516	\$ 880,953	\$ 8,059,394

See notes to financial statements.

Japanese American National Museum
Statements of Cash Flows
Years Ended June 30, 2016 and 2015

	<u>2016</u>	<u>2015</u>
Cash Flows from Operations		
Change in net assets	\$ (2,467,572)	\$ 4,719
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities		
Depreciation expense	802,150	722,003
Amortization of forgivable debt	(15,000)	(15,000)
Net realized and unrealized (gain) loss on investment	199,369	(83,987)
Valuation of swap agreement		(75,139)
Valuation of beneficial interest in split-interest arrangements	314,118	90,698
Permanently restricted contributions	(42,347)	(20,000)
Changes in operating assets and liabilities		
(Increase) decrease in restricted cash: gift annuities	(1,573)	6,628
(Increase) decrease in inventories, net	37,272	(216,558)
Decrease in pledges and grants receivable, net	214,753	6,766
Decrease in leased Historic Building and land lease	267,422	251,195
(Increase) decrease in other assets	(61,316)	151,729
Decrease in capitalized bond issuance costs, net	28,388	10,646
Increase (decrease) in accounts payable and accrued expenses	(104,771)	181,436
Decrease in other liabilities		(174,861)
Increase (decrease) in gift annuities and planned giving liabilities	(37,581)	16,629
Cash Provided by (Used in) Operating Activities	(866,688)	856,904
Cash Flows from Investing Activities		
Purchases of property and equipment	(257,387)	(450,209)
Purchases of investments in securities	(421,157)	(372,152)
Proceeds from sales of investments in securities	926,194	155,500
Cash Provided by (Used in) Investing Activities	247,650	(666,861)
Cash Flows from Financing Activities		
Permanently restricted contributions	42,347	20,000
Payment of bond principal	(555,000)	(540,000)
Cash Used in Financing Activities	(512,653)	(520,000)
Net Decrease in Cash	(1,131,691)	(329,957)
Cash at Beginning of Year	1,854,489	2,184,446
Cash at End of Year	\$ 722,798	\$ 1,854,489
Supplementary Disclosures		
Income taxes paid	<u>\$</u>	<u>\$</u>
Interest paid	<u>\$ 79,192</u>	<u>\$ 82,304</u>

See notes to financial statements.

Japanese American National Museum
Notes to Financial Statements
June 30, 2016 and 2015

Note 1—Organization and Summary of Significant Accounting Policies

Organization—The Japanese American National Museum (National Museum) is a California not-for-profit corporation, incorporated March 1, 1985 in the State of California. The mission of the National Museum is to promote understanding and appreciation of America's ethnic and cultural diversity by sharing the Japanese American experience. As the premier institution in its field, the National Museum houses the largest well-documented collection of Japanese American artifacts in the world. The National Museum sponsors ongoing exhibitions, lectures, workshops, educational programs, and related events at its Los Angeles headquarters. As a "museum without borders", the institution regularly presents exhibitions, public programs, and research projects in collaboration with Japanese American communities, other ethnic communities, and pre-eminent scholars, museums, and educational and cultural institutions around the globe. The National Museum is accredited by the American Association of Museums and is an affiliate of the Smithsonian Institution.

Artifact Collection—The National Museum's artifact collection is comprised of objects, photographs, home movies, books, manuscripts, works of art, and artifacts of historical significance that are held for educational and curatorial purposes. Each item is catalogued, preserved, and cared for, and activities verifying their existence and assessing their condition are performed continuously. The artifact collection, which was acquired primarily through contributions since the National Museum's inception, is not recognized as an asset on the statement of financial position. The National Museum's collection policies are consistent with the Code of Ethics for Museums adopted by the American Association of Museums.

Financial Statement Presentation—The financial statements of the National Museum have been prepared on the accrual basis of accounting, in conformity with Generally Accepted Accounting Principles in the United States of America (GAAP). The National Museum's net assets are classified based on the existence or absence of donor-imposed restrictions. As such, the net assets of the National Museum and changes therein are presented and reported as follows:

Unrestricted net assets—Net assets that are not subject to donor-imposed stipulations and that may be expendable for any purpose in carrying out the National Museum's mission.

Temporarily restricted net assets—Net assets subject to donor-imposed stipulations that may or will be met either by actions of the National Museum and/or the passage of time. As the restrictions are satisfied, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the accompanying statement of activities as net assets released from restrictions.

Permanently restricted net assets—Net assets subject to donor-imposed stipulations that resources be maintained in perpetuity. Investment income generated from these funds is available for general support of the National Museum's programs and operations unless otherwise stipulated by the donor.

Income Taxes—The Internal Revenue Service (IRS) has classified the National Museum as exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code, and the National Museum is exempt from California state income taxes from the Franchise Tax Board.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 1—Organization and Summary of Significant Accounting Policies—Continued

Accounting standards require an organization to evaluate its tax positions and provide for a liability for any positions that would not be considered 'more likely than not' to be upheld under a tax authority examination. Management has evaluated its tax positions and has concluded that a provision for a tax liability is not necessary at June 30, 2016 and 2015. Generally, the National Museum's information returns remain open for examination for a period of three (federal) or four (state of California) years from the date of filing.

Cash and Cash Equivalents—Cash and cash equivalents consist of cash on premises generated through the course of daily activities and cash on deposit with banks as well as money market funds or short-term investments held at financial institutions, with original maturities of three months or less from the date of purchase.

Restricted Cash: Gift Annuities—Restricted cash: gift annuities represents the National Museum's charitable gift annuity fund. The National Museum offers a charitable remainder annuities program for those who desire to donate. The National Museum's annuities are written under authority granted to it by the Insurance Commissioner of the State of California. Annuity assets are held by a custodian at fair value. All investments are in a money market fund. Payments are made from these assets to the annuity beneficiary in accordance with the contract.

Inventories—Inventories are stated at the lower of cost or market. Cost is determined under the first-in, first-out (FIFO) method. Inventories consist of sundry items such as books, gift items, cards and educational materials available through the National Museum's retail store. The National Museum's allowance for excess and obsolete inventory amounted to \$100,000 and \$46,000 at June 30, 2016 and 2015, respectively.

Concentration of Credit Risk—Cash and cash equivalents, investments in securities, and receivables are the primary form of concentration of credit risk to which the National Museum is subject. The National Museum places its cash and cash equivalents with high credit quality financial institutions where the funds are guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 per institution. Cash held in investment accounts at investment custodians are insured by the Securities Investors Protection Corporation (SIPC) up to \$250,000 and the investments in securities are insured up to \$500,000. At times, in the normal course of business, such cash balances are in excess of the FDIC/SIPC insurance limits, but management deems the risk of loss due to these concentrations to be minimal. Conservative investment guidelines established by the Board of Trustees (Board) govern the National Museum's investments in securities to achieve diversification of the portfolio.

During the year ended June 30, 2015, two donors contributed 20% and 17% of total contributions and grant income, respectively.

Allowance for Doubtful Accounts—An allowance for uncollectible amounts is determined using the age of the receivable, creditworthiness of parties and historical collection experience.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 1—Organization and Summary of Significant Accounting Policies—Continued

Fair Value of Financial Instruments—The fair value of the National Museum's financial instruments as of June 30, 2016 and 2015 represents management's best estimates of the amounts that would be received to sell those assets in an orderly transaction between market participants at that date. Those fair value measurements maximize the use of observable inputs. However, in situations where there are little, if any observable inputs, management's own judgments about the assumptions of market participants were used in pricing the asset. Those judgments are developed by management based on the best information available in the circumstances as further detailed in Note 5 to the financial statements.

Investments—Investments in securities are initially recorded at cost, if purchased, or fair market value, if received as a contribution. Subsequent to acquisition, investments in securities are reported at fair value. Investment income, gains and losses are reported as unrestricted income unless use of the earnings is restricted by the donor.

Land Held for Investment—Undeveloped land was donated in 1990 and was recorded at the estimated fair market value on the date of receipt. It is the intention of the National Museum to hold the land as a long-term investment. The property is carried at the lower of the value recorded at the date of receipt or net realizable value.

Beneficial Interest in Split-Interest Arrangements—The National Museum is the beneficiary under various charitable remainder trusts. The National Museum is the trustee of some of the irrevocable and revocable trusts; others are administered by third party trustees.

National Museum as Trustee—For irrevocable agreements, assets are included in the National Museum's beneficial interest in split-interest arrangements and stated at fair value. Contribution revenue is recognized at the date each trust is established after recording liabilities for the actuarially-determined present value of the estimated future payments to be made to the beneficiaries. The actuarial liability is based on the present value of the future payments discounted at the appropriate risk-free rate at the inception of each agreement and the applicable mortality tables.

Liabilities are adjusted during the terms of the trust for changes in the fair value of the assets, accretion of discounts, and other changes in the estimates of future benefits. Actuarial liabilities totaled \$231,420 and \$206,152 at June 30, 2016 and 2015, respectively, and are included in gift annuities and planned giving liabilities in the statement of financial position. The Annuity 2000 Mortality Table was used for both of the years ended June 30, 2016 and 2015.

Assets held by others—The National Museum is the beneficiary of charitable remainder trusts held and administered by others. The present value of the estimated future cash flows from these trusts approximates the value of the underlying assets and is included in beneficial interest in split-interest arrangements in the statement of financial position. Contribution revenues are recognized at the date the trusts are established.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 1—Organization and Summary of Significant Accounting Policies—Continued

Property and Equipment—Purchased property and equipment are recorded at cost, and donated assets are recorded at the estimated fair value on the date of receipt. The National Museum depreciates its property and equipment using the straight-line-method over the following estimated useful lives:

Furniture, fixtures and equipment	3-10 years
Building improvements	10-20 years
Buildings	55 years
Exhibition and media development costs	5-10 years

Repairs and maintenance costs are expensed as incurred. Gifts of long-lived assets with explicit restrictions as to how the assets are to be used and gifts of cash or other assets that must be used to acquire and maintain long-lived assets are reported as restricted support. Absent explicit donor stipulations, the National Museum reports expirations of donor restrictions when such long-lived assets are placed in service.

Capitalized Bond Issuance Costs—Bond discount and issuance costs are amortized as additional interest expense based on the terms of the bond using the straight-line method, which approximates the effective interest method.

Revenue Recognition—The National Museum's revenue recognition policies are as follows:

Contributions—Contributions are reported as support in the period received and as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expiration of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as net assets released from restrictions in the accompanying statement of activities. Contributions whose restrictions are met in the same year as the contribution is made are initially classified as temporarily restricted net assets. Amounts expected to be collected beyond one year are recorded at the present value of estimated future cash flows. Management determined an appropriate interest rate based on historical risk-free interest adjusted for determined risk. The amortization of the discount is included in support.

Grants and contracts—Revenues from grants and contracts are reported as increases in unrestricted net assets as allowable expenditures under such agreements are incurred. The amounts expended in excess of reimbursements are reported as grants receivable.

Membership fees—Membership fees are recognized as revenue when such income is received.

Admissions—Revenues from service revenue are recognized at the time services are provided.

Auxiliary enterprises—Revenues from supporting services, such as the National Museum gift shop are recorded at the time of delivery of a product or service.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 1—Organization and Summary of Significant Accounting Policies—Continued

Investment gain (loss)—Investment transactions are recorded on the trade date. Investment income and realized and unrealized gains and losses, net of investment management fees, are reported as increases or decreases in the appropriate net asset category.

Rental Income—Rental income consists of facilities rental fees earned from unrelated third parties including retail vendors, film production companies, and individuals. Rental income is recognized upon the occurrence of the events for which the facilities were rented.

Benefits Provided to Donors at Special Events—The National Museum conducts special fundraising events in which a portion of the gross proceeds paid by the participants represents payment for the direct cost of the benefits received by participants at the event. The National Museum values benefits, primarily the meals and entertainment, at the actual cost.

Contributed Services—A substantial number of unpaid volunteers have made significant contributions of their time and services to further the National Museum’s mission. During the years ended June 30, 2016 and 2015, these in-kind contributions amounted to over 28,000 and 29,000 volunteer hours valued at approximately \$560,000 and \$580,000, respectively. These amounts are not reflected in these financial statements as the recognition criteria under GAAP were not met.

Functional Expenses—The costs of providing the various program and supporting activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been directly charged to the program services and supporting services benefitted. Indirect costs are allocated between program services, management and general, and fundraising expenses, based on an analysis of personnel time utilized for the related activities.

Use of Estimates—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications—Certain amounts in 2015 have been reclassified to conform with the 2016 financial statement presentation.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 2—Pledges and Grants Receivable, Net

Net pledges and grants receivable at June 30, 2016 and 2015 consist of:

	<u>2016</u>	<u>2015</u>
Due within 1 year	\$ 306,172	\$ 405,900
Due within 2 to 5 years	87,500	208,325
	Gross	614,225
	393,672	614,225
Less present value discount	(4,200)	(10,000)
	Net	604,225
	\$ 389,472	\$ 604,225

The present value of estimated future cash flows on unconditional promises to give was determined using a discount rate of 5% for the years ended June 30, 2016 and 2015.

Note 3—Investments

Investments consist of the following as of June 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Fixed income funds	\$ 6,426,794	\$ 6,319,662
Domestic equity funds	5,131,518	5,849,385
International equity fund	875,239	968,910
	Totals	13,137,957
	\$ 12,433,551	\$ 13,137,957

Return on investments for the years ended June 30, 2016 and 2015 is as follows:

	<u>2016</u>	<u>2015</u>
Realized loss on investments	\$ (20,435)	\$ (2,186)
Unrealized gain (loss) on investments	(178,934)	86,173
	Realized and Unrealized Gain (Loss)	83,987
	(199,369)	83,987
Investment interest and dividends	421,157	372,152
	Return on Investments, Net	456,139
	\$ 221,788	\$ 456,139

Japanese American National Museum
Notes to Financial Statements—Continued

Note 4—Beneficial Interest in Split-Interest Arrangements

Beneficial interest in split-interest arrangements, by trustee, consists of the following:

	<u>National Museum</u>	<u>Others</u>	<u>Total</u>
Beneficial Interest in Split-Interest Arrangements at July 1, 2014	\$ 581,405	\$ 1,675,284	\$ 2,256,689
Contributions	359,932		359,932
Termination of agreements	(398,092)		(398,092)
Amortization of discount, payments to income beneficiaries, and income	93,397	(145,935)	(52,538)
Beneficial Interest in Split-Interest Arrangements at June 30, 2015	636,642	1,529,349	2,165,991
Amortization of discount, payments to income beneficiaries, and income	(29,562)	(284,556)	(314,118)
Beneficial Interest in Split-Interest Arrangements at June 30, 2016	<u>\$ 607,080</u>	<u>\$ 1,244,793</u>	<u>\$ 1,851,873</u>

Payout rates ranged between 5% and 9.2% for those assets held by the National Museum and 6.5% and 8% for assets held by others.

The National Museum used a discount rate under Internal Revenue Code section 7520(a) of 2.2% to value all trust assets as of June 30, 2016 and 2015. Included with charitable remainder trusts is real property. Real property market value was \$180,000 as of June 30, 2016 and 2015. The remaining assets are invested in various institutional trust funds for which the underlying assets are generally traded in public or private markets and are reported at fair value. The charitable remainder trust amounts include vested and non-vested trusts, of which only the vested portions are recognized by the National Museum.

Note 5—Fair Value

Accounting standards have established a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. This 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 measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets that the entity has the ability to access at the measurement date. The National Museum's Level 1 assets consist of common stock and domestic, international, and fixed income mutual funds.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 5—Fair Value—Continued

Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the assets, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other observable inputs that can be corroborated by observable market data. The National Museum has no Level 2 assets or liabilities.

Level 3 inputs are unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset or liability. The National Museum's Level 3 assets include beneficial interests in split-interest arrangements, and assets and liabilities related to its gift annuities.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest level input that is significant to the fair value measurement in its entirety. Assets and liabilities measured at fair value on a recurring basis at June 30, 2016 consist of the following:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Fair Value</u>
June 30, 2016:				
Investments	\$ 12,433,551	\$	\$	\$ 12,433,551
Split-interest arrangements			1,851,873	1,851,873
Planned giving liabilities			(170,921)	(170,921)
Gift annuities—assets	53,386			53,386
Gift annuities—liabilities			(60,499)	(60,499)
Totals	<u>\$ 12,486,937</u>	<u>\$</u>	<u>\$ 1,620,453</u>	<u>\$ 14,107,390</u>

Assets and liabilities measured at fair value on a recurring basis at June 30, 2015 consist of the following:

June 30, 2015:				
Investments	\$ 13,137,957	\$	\$	\$ 13,137,957
Split-interest arrangements			2,165,991	2,165,991
Planned giving liabilities			(206,153)	(206,153)
Gift annuities—assets	51,813			51,813
Gift annuities—liabilities			(62,848)	(62,848)
Totals	<u>\$ 13,189,770</u>	<u>\$</u>	<u>\$ 1,896,990</u>	<u>\$ 15,086,760</u>

A reconciliation of the National Museum's Level 3 assets and liabilities is as follows:

	<u>2016</u>	<u>2015</u>
Beginning balance	\$ 1,896,990	\$ 2,004,317
New split-interest arrangements		359,932
Maturities of split-interest arrangements		(398,092)
Change in value of split-interest arrangements	(276,537)	(69,167)
Ending Balance	<u>\$ 1,620,453</u>	<u>\$ 1,896,990</u>

Japanese American National Museum
Notes to Financial Statements—Continued

Note 6—Historic Building and Land Leases

In February 1987, the National Museum entered into a 50-year lease at \$1 per year with the City of Los Angeles for the use of land and a 33,000 square foot building (Historic Building). The National Museum restored the facility and opened it to the public in May 1992. In February 1997, the original lease was superseded by a new 55-year lease with the City of Los Angeles for the same property, as well as three adjacent parcels of land, the largest of which is the site of an 85,000 square foot expansion pavilion, which opened to the public in January 1999. In 2002, the lease was amended to provide an additional 5,000 square feet for use by the National Museum. The present value of the building and land lease is \$8,015,905 and \$8,078,594 as of June 30, 2016 and 2015, respectively, based on an annual estimated lease expense of \$594,060 and a discount rate of 6.6%.

The Historic Building was expanded and renovated to support the National Center for the Preservation of Democracy (National Center) with a \$20 million federal grant awarded in 2001. The construction was completed and the National Center was opened in October 2005. The federal government retains a reversionary interest in the building costs purchased under the grant. As such, the building costs paid with the funds received from the grant are not recorded on the National Museum's financial statements. However, the National Museum has been allowed to use the building rent-free. Accordingly, the National Museum initially recorded the present value of the building rent of \$6,881,032 as a historic building on the statement of financial position and as corresponding temporarily restricted contributions in the statement of activities for the year ended June 30, 2007, based upon an estimated annual rent expense of \$569,250 and a discount rate of 6.6%. A rent period of 25 years was used, approximating the estimated useful life of the building, as there is no definitive time restriction for the National Museum's use of the building under the grant. The present value of the Historic Building was \$5,318,252 and \$5,522,985 as of June 30, 2016 and 2015, respectively.

Note 7—Property and Equipment, Net

The major classes of property and equipment, net at June 30, 2016 and 2015 are as follows:

	<u>2016</u>	<u>2015</u>
Museum building	\$ 30,118,137	\$ 30,118,137
Furniture, fixtures, and equipment	2,919,156	2,661,769
Exhibition and media development costs	1,812,221	1,812,221
Historic Building improvements	1,487,643	1,487,643
Museum building improvements	254,348	254,348
	<u>36,591,505</u>	<u>36,334,118</u>
Less accumulated depreciation	(15,531,785)	(14,729,635)
	<u><u>Net \$ 21,059,720</u></u>	<u><u>\$ 21,604,483</u></u>

Total depreciation expense recorded for the years ended June 30, 2016 and 2015 was \$802,150 and \$722,003, respectively.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 8—Notes and Bonds Payable

Notes and bonds payable as of June 30, 2016 and 2015 are as follows:

	<u>2016</u>	<u>2015</u>
California Statewide Communities Development Authority Variable Rate Demand Revenue Bonds, Series 2000A, maturing August 1, 2030. Secured by the full faith and credit of the National Museum, a lien on gross revenues, and a pledge of real property and endowment assets. The National Museum was in compliance with required financial covenants.	\$ 3,370,000	\$ 3,925,000
Noninterest-bearing note payable to the Community Redevelopment Agency of the City of Los Angeles (CRA) with \$15,000 of principal balance forgiven each year.	37,500	52,500
\$500,000 line of credit from a bank, bearing interest at variable rates (5% at June 30, 2016), maturing on December 31, 2016.		
Totals	<u>\$ 3,407,500</u>	<u>\$ 3,977,500</u>

On June 15, 2000, the California Statewide Communities Development Authority (Issuer) sold \$10,000,000 of Variable Rate Demand Revenue Bonds (Japanese American National Museum), Series 2000A (Bonds). The proceeds were loaned by the Issuer to the National Museum pursuant to a loan agreement and were used to (a) repay and retire an existing five-year term loan provided by a group of banks and (b) to pay a portion of costs of issuance of the bonds. The bonds have a variable interest rate which is reset weekly. The effective rate was 1.48% for the years ended June 30, 2016 and 2015, respectively.

The aggregate future maturities of notes payable and bonds payable are as follows:

<u>For the Year Ending June 30,</u>		
2017		\$ 345,000
2018		360,000
2019		367,500
2020		380,000
2021		395,000
Thereafter		<u>1,560,000</u>
	Total	<u>\$ 3,407,500</u>

Japanese American National Museum
Notes to Financial Statements—Continued

Note 9—Temporarily Restricted Net Assets

The National Museum's temporarily restricted net assets as of June 30, 2016 and 2015 consist of the following:

	<u>2016</u>	<u>2015</u>
Building and land lease	\$ 8,015,905	\$ 8,078,594
Historic Building	5,318,252	5,522,985
Exhibitions, education, public programs and research	526,573	2,104,842
Charitable remainder trusts and gift annuities	1,433,464	1,708,382
Grants and contributions pledged for future periods	1,513,164	604,225
Totals	<u>\$ 16,807,358</u>	<u>\$ 18,019,028</u>

Note 10—Permanently Restricted Net Assets

The National Museum's endowment consists of its beneficial interest in split-interest agreements held by others, and one investment fund and four unified pools of investments managed by the National Museum established to support its operations and programs. The endowment comprises donor-restricted endowment funds only and, as of June 30, 2016 and 2015, there were no funds designated by the Board to function as endowments. As required by GAAP, net assets associated with the endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

In January 1, 2009, the State of California adopted the Uniform Prudent Management of Institutional Funds Act (UPMIFA). UPMIFA requires 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. The Board is aware that there is an implicit understanding that the market value of the donor-restricted endowment may, from time to time, fall below the fair value of the original gift as of the gift date due to market conditions or continued prudent expenditures by the Board of certain amounts of the endowment. If such a temporary deficit condition occurred, the Board would take all prudent steps, given ongoing market conditions, to restore the fair value of the fund to an amount at or above the amount of the original gift.

The National 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 National Museum in a manner consistent with the standard of prudence prescribed by UPMIFA.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 10—Permanently Restricted Net Assets—Continued

In accordance with UPMIFA, the National Museum considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- 1) The duration and preservation of the fund
- 2) The purposes of the National Museum and the donor-restricted endowment fund
- 3) General economic conditions
- 4) The possible effect of inflation and deflation
- 5) The expected total return from income and the appreciation of investments
- 6) Other resources of the National Museum
- 7) The investment policies of the National Museum

Return Objectives and Risk Parameters—It is the purpose of the National Museum's endowment fund to secure the future of the National Museum and to support its programs and operations as designated by the Board.

The primary long-term financial objective is to preserve and enhance the real (i.e., inflation-adjusted) purchasing power of the endowment through a prudent long-term investment strategy. This objective should be achieved over rolling three-, five-, and ten-year periods on a total return basis. An additional objective is to provide a relatively predictable, stable, and (in real terms) constant stream of current income for the National Museum's annual operating needs.

The primary investment objective of the endowment is to earn an average annual minimum nominal return of 8% per year and a real total return of at least 5% per year, net of management fees, over the long-term (rolling three-, five- and ten-year periods). The National Museum considers itself a risk-averse investor. That is, among various investment alternatives with comparable expected returns, the preference is for those having the lowest risk.

Strategies Employed for Achieving Objectives—The National Museum manages its endowment on a total rate of return basis consisting of dividends, interest, and any net increase / decrease in market value of securities for the fiscal year, not favoring returns from one source over another.

The National Museum has determined that marketable debt and equity securities traded in the United States are appropriate investments consistent with its return objectives and risk parameters. Cash invested in money market accounts is also an acceptable investment within these guidelines. The investment portfolio is to be sufficiently balanced so that no single security or class of securities will have a disproportionate impact on the risk of the total portfolio.

Spending Policy and How the Investment Objectives Relate to Spending Policy—The National Museum has a policy governing the amount of endowment earnings that can be released annually for spending, consistent with the restrictions, if any, placed on the endowment by donors. The spending policy authorizes an annual distribution equal to 5% of the average market value of the portfolios as of the preceding 20 calendar quarters, subject to the requirement that the portfolios increase by an inflation factor annually.

Japanese American National Museum
Notes to Financial Statements—Continued

Note 10—Permanently Restricted Net Assets—Continued

In establishing this policy, the National Museum considered the long-term expected return on its endowment. Accordingly, over the long term, the National Museum expects the current spending policy to allow its endowment to grow at an amount that will at least keep pace with expected inflation.

Summary of Endowment Fund Balances and Activity—Endowment net asset composition by donor-imposed stipulations for the years ended June 30, 2016 and 2015 is as follows:

	<u>2016</u>	<u>2015</u>
Nikkei Legacy program	\$ 3,000,000	\$ 3,000,000
Artistic programs	2,811,665	2,811,711
General operating purposes	2,119,517	2,077,170
Humanities programs	1,000,000	1,000,000
Totals	\$ 8,931,182	\$ 8,888,881

Change in endowment net assets for the year ended June 30, 2016 and 2015 consists of:

	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment Net Assets at June 30, 2014	\$ 1,657,293	\$ 8,809,575	\$ 10,466,868
Investment income	304,431		304,431
Change in value of split-interest agreements		59,306	59,306
Realized and unrealized gain on investments, net	27,389		27,389
Total Investment Return	331,820	59,306	391,126
Contributions		20,000	20,000
Appropriation of expenditure	(525,006)		(525,006)
Endowment Net Assets at June 30, 2015	1,464,107	8,888,881	10,352,988
Investment income	406,987		406,987
Change in value of split-interest agreements		(46)	(46)
Realized and unrealized loss on investments, net	(230,978)		(230,978)
Total Investment Return	176,009	(46)	175,963
Contributions		42,347	42,347
Appropriation of expenditure	(518,623)		(518,623)
Endowment Net Assets at June 30, 2016	\$ 1,121,493	\$ 8,931,182	\$ 10,052,675

Japanese American National Museum
Notes to Financial Statements—Continued

Note 11—Special Events

Special events during the years ended June 30, 2016 and 2015 represent activities related to the annual gala event and are summarized as follows:

	<u>2016</u>	<u>2015</u>
Revenue	\$ 1,281,101	\$ 1,378,129
Less direct expenses	<u>(324,305)</u>	<u>(250,274)</u>
Net	<u>\$ 956,796</u>	<u>\$ 1,127,855</u>

Total fundraising expenses for the years ended June 30, 2016 and 2015 consist of the following:

	<u>2016</u>	<u>2015</u>
Fundraising expenses per statement of functional expenses	\$ 660,821	\$ 880,953
Special event expenses	<u>324,305</u>	<u>250,274</u>
Totals	<u>\$ 985,126</u>	<u>\$ 1,131,227</u>

Note 12—Employee Benefit Plan

The National Museum has a defined contribution retirement plan covering substantially all of its employees. The Board annually determines the amount to be contributed to the plan. Participants are fully vested after five years of service. The National Museum made contributions of \$14,565 and \$16,806 to the plan during the years ended June 30, 2016 and 2015, respectively.

Note 13—Subsequent Events

Management evaluated all activities of Japanese American National Museum through October 28, 2016, which is the date the financial statements were available to be issued, and concluded that no other material subsequent events have occurred that would require adjustment to the financial statements or disclosure in the notes to the financial statements.