

**The Museum of Art and History
at the McPherson Center**

(A California Public Benefit Corporation)

Financial Statements

June 30, 2021



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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
The Museum of Art and History
at the McPherson Center
Santa Cruz, California

We have audited the accompanying financial statements of The Museum of Art and History at the McPherson Center ("MAH," A California Public Benefit Corporation), which comprise the statement of financial position as of June 30, 2021, and the related statements of activities and changes in net assets, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Museum of Art and History at the McPherson Center as of June 30, 2021, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

Change in Accounting Principle

As discussed in Note 2 to the consolidated financial statements the Company adopted Accounting Standards Codification ("ASC") 606, Revenue from Contracts with Customers. The MAH adopted the standard for its annual reporting period beginning July 1, 2020. Our opinion is not modified with respect to this matter.



Armanino^{LLP}
San Jose, California

December 2, 2021

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Statement of Financial Position
June 30, 2021

ASSETS

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Current assets			
Cash and cash equivalents	\$ 767,637	\$ 178,562	\$ 946,199
Accounts and grants receivable	798	142,500	143,298
Rents and trash district fees receivable, net of allowance for doubtful accounts of \$-0-	48,439	-	48,439
Prepaid expenses	129,104	-	129,104
Inventories	<u>35,336</u>	<u>-</u>	<u>35,336</u>
 Total current assets	 <u>981,314</u>	 <u>321,062</u>	 <u>1,302,376</u>
 Property, equipment, and improvements, net	 <u>5,208,104</u>	 <u>-</u>	 <u>5,208,104</u>
Other assets			
Investments	-	450,224	450,224
Unemployment insurance reserve	4,486	-	4,486
Straight-line rent receivable	56,025	-	56,025
Beneficial interest in assets held by Community Foundation of Santa Cruz County	<u>55,874</u>	<u>-</u>	<u>55,874</u>
 Total other assets	 <u>116,385</u>	 <u>450,224</u>	 <u>566,609</u>
 Total assets	 <u>\$ 6,305,803</u>	 <u>\$ 771,286</u>	 <u>\$ 7,077,089</u>

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

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Statement of Financial Position (continued)
June 30, 2021

LIABILITIES AND NET ASSETS

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Current liabilities			
Current portion - note payable	\$ 130,675	\$ -	\$ 130,675
Refundable advance, Paycheck Protection Program	68,928	-	68,928
Accounts payable	131,002	-	131,002
Tenant and facilities rental deposits	28,125	-	28,125
Deferred revenue	90,903	-	90,903
Accrued personal time off	56,480	-	56,480
	<u>506,113</u>	<u>-</u>	<u>506,113</u>
Total current liabilities			
Non-current liabilities			
Note payable	135,988	-	135,988
	<u>642,101</u>	<u>-</u>	<u>642,101</u>
Total liabilities			
Net assets			
Without donor restrictions			
Undesignated	297,616	-	297,616
Invested in property and equipment, net of related debt	4,941,441	-	4,941,441
Board designated - operating reserve	200,000	-	200,000
Board designated - facilities reserve	201,075	-	201,075
Board designated - publications fund	23,570	-	23,570
Total net assets without donor restrictions	<u>5,663,702</u>	<u>-</u>	<u>5,663,702</u>
With donor restrictions			
Time and use restricted	-	538,215	538,215
Donor-restricted endowment	-	233,071	233,071
Total net assets with donor restrictions	<u>-</u>	<u>771,286</u>	<u>771,286</u>
	<u>5,663,702</u>	<u>771,286</u>	<u>6,434,988</u>
Total net assets			
Total liabilities and net assets	<u>\$ 6,305,803</u>	<u>\$ 771,286</u>	<u>\$ 7,077,089</u>

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

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Statement of Activities and Changes in Net Assets
For the Year Ended June 30, 2021

	Without Donor Restrictions	With Donor Restrictions	Total
Revenue and other support			
Contributions and grants	\$ 259,293	\$ 160,000	\$ 419,293
Contributions Paycheck Protection Program	233,540	-	233,540
Contracts Santa Cruz County historic preservation	139,135	-	139,135
Memberships	84,883	-	84,883
Museum admissions	6,721	-	6,721
Program service fees	945	-	945
Museum store sales, net of direct costs	2,875	-	2,875
Interest and dividend income	576	8,142	8,718
Realized and unrealized gains on investments, net of investment expenses	11,487	73,844	85,331
Net assets released from restrictions	200,832	(200,832)	-
Total revenue and other support	940,287	41,154	981,441
Other income			
McPherson Center rental and trash service	835,864	-	835,864
Expenses related to rents and trash service	(447,052)	-	(447,052)
Total other income	388,812	-	388,812
Total revenue, support and other income	1,329,099	41,154	1,370,253
Expenses			
Program services			
Art and History Museum	1,038,082	-	1,038,082
Supporting services			
Management and general	505,930	-	505,930
Development	298,808	-	298,808
Total supporting services expenses	1,842,820	-	1,842,820
Change in net assets	(513,721)	41,154	(472,567)
Net assets, beginning of year	6,177,423	730,132	6,907,555
Net assets, end of year	\$ 5,663,702	\$ 771,286	\$ 6,434,988

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

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Statement of Functional Expenses
For the Year Ended June 30, 2021

	Program Services	Management and General	Development	McPherson Center	Total
Personnel	\$ 533,007	\$ 382,964	\$ 222,760	\$ 51,600	\$ 1,190,331
Professional services	29,483	48,771	53,315	-	131,569
Administration and facility	85,739	61,513	139	218,785	366,176
Insurance	21,811	9,415	-	15,795	47,021
Interest expense	-	-	-	13,689	13,689
Marketing and promotion	9,567	100	6,141	-	15,808
Property taxes	-	-	-	48,056	48,056
Fundraising and memberships	917	-	11,228	-	12,145
Exhibitions and collections	79,196	-	-	-	79,196
Programs	22,295	-	2,761	-	25,056
Other expenses	3,961	703	-	-	4,664
Depreciation	252,106	2,464	2,464	131,627	388,661
Bad debt recovery	-	-	-	(32,500)	(32,500)
	<u>1,038,082</u>	<u>505,930</u>	<u>298,808</u>	<u>447,052</u>	<u>2,289,872</u>
Less expenses included with other income as expenses related to rents	-	-	-	(447,052)	(447,052)
Plus expenses included with revenue and other support					
Museum store sales cost of goods sold	-	-	-	-	3,514
	<u>\$ 1,038,082</u>	<u>\$ 505,930</u>	<u>\$ 298,808</u>	<u>\$ -</u>	<u>\$ 1,846,334</u>

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

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Statement of Cash Flows
For the Year Ended June 30, 2021

Cash flows from operating activities	
Change in net assets	\$ (472,567)
Adjustments to reconcile change in net assets to net cash used in operating activities	
Depreciation	388,661
Realized and unrealized gains on investments	(85,331)
Straight-line rental income	19,869
Change in assets and liabilities	
Accounts and grants receivable	132,026
Rents and trash district fees receivable	2,743
Prepaid expenses	(116,994)
Inventories	6,720
Unemployment insurance reserve	(2,920)
Accounts payable	88,928
Refundable advance, Paycheck Protection Program	(12,970)
Deferred revenue	22,004
Accrued personal time off	<u>11,976</u>
Cash used in operating activities	<u>(17,855)</u>
Cash flows from investing activities	
Proceeds from investments - distributions from community foundation	1,856
Proceeds from sale of investments	55,416
Purchase of investments	(63,558)
Purchase of property, equipment, and improvements	<u>(66,389)</u>
Cash used in investing activities	<u>(72,675)</u>
Cash flows from financing activities	
Principal payments on debt	<u>(125,337)</u>
Cash used in financing activities	<u>(125,337)</u>
Net decrease in cash, cash equivalents, and restricted cash	(215,867)
Cash, cash equivalents, and restricted cash at beginning of year	<u>1,162,066</u>
Cash, cash equivalents, and restricted cash at end of year	<u>\$ 946,199</u>
<u>Supplemental disclosure of cash flow information</u>	
Interest paid	<u>\$ 13,689</u>

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

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

1. General Information

The Museum of Art and History at the McPherson Center ("MAH") is a nonprofit organization, incorporated as A California Public Benefit Corporation, that operates under the direction of its Board of Trustees ("Board"). The MAH's objectives and purposes include exploring diverse cultural ideas, issues and perspectives through artistic experience and regional history. Dedicated to excellence, the MAH provides accessible programs, exhibits, resources and services for exploration, education and research; collection and preservation of works of art and regional historic resources; and development and maintenance of public awareness and appreciation.

The MAH receives a substantial amount of support from donations from individuals and businesses located in Santa Cruz County, which is affected by the local economy. Additional sources of revenue include grants from foundations and a contract with the County of Santa Cruz.

Included in the financial statements is the activity of the History Forum, a supporting organization. The income from that organization provides additional sources of funding for the MAH.

The McPherson Center consists of two components: 1) Museum building, housing the exhibition and administrative offices of The Museum of Art and History, and 2) Office/Retail Building, containing approximately 23,873 square feet of office and retail space.

The initial funding mix for the project consisted of the following:

Economic Development Administration of The United States - Economic Adjustment Assistance Award in the amount of \$1,920,000 and California Department of Commerce local match of \$640,000.

Capital lease from Santa Cruz County in the amount of \$2,255,000 at an annual interest rate of 7.1 percent.

Major Fundraising Campaign - The predecessors, the Art Museum of Santa Cruz County and the History Museum of Santa Cruz County, under their joint venture agreement, raised \$3,590,006 toward the project.

Significant Standing Committees of the Board responsible for overseeing certain aspects of the MAH are: 1) Executive Committee, assuring continuity of organizational decision-making between Board meetings; 2) Finance Committee, reviewing financial matters including budgets, financial reports, and investments and investment policy; 3) Audit Committee, overseeing material aspects of the organization's financial reporting, internal controls, risk management, and compliance; 4) Development Committee, exploring and developing strategies for financial resources to cover operating and capital funding goals. Other Standing Committees oversee aspects of the work related to Nominating & Governance, Strategic Planning, and Diversity, Equity, Inclusion and Accessibility (DEIA).

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

2. Summary of Significant Accounting Policies

Financial statement presentation

The financial statements are presented on the accrual basis of accounting and in conformity with accounting principles generally accepted in the United States of America applicable to not-for-profit organizations. Revenues are reported as increases in net assets without donor restrictions unless there are donor-imposed purposes and/or time restrictions on the gifted assets. Expenses are reported as decreases in net assets without donor restrictions. Gains or losses on investments and other assets or liabilities are reported as increases or decreases in net assets without donor restrictions unless their use is restricted by explicit donor stipulation.

Change in Accounting Principles

The MAH adopted the following accounting pronouncement in the current year.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes existing revenue recognition guidance under GAAP. This standard provides a five-step analysis of contracts to determine when and how revenue is recognized. The core principle of the new guidance is that an entity will recognize revenue to reflect the transfer of goods or services to customers in an amount that reflects the consideration that the entity expects to receive. ASU 2014-09 also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts. The MAH adopted the standard for its annual reporting period beginning July 1, 2020, using the cumulative effect method. The MAH has reviewed its contracts with customers and determined that the timing and amount of revenue recognized previously is consistent with the new standard. The adoption had no impact on the MAH's opening net assets.

New accounting standards not yet adopted.

Leases (Topic 842) Lease guidance is effective for the MAH annual reporting periods beginning after December 15, 2021 (fiscal year beginning July 1, 2022). The new guidance requires lessees to recognize assets and liabilities related to certain operating leases on the statement of financial position. The guidance also requires additional disclosures by lessees and contains targeted changes to accounting by lessors. The MAH is currently in the process of evaluating the impact of the new standard on its financial statements.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

2. Summary of Significant Accounting Policies (continued)

Net assets

Net assets, revenues, gains, and losses are classified based on the existence or absence of donor or grantor imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

Net Assets Without Donor Restrictions – include those assets over which the governing Board has discretionary control in carrying out the operations of the MAH. Under this category the MAH maintains an operating fund, plus any net assets designated by the governing Board for specific purposes. Governing Board restrictions from net assets without donor restrictions are described in Note 10.

Net Assets With Donor Restrictions - include those assets which are subject to donor restriction and for which the applicable restriction was not met as of the year end of the current reporting period and also include those net assets which are subject to a non-expiring donor restriction, such as endowments.

Cash and cash equivalents

For purposes of reporting cash flows, the MAH considers all cash accounts which are not subject to withdrawal restrictions or penalties to be cash or cash equivalents. The MAH maintains its cash and cash equivalents in bank deposit accounts at various financial institutions.

Accounts and grants receivable

Accounts and grants receivable represent amounts owed to the MAH from unconditional promises to give, and conditional promises that have become unconditional, and may be in the form of gifts or grants, and other receivables related to the MAH's programs. The MAH considers all accounts and grants receivable to be fully collectible, accordingly, no allowance for doubtful accounts is considered necessary.

Rents and trash district fees receivable

Rents and trash district fees receivable represents amounts owed to the MAH for McPherson Center tenant rent, triple net charges, and trash district fees based on the terms of the lease agreements.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

2. Summary of Significant Accounting Policies (continued)

Rents and trash district fees receivable (continued)

The MAH makes estimates of the collectability of its tenant receivables related to base rents, straight-line rent and triple net charges. The MAH considers such things as historical bad debts, tenant creditworthiness, current economic trends, facility operating performance, lease structure, developments relevant to a tenant's business, and changes in tenants' payment patterns in its evaluation of the adequacy of the allowance for doubtful accounts. As of June 30, 2021, the MAH expects all rents and trash district fees to be collected.

Inventories

Inventories are comprised of program-related books and merchandise held for sale and are stated at the lower of cost or net realizable value determined by the first-in, first-out basis.

Property, equipment, and improvements

All property and equipment are stated at cost. Major improvements are charged to the property, equipment and improvements accounts, while maintenance and repairs which do not extend the life for the respective assets are expensed currently. The MAH capitalizes all purchases of furniture, fixtures, and equipment with a cost of \$2,500 or more, or leasehold improvements of \$10,000 or more, and a useful life greater than one year. When property is retired or otherwise disposed of, the cost of the property and the related accumulated depreciation are removed from the accounts and any resulting gains or losses are reflected in income.

Depreciation is computed by use of the straight-line method based on the estimated useful life of the respective assets currently 5-7 years for office furniture and equipment and 15-40 years for building and building improvements.

Investments

The MAH records investment purchases at cost, or if donated, at fair value on the date of donation. Thereafter, investments are reported at fair value in the statement of financial position. Net investment return/(loss) is reported in the statement of activities and changes in net assets, and consists of interest and dividend income, and realized and unrealized capital gains and losses, less external and direct internal investment expenses.

Investment securities are exposed to various risks, such as changes in interest rates or credit ratings and market fluctuations. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is possible that the value of the MAH's investments and total net assets balance could fluctuate materially.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

2. Summary of Significant Accounting Policies (continued)

Investments (continued)

Fair value is defined as "the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants on the measurement date."

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

This hierarchy consists of three broad levels:

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

Investments – beneficial interest in assets held by Community Foundation of Santa Cruz County

The MAH has transferred net assets without donor restrictions to the Community Foundation of Santa Cruz County which holds funds for MAH's benefit and are invested in a long-term portfolio of assets. Those investments are not covered under FDIC, it is possible that the value of the investments and total net assets balance could fluctuate materially.

When nonprofit organizations transfer assets to a charitable trust or community foundation in which the resource provider names itself as beneficiary, the economic benefit of the transferred asset remains with the resource provider. The asset received in exchange is a beneficial interest in assets held by others, measured at the fair value of the asset contributed.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

2. Summary of Significant Accounting Policies (continued)

Investments – beneficial interest in assets held by Community Foundation of Santa Cruz County (continued)

Changes in the value are recognized less investment expenses, in the statement of activities and changes in net assets and included in "realized and unrealized gains on investments, net of investment expenses." Distributions to the MAH from the fund held by the Community Foundation of Santa Cruz County are limited to an annual distribution and may be waived by the MAH. The maximum allowable distribution that can be made is 4% of the average fund balance on the previous 12 quarters, limited to the extent that accumulated earnings are available. Other distributions may be made to the MAH only by a final determination made by the Board of Directors of the Community Foundation of Santa Cruz County.

Accrued personal time off

Full-time MAH employees who work a regular schedule of 30 or more hours per week, accrue paid time off (PTO) which can be used by employees for paid vacation days or for other paid personal time. The MAH records the value of PTO that has been earned but not yet used in the "Current liabilities" section in the statement of financial position. The amount of the accrued PTO as of June 30, 2021 was \$56,480.

Revenue and revenue recognition

Contributions and contributions receivable are recognized when a donor makes a pledge to give that is, in substance, an unconditional promise. Contributions are recorded as with or without donor restrictions, depending on the nature of donor restrictions. Contributions with donor restrictions are reported as increases in net assets with donor restrictions. When the restriction is met the amount is shown in the statement of activities and changes in net assets as a reclassification of net assets with donor restrictions to net assets without donor restrictions.

Conditional grants and contributions are recognized when the MAH meets the terms or the conditions.

The MAH has multiple revenue streams that are accounted for under *Revenue from Contracts with Customers (Topic 606)*, including admissions, membership, facility rental, and store activities. The MAH recognizes revenue from admissions at the time of admission. Membership dues, the term of the membership is for twelve months, dues are recognized as revenue over the membership period. Facility rental income includes a non-refundable advance recorded as revenue when the facility rental agreement is signed, the remainder is recognized when the event is held. Store sales are recognized at point of sale. Amounts received under contracts with customers in advance are reported as "Deferred revenue" in the "Current liabilities" section on the statement of financial position.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

2. Summary of Significant Accounting Policies (continued)

Revenue and revenue recognition (continued)

Rental Revenue – The MAH, as a lessor, for leases at The McPherson Center, has retained substantially all of the risks and benefits of ownership and accounts for its leases as operating leases. For lease agreements that provide for scheduled rent increases, rental income is recognized on a straight-line basis over the non-cancellable term of the leases, which commences when control of the space has been provided to the customer. If rental income calculated on a straight-line basis exceeds the cash rent due under a lease, the difference is recorded as an increase to straight-line rent receivable and an increase in rental income. If rental income on a straight-line basis is calculated to be less than cash received, there is a decrease in the same accounts. Contingent rental income, for example additional rent based on the tenant meeting gross revenue benchmarks, is recorded at the time the tenant reaches the applicable benchmarks. When current rent is paid in advance it is recorded in "Deferred revenue" in the "Current liabilities" section in the statement of financial position. The amount of the straight-line rent receivable included in "Other assets" in the statement of financial position was \$56,025 as of June 30, 2021.

Expenses subject to common area charges

The McPherson Center Office/retail building lease agreements with tenants generally contain provisions that require tenants to reimburse the MAH for certain property expenses. Estimated reimbursements from tenants for real estate taxes, common area maintenance and other recoverable operating expenses are recognized as revenues in the period that the expenses are incurred. Subsequent to year-end, the MAH performs final reconciliations on a lease-by-lease basis and bill or credit each tenant for any cumulative annual adjustments.

Donated materials, services and facilities

Donated services and materials are recorded at their estimated fair value if they enhance the MAH's nonfinancial assets or require specialized skills that the MAH would normally purchase if not provided by donation. No amounts have been reflected in the financial statements for contributed services for the substantial number of volunteers who donate significant amounts of their time in the MAH's program and supporting services, principally in membership development and in the display of exhibits because they did not qualify for recording under generally accepted accounting principle guidelines. In-kind special event auction items to be sold are reported part of special event at the auction price.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

2. Summary of Significant Accounting Policies (continued)

Permanent Collection

The MAH maintains a permanent collection of art, consisting of regionally significant art and artifacts, and history, consisting of original publications, detailed history journals, research library, historical archive, and historic sites including the Evergreen Cemetery, Octagon Building and Davenport Jail. Collections are managed under the MAH's collection policy. The collection is not recognized as an asset in the statement of financial position. The MAH acquires most of its art and historical archival collections through contributions. The value of archives acquired through contributions is not susceptible to objective valuation and have not been reflected in the financial statements. Current year purchases are reflected in the statement of activities and changes in net assets. Each piece of the collection is inventoried and cared for. Proceeds from and deaccessions or insurance recoveries may be allocated for purposes that clearly benefit the collections, such as acquisition, preservation or conservation.

Estimates

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

Functional expenses

The costs of program and supporting services activities have been summarized on a functional basis in the statement of activities and changes in net assets. The statement of functional expenses presents the natural classification detail of expenses by function. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

The financial statements report certain categories of expenses that are attributed to more than one program or supporting function. Therefore, expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include salaries, payroll taxes and employee benefits, which are allocated on the basis of estimates of time and effort, as well as occupancy, utilities, depreciation and amortization, which are allocated on a square footage basis.

Taxes on income

The MAH has received notification from the Internal Revenue Service and the state of California that it qualifies for tax-exempt status under Section 501(c)(3) of the Internal Revenue Code and Section 27301(d) of the California Revenue and Taxation Code.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER
(A California Public Benefit Corporation)
Notes to Financial Statements
June 30, 2021

2. Summary of Significant Accounting Policies (continued)

Taxes on income (continued)

The MAH's federal returns for the tax years ended June 30, 2018 and beyond remain subject to possible examination by the Internal Revenue Service. The MAH's California returns for the tax years ended June 30, 2017 and beyond remain subject to possible examination by the Franchise Tax Board.

The MAH recognizes the effect of income tax positions only if those positions are more likely than not of being sustained, and changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The MAH has evaluated its current tax positions and has concluded that as of June 30, 2021 the MAH does not have any significant uncertain tax positions for which a reserve would be necessary.

Subsequent events

Management of the MAH has evaluated events and transactions subsequent to June 30, 2021, for potential recognition or disclosure in the financial statements. The MAH did not have subsequent events that required recognition or disclosure in the financial statements for the year ended June 30, 2021. Subsequent events have been evaluated through the date the financial statements became available to be issued, December 2, 2021.

3. Front Street Annex Lease

The MAH leases certain real property that houses the commercial and professional space of the McPherson Center under an agreement with the County of Santa Cruz, Amendment No. 1 dated April 9, 2014. Under the agreement rental payments of 10% of gross rent are due on or before September 1 (10% of gross rent from January 1 to June 30) and March 1 (10% of gross rent from July 1 to December 31).

For any six month period for which a use payment has been made (defined as a payment on the debt described in Note 8) such use payment shall satisfy the rental payment obligation.

Rental payments, other than those to be satisfied by a use payment, were scheduled to commence September 1, 2021. Current debt maturity is June 30, 2023, the MAH is requesting clarity from the County of Santa Cruz regarding the commencement date of rental payments.

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4. Liquidity and Availability

The MAH, as part of liquidity management, structures financial assets to be available as general expenditures and liabilities, and other obligations become due. Subsequent to June 30, 2021 the governing body released \$58,000 from the facilities reserve due to capital replacements made in the year ended June 30, 2021, and released \$100,000 from the operating reserve to support near term operating cash flow. The MAH has an available revolving line of credit, as described in Note 18. The MAH has minimum future payments required on a note payable, as disclosed in Note 8.

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the balance sheet date, comprise the following:

Cash and cash equivalents	\$ 767,637
Accounts and grants receivable	798
Rents and trash district fees receivable	48,439
Time restricted net assets available in 2021	<u>89,993</u>
	906,867
Less financial assets unavailable for General expenditures due to Board of Trustees designations	<u>424,645</u>
Net available financial assets	<u>\$ 482,222</u>

5. Concentration of Credit and Market Risk

The MAH maintains its cash and cash equivalents in bank deposit accounts at various financial institutions. The balances at times may exceed federally insured limits. At June 30, 2021, the MAH had \$351,628 in bank deposits in excess of the \$250,000 FDIC limits.

The MAH holds investment funds in various brokerage accounts, and at the Community Foundation of Santa Cruz County, with investments in mutual funds and U.S. treasury bills subject to market risk and interest rate risk.

The MAH is mainly dependent on membership revenue, donations and contributions from the community, grants from private foundations, and net rent revenue from its Office/Retail Building for its operations. The MAH receives a substantial amount of its support from local government. A significant reduction in the level of this support, if this were to occur, may have an effect on the MAH's programs and activities. The MAH's rent income is concentrated in major tenants as disclosed in Note 12.

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6. Deferred Revenue

Deferred revenue at June 30, 2021, consisted of the following:

July 2021 rent income received in advance	\$ 19,457
Membership dues to be recognized as revenue over the membership period	28,200
Facility rental to be recognized when the event is held	<u>43,246</u>
	<u>\$ 90,903</u>

7. Property, Equipment, and Improvements

Details of property, equipment and improvements as of June 30, 2021, and related depreciation expense for the year then ended are as follows:

	<u>Museum</u>	<u>McPherson Center</u>	<u>Total</u>
Office furniture	\$ 59,126	\$ 20,406	\$ 79,532
Equipment	349,652	98,828	448,480
Museum store	68,625	-	68,625
Leasehold improvements	346,503	136,888	483,391
Land improvements	-	4,760	4,760
Evergreen Cemetery	81,317	-	81,317
Building use remodel	2,835,104	-	2,835,104
Museum building	3,721,658	-	3,721,658
McPherson Center Building, Leasehold improvements			
Front Street Annex	<u>-</u>	<u>4,175,389</u>	<u>4,175,389</u>
	7,461,985	4,436,271	11,898,256
Less: accumulated depreciation	<u>(3,526,737)</u>	<u>(3,163,415)</u>	<u>(6,690,152)</u>
	<u>\$3,935,248</u>	<u>\$1,272,856</u>	<u>\$5,208,104</u>

Depreciation expense for the year ended June 30, 2021 totaled \$388,661 and consisted of \$257,034 included in expenses, and \$131,627 included in expenses related to rents.

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8. Note Payable

Note payable at June 30, 2021, consisted of the following:

Santa Cruz County Bank - Entered into on April 29, 2016, as subsequently modified, with a Maturity date of June 30, 2023. Secured by a blanket UCC-1 lien. Due in monthly principal and interest payments of \$11,586 at an at an interest of 4.1 percent.	\$266,663
Less: current portion	<u>(130,675)</u>
	<u>\$135,988</u>

Minimum future payments are as follows:

<u>Year Ending June 30,</u>	
2022	\$130,675
2023	<u>135,988</u>
	<u>\$266,663</u>

Interest expense for the year ended June 30, 2021 was \$13,689.

9. Paycheck Protection Program Loans

The MAH received loan proceeds from promissory notes issued by financial institution, under the Paycheck Protection Program ("PPP") which was established under the CARES Act and is administered by the U.S. Small Business Administration. The terms on the loans are two years and the annual interest rate is 1.00%. Payments of principal and interest are deferred to the date the SBA remits the loan forgiveness amount to the lender or ten months after the loan forgiveness covered period if the borrower has not applied for forgiveness. Under the terms of the CARES Act, PPP loan recipients can apply for and be granted forgiveness for all or a portion of the loans granted under PPP. Such forgiveness will be determined based on the use of the loan proceeds for payroll costs, rent and utility expenses and the maintenance of workforce and compensation levels with certain limitations.

The MAH expects to meet the PPP's eligibility criteria and concludes that the PPP loan represents, in substance, a grant that is expected to be forgiven. As a result the MAH initially classifies PPP loan proceeds as "Refundable advance, Paycheck Protection Program" under current liabilities on the statement of financial position, and then reclassifies as "Contributions Paycheck Protection Program" on the statement of activities and changes in net assets as qualifying expenses are incurred.

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9. Paycheck Protection Program Loans (continued)

The MAH received its first PPP loan of \$258,729 during the year ended June 30, 2020 and recognized \$176,831 as "Contributions Paycheck Protection Program" on the statement of activities and changes in net assets for the year ended June 30, 2020. The remaining balance of \$81,898 was recognized as "Contributions Paycheck Protection Program" on the statement of activities and changes in net assets as qualifying expenses for the year ended June 30, 2021. The MAH received notification from the SBA in May 2021 that the first PPP loan of \$258,729 was issued a judgement of full forgiveness.

The MAH received its second PPP loan of \$220,570 on February 11, 2021. The MAH has recognized \$151,642 as "Contributions Paycheck Protection Program" to the extent qualifying expenses were incurred through June 30, 2021. The remaining balance of \$68,928 is shown as "Refundable advance, Paycheck Protection Program" under current liabilities on the statement of financial position. The MAH plans to submit its forgiveness application during year ended June 30, 2022. The MAH believes that it will likely qualify for full forgiveness, but there is uncertainty around the standards and operation of the PPP, and no assurance is provided that the MAH will obtain forgiveness in whole or in part.

10. Net Assets Without Restrictions, Board Designated Funds

As of the year ended June 30, 2021, the Board has the following designated funds:

Operating Reserve Fund

During the year ended June 30, 2014, to establish an Operating Reserve Fund, the Board designated \$100,000 of existing accumulated liquid net assets as the beginning balance of the Operating Reserve Fund. The goal was to add \$150,000 to the fund over the next six (6) fiscal years in annual increments of \$25,000. As of June 30, 2021 designated operating reserve was \$200,000. Subsequent to June 30, 2021 the governing body released \$100,000 from the operating reserve to support near term operating cash flow.

Facilities Reserve Fund

During the year ended June 30, 2014, the Board determined the need for a Facilities Reserve Fund and created a policy for funding. The Facility Reserve Fund was established at \$233,071. During the year ended June 30, 2017, the Board defunded the reserve in the amount of \$60,000 leaving a remaining reserve of \$161,075. During the year ended June 30, 2019 the reserve was increased by \$40,000 to a current balance of \$201,075. Subsequent to June 30, 2021 the governing body released \$58,000 from the facilities reserve due to capital replacements made in the year ended June 30, 2021.

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10. Net Assets Without Restrictions, Board Designated Funds (continued)

Publications Fund

The MAH has a Publications Fund for the purpose of setting aside funds for future publications, the balance at June 30, 2021 was \$23,570.

11. Net Assets With Donor Restrictions

Net assets with donor restrictions are summarized as follows:

	<u>2020</u>	<u>Additions</u>	<u>Released from Restrictions</u>	<u>2021</u>
Donor-restricted endowments to support general activities, subject to spending policy	\$ 233,071	\$ -	\$ -	\$ 233,071
Accumulated earnings	<u>135,167</u>	<u>81,986</u>	<u>-</u>	<u>217,153</u>
	<u>368,238</u>	<u>81,986</u>	<u>-</u>	<u>450,224</u>
Subject to passage of time				
Year ending June 30, 2021	120,000	40,000	160,000	-
Year ending June 30, 2022	<u>89,993</u>	<u>-</u>	<u>-</u>	<u>89,993</u>
	<u>209,993</u>	<u>40,000</u>	<u>160,000</u>	<u>89,993</u>
Subject to expenditure for specified purposes				
Evergreen Cemetery	150,000	-	-	150,000
Exhibit	-	120,000	40,832	79,168
Other	<u>1,901</u>	<u>-</u>	<u>-</u>	<u>1,901</u>
	<u>151,901</u>	<u>120,000</u>	<u>40,832</u>	<u>231,069</u>
	<u>\$ 730,132</u>	<u>\$ 241,986</u>	<u>\$ 200,832</u>	<u>\$ 771,286</u>

Grants and contracts awarded to the MAH are subject to the funding agencies' criteria, contract terms and regulations under which expenditures may be charged and are subject to audit under such terms, regulations, and criteria. MAH could be held responsible for repayments to the funding agency for the questioned costs or be subject to the reductions of future funding in the amount of the questioned costs. Management does not anticipate any material questioned costs for the contracts and grants administered during the period.

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12. Rental Income

McPherson Center rental and trash service fees, for the year ended June 30, 2021, consisted of the following:

Rent	\$ 614,071
Operating costs charges	106,137
Trash district fees	<u>115,656</u>
	<u>\$ 835,864</u>

As of June 30, 2021, rent from three tenants in the office/retail building represented the majority of gross base rent. Concentration percentage of gross base rent from tenants is as follows:

	<u>Percent of Gross Base Rent</u>
Tenant A	38%
Tenant B	32%
Tenant C	13%

Minimum future rental receipts are due as follows:

<u>Year Ending June 30,</u>	
2022	\$ 648,052
2023	459,678
2024	229,732
2025	231,119
2026	238,053
Thereafter	<u>120,785</u>
	<u>\$1,927,419</u>

13. Employee Benefit Plans

The MAH sponsors a tax-deferred annuity plan ("the Plan") under Section 403(b) of the Internal Revenue Code. The plan covers all employees of the MAH. The MAH has discretion to vary the contribution rate from year to year. For the year ended June 30, 2021, the MAH made no contributions. Employees may make contributions to the plan up to the maximum amount allowed by the Internal Revenue Code if they wish.

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14. Related Party Transactions

The following related party transactions occurred with the MAH and its Board or senior staff. Contributions received for the year ended June 30, 2021 of \$30,242.

15. Self-Insured for Unemployment Insurance

The MAH is a member of Unemployment Services Trust (UST) which enables the MAH to be self-insured for unemployment claims. As such, the MAH does not pay unemployment taxes directly to the state of California and does not have unemployment insurance. UST acts as the administrator of any claims made against the MAH and specifies the recommended reserve the MAH maintains. The reserve account is held by UST. The MAH has reserved the amount recommended by UST, and at June 30, 2021, the MAH has \$4,486 on deposit with UST as a reserve to fund future claims. The reserve account is included in "Other assets" in the statement of financial position. The MAH could be required to make additional payments if claims exceed the reserve account.

16. Fair Value Measurements

The following is a description of calculation methodologies used for assets and liabilities recorded at fair value and the basis for estimating fair value. These are reflected as recurring or non-recurring in compliance with required disclosures.

Assets

Investments (Endowment Fund) - Represents assets invested in a mix of funds in a brokerage account.

Beneficial interests in assets held by Community Foundation of Santa Cruz County – are held in an investment pool (Long Term Portfolio).

The following table presents the MAH's fair value hierarchy for those assets measured at fair value as of June 30, 2021:

	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Endowment fund - exchange traded funds	\$ 450,224	\$ 450,224	\$ -	\$ -
Beneficial interest in assets held by Community Foundation of Santa Cruz County	55,874	55,874	-	-

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17. Endowment Fund

As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor imposed restrictions.

Interpretation of relevant law

The Board has interpreted the California version of the Uniform Prudent Management of Institutional Funds Acts (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 MAH retains in perpetuity (a) the original value of gifts donated to the endowment, (b) the original value of subsequent gifts to the endowment, and (c) accumulations to the 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 held in perpetuity is included in with donor restricted net assets until those amounts are appropriated for expenditure by the MAH in a manner consistent with the standard of prudence prescribed by UPMIFA.

Investment return objectives, risk parameters and strategies

The MAH has adopted investment and spending policies, approved by the Board, for endowment assets. The investment policy seeks to maintain fund principal and provide a reasonable rate of return. Safety of principal and preservation of capital is based on prudent investment principles. While short-term stability is desirable, achieving superior long-term returns takes precedence as an investment objective.

Spending policy

The MAH spending policy is to transfer as a distribution to the MAH an amount equal to the annual interest/dividend earnings while leaving market value increase in the fund. Undistributed investment income, including market value increase in the fund, on the funds are classified as with donor restrictions.

Endowment net asset composition

As of June 30, 2021 amounts held in the Endowment Fund at fair value totaled \$450,224, and consisted of the following:

	<u>2021</u>
Donor-restricted for general operations	\$ 233,071
Net unrealized gains, net of distributions	<u>217,153</u>
Ending balance	<u>\$ 450,224</u>

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18. Revolving Line of Credit

The MAH has an available revolving line of credit for \$250,000, secured with a blanket UCC-1 lien, with a current maturity date of December 5, 2021. The reference rate (the Prime rate, currently 3.250%, with an interest rate floor of 4.250%), is added to the margin of 1.000%, resulting current rate of 4.250%. As of June 30, 2021 no balance is due on the line.

19. Impact of COVID-19

The novel strain of coronavirus (COVID-19) outbreak has had far reaching and unpredictable impacts on the global economy and business operations. Governments have taken substantial action to contain the spread of the COVID-19 virus including mandating social distancing, suspension of certain gatherings, and shuttering of certain nonessential businesses.

The COVID-19 pandemic has directly impacted the operational and financial performance of the MAH's business, due in part to a physical closure of the museum for a full year, including 8 months of the fiscal year in this report. This closure resulted in negative impacts to both earned and contributed revenue, including lost admission fees, event ticket revenue, museum shop sales, facility rentals, and other funding shortfalls. The museum reopened in March 2021 with reduced hours, and continues to work through the changes with local, state, and federal health and safety restrictions. Included in MAH financial statements is McPherson Center rent income. The pandemic may adversely affect the business of the lessees, and the lessees' ability to make timely rent payments, and lessees' decisions on office space lease renewal.

There is uncertainty in the nature and degree of its continued effects on the MAH's business over time. The extent to which it will impact the MAH's business going forward, either positively or negatively, will depend on a variety of factors including the duration and continued spread of the outbreak, impact on our donors and employees, as well as governmental, regulatory and private sector responses. Further, the pandemic may have a significant impact on management's accounting estimates and assumptions.

Despite the toll the COVID-19 closures have taken on the MAH and the global cultural sector, the museum has been working diligently to ensure financial sustainability now and in the future. In the short term, the MAH reduced staff numbers and has been actively pursuing relief funding opportunities including grants, small business loans, and assistance programs focused on capacity-building, resilience, and recovery. For the long term, the MAH has been working to strengthen its business model with strategies that include striking a realistic balance between earned and contributed revenue, shoring up cash flow, expanding its resources, and broadening its base of support.