

**THE MUSEUM OF ART AND HISTORY
AT THE MCPHERSON CENTER**

Financial Report

Year ended June 30, 2022

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INDEPENDENT AUDITORS' REPORT

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

Opinion

We have audited the accompanying financial statements of The Museum of Art and History at the McPherson Center (a nonprofit organization), which comprise the statement of financial position as of June 30, 2022, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Organization as of June 30, 2022, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS). Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Organization and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Organization's ability to continue as a going concern within one year after the date that the financial statements are issued (or within one year after the date that the financial statements are available to be issued when applicable).

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Organization's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Organization's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

A handwritten signature in black ink that reads "Hatcher and Bloodgood LLP". The signature is written in a cursive, flowing style.

November 21, 2022

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

STATEMENT OF FINANCIAL POSITION

June 30, 2022

	Without Donor Restrictions	With Donor Restrictions	Total
ASSETS			
CURRENT ASSETS			
Cash and cash equivalents	\$ 336,264	\$ 178,742	\$ 515,006
Grants receivable, current	--	467,566	467,566
Accounts receivable	74,178	--	74,178
Rents and trash district fees receivable	53,289	--	53,289
Prepaid expenses	58,813	--	58,813
Inventories	29,858	--	29,858
	552,402	646,308	1,198,710
PROPERTY, EQUIPMENT AND IMPROVEMENTS, net	4,827,613	--	4,827,613
OTHER ASSETS			
Investments	--	361,489	361,489
Unemployment insurance reserve	20,186	--	20,186
Grants receivable, net of discount	--	111,950	111,950
Straight-line rent receivable	84,983	--	84,983
Beneficial interest in assets held by others	49,036	--	49,036
	154,205	473,439	627,644
	\$ 5,534,220	\$ 1,119,747	\$ 6,653,967

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

STATEMENT OF FINANCIAL POSITION

June 30, 2022

	Without Donor Restrictions	With Donor Restrictions	Total
LIABILITIES AND NET ASSETS			
CURRENT LIABILITIES			
Accounts payable	\$ 73,771	\$ --	\$ 73,771
Accrued personal time off	50,631	--	50,631
Tenant deposits	30,125	--	30,125
Deferred revenue	81,343	--	81,343
Note payable	136,086	--	136,086
Total current liabilities	371,956	--	371,956
NET ASSETS			
Without donor restrictions			
Undesignated	304,092	--	304,092
Invested in property and equipment, net of related debt	4,691,527	--	4,691,527
Board designated - facilities reserve	143,075	--	143,075
Board designated - publications fund	23,570	--	23,570
Total net assets without donor restrictions	5,162,264	--	5,162,264
With donor restrictions			
Time and use restricted	--	886,676	886,676
Donor-restricted endowment	--	233,071	233,071
Total net assets with donor restrictions	--	1,119,747	1,119,747
Total net assets	5,162,264	1,119,747	6,282,011
	\$ 5,534,220	\$ 1,119,747	\$ 6,653,967

The notes to financial statements are an integral part of this statement.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

STATEMENT OF ACTIVITIES

Year Ended June 30, 2022

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
SUPPORT AND REVENUE			
Revenue and other support:			
Contributions and grants	\$ 444,509	\$ 652,297	\$ 1,096,806
Contributions Paycheck Protection Program (PPP)	68,928	--	68,928
Contracts Santa Cruz County historic preservation	154,594	--	154,594
Memberships	82,436	--	82,436
Museum admissions	106,221	--	106,221
Program service fees	183,944	--	183,944
Museum store sales	29,633	--	29,633
Interest and dividend income	10,288	--	10,288
Unrealized loss	(9,720)	(63,034)	(72,754)
Net assets released from restrictions	240,802	(240,802)	--
Total revenue and other support	<u>1,311,635</u>	<u>348,461</u>	<u>1,660,096</u>
Other income:			
McPherson Center rental and trash service	976,474	--	976,474
Expenses related to rents and trash service	(606,192)	--	(606,192)
Total other income	<u>370,282</u>	<u>--</u>	<u>370,282</u>
Total revenue, support and other income	<u>1,681,917</u>	<u>348,461</u>	<u>2,030,378</u>
EXPENSES			
Program services	1,591,652	--	1,591,652
Management and general	282,779	--	282,779
Fundraising	308,924	--	308,924
Total program and support services	<u>2,183,355</u>	<u>--</u>	<u>2,183,355</u>
Increase (decrease) in net assets	<u>(501,438)</u>	<u>348,461</u>	<u>(152,977)</u>
Net assets, beginning	<u>5,663,702</u>	<u>771,286</u>	<u>6,434,988</u>
Net assets, ending	<u>\$ 5,162,264</u>	<u>\$ 1,119,747</u>	<u>\$ 6,282,011</u>

The notes to financial statements are an integral part of this statement.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

STATEMENT OF FUNCTIONAL EXPENSES

Year Ended June 30, 2022

	Program Services	Support Services		Total Support Services	McPherson Center	Total
		Management and General	Fundraising			
Personnel	\$ 759,090	\$ 179,965	\$ 233,312	\$ 413,277	\$ 57,600	\$ 1,229,967
Professional services	7,239	64,194	6,496	70,690	1,539	79,468
Administration and facility	126,870	24,436	24,156	48,592	347,424	522,886
Depreciation	250,462	2,556	2,556	5,112	124,917	380,491
Exhibitions and collections	311,541	--	--	--	--	311,541
Fundraising and memberships	--	--	19,757	19,757	--	19,757
Insurance	18,779	11,198	4,861	16,059	17,821	52,659
Interest	--	--	--	--	8,450	8,450
Programs	40,211	--	--	--	--	40,211
Museum store sales cost of goods sold	19,049	--	--	--	--	19,049
Marketing and promotion	58,411	113	17,786	17,899	--	76,310
Property taxes	--	317	--	317	48,441	48,758
	<u>1,591,652</u>	<u>282,779</u>	<u>308,924</u>	<u>591,703</u>	<u>606,192</u>	<u>2,789,547</u>
Less expenses included with other income as expenses related to rents	--	--	--	--	(606,192)	(606,192)
	<u>\$ 1,591,652</u>	<u>\$ 282,779</u>	<u>\$ 308,924</u>	<u>\$ 591,703</u>	<u>\$ --</u>	<u>\$ 2,183,355</u>

The notes to financial statements are an integral part of this statement.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

STATEMENT OF CASH FLOWS

Year Ended June 30, 2022

RECONCILIATION OF CHANGE IN NET ASSETS TO NET CASH FLOWS FROM OPERATING ACTIVITIES

Decrease in net assets	\$ (152,977)
Adjustments to reconcile decrease in net assets to cash used by operating activities	
Depreciation	380,491
Change in beneficial interest in assets held by others	6,838
Change in investments	63,034
Straight-line rental income	(28,958)
(Increase) decrease in:	
Accounts and grants receivable	(479,074)
Rents and trash district fees receivable, net of allowance of \$0	(36,172)
Prepaid expenses	70,291
Inventories	5,478
Unemployment insurance reserve	(15,700)
Increase (decrease) in:	
Accounts payable	(57,231)
Accrued personal time off	(5,849)
Tenant deposits	2,000
Deferred revenue	(9,560)
Refundable advance - PPP loan	(68,928)
Net cash used by operating activities	(326,317)
CASH FLOWS FROM INVESTING ACTIVITIES	
Proceeds from sale of investments	25,701
CASH FLOWS FROM FINANCING ACTIVITIES	
Payments of principal on note payable	(130,577)
Net decrease in cash and cash equivalents	(431,193)
Cash and Cash Equivalents, beginning	946,199
Cash and Cash Equivalents, ending	<u>\$ 515,006</u>
Supplemental disclosure of cash flow information	
Cash paid during the year for interest	<u>\$ 8,450</u>

The notes to financial statements are an integral part of this statement.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business: The Museum of Art and History at the McPherson Center (the Organization) was incorporated as a California public benefit corporation, that operates under the direction of its Board of Trustees. The Organization's objectives and purposes include exploring diverse cultural ideas, issues and perspectives through artistic experience and regional history. Dedicated to excellence, the Organization 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 Organization 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 Organization.

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%.

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

Significant Standing Committees of the Board responsible for overseeing certain aspects of the Organization 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

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accounting Policies: Significant accounting policies are:

Basis of Accounting: The Organization uses the accrual method of accounting. Revenues are recognized when earned and expenses are recognized when incurred.

Net Assets: The Organization's net assets and changes therein are classified and reported as follows:

- Net assets without donor restrictions: Net assets that are not subject to donor-imposed restrictions and may be expended for any purpose in performing the primary objectives of the Organization. These net assets may be used at the discretion of the Organization's management and the governing Board. Under this category, the Organization 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 8.
- Net assets with donor restrictions: Net assets subject to stipulations imposed by donors or grantors. Some donor restrictions are temporary in nature; those restrictions will be met by actions of the Organization or by the passage of time. Other donor restrictions are perpetual in nature, whereby the donor has stipulated the funds be maintained in perpetuity.

Functional Allocation of Expenses: The costs of providing program services and other activities have been presented on a functional basis in the statement of activities. Expenses that are attributable to more than one program or supporting function, such as salaries, payroll taxes and employee benefits, are allocated based on studies of time and effort. Occupancy, utilities, depreciation and amortization are allocated on a square footage basis.

Cash and Cash Equivalents: For purposes of the statement of cash flows, cash and cash equivalents include time deposits, certificates of deposit, and all highly liquid debt instruments with original maturities of three months or less.

Rents and Trash District Fees Receivable: Rents and trash district fees receivable represents amounts owed to the Organization for McPherson Center tenant rent, triple net charges and trash district fees based on the terms of the lease agreements.

The Organization makes estimates of the collectability of its tenant receivables related to base rents, straight-line rent and triple net charges. The Organization 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, 2022, the Organization expects all rents and trash district fees to be collected.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Grants and Accounts Receivable: Grants and accounts receivable that are expected to be collected within one year are recorded at net realizable value. Grants and accounts receivable that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using risk-free interest rates applicable to the years in which the promises are received. Amortization of the discounts is included in contribution revenue. Grants and accounts receivable are stated as unpaid balances, less an allowance for doubtful accounts. Accounts and grants receivable are stated at face value since probable uncollectible amounts are immaterial.

Grants and Donations: Grants and donations that are restricted by the donor or grantor are reported as increases in net assets without donor restrictions if the restrictions expire (that is, when a stipulated time restriction ends or purpose restriction is accomplished) in the reporting period in which the revenue is recognized. All other restricted revenue is reported as increases in net assets with donor restrictions. When a restriction expires, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statement of activities as net assets released from restrictions.

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 and Equipment: The Organization capitalizes all expenditures for property and equipment in excess of \$2,500 or leasehold improvements in excess of \$10,000. All property and equipment is stated at cost, or if donated, at estimated fair value on the date of donation. When property is retired or otherwise disposed, 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 on the straight-line method over the useful lives of the assets as follows:

Buildings and improvements	15 to 40 years
Furniture and equipment	5 to 7 years

Permanent Collection: The Organization 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 Organization's collection policy. The collection is not recognized as an asset in the statement of financial statements. The Organization acquires most 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.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments: The Organization 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 Organization's investments and total net assets balance could fluctuate materially.

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 Organization meets the terms or the conditions.

The Organization has multiple revenue streams, including admissions, membership, facility rental, and store activities. The Organization recognizes revenue from admissions at the time of admission. Membership dues have a term of twelve months, hence, 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 and the remainder is recognized when the event is held. Store sales are recognized at point of sale. Amounts received in advance under contracts with customers are reported as deferred revenue.

The Organization, 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. The amount of the straight-line rent receivable was \$84,983 as of June 30, 2022.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Donated Materials, Services and Facilities: Donated services and materials are recorded at their estimated fair value if they enhance the Organization's nonfinancial assets or require specialized skills that the Organization 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 Organization'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.

Expenses Subject to Common Area Charges: The McPherson Center office/retail building lease agreements with tenants generally contain provision that require tenants to reimburse the Organization for certain property expenses. Estimated reimbursements from tenant 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 Organization performs final reconciliations on a lease-by-lease basis and bill or credit each tenant for cumulative annual adjustments.

Use of Estimates: Preparing the Organization's financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosures 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.

Advertising: Advertising costs are expensed as incurred and totaled \$33,204 for the year ended June 30, 2022.

Income Taxes: The Organization is a nonprofit corporation that is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue code and from state franchise tax under Revenue and Taxation Code Section 23701(d).

The Financial Accounting Standards Board (FASB) has issued guidance that clarifies the accounting for uncertainty in income taxes recognized in an organization's financial statements. Using that guidance, tax positions initially need to be recognized in the financial statements when it is more likely than not the positions will be sustained upon examination by the tax authorities. As of June 30, 2022, the Organization has no uncertain tax positions that qualify for either recognition or disclosure in the financial statements.

Upcoming Accounting Pronouncements: In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract (i.e. lessees and lessors). The new standard requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase by the lessee.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Upcoming Accounting Pronouncements (continued): This classification will determine whether lease expense is recognized based on an effective interest method or on a straight-line basis over the term of the lease, respectively. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months regardless of their classification. Leases with a term of 12 months or less will be accounted for similar to existing guidance for operating leases today. The new standard requires lessors to account for leases using an approach that is substantially equivalent to existing guidance for sales-type leases, direct financing leases and operating leases. The new standard is effective for fiscal years beginning after December 15, 2021, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Organization is assessing the impact this ASU will have on its financial statements.

NOTE 2. AVAILABILITY AND LIQUIDITY

The following reflects the Organization's financial assets as of June 30, 2022, reduced by amounts not available for general use because of contractual or donor-imposed restrictions within one year of the statement of financial position date.

Financial assets at year end:	
Cash and cash equivalents	\$ 515,006
Grants and accounts receivable	617,250
Rents and trash districts fees receivable	89,733
Beneficial interest in assets held by others	49,036
Investments	<u>361,489</u>
Total financial assets	1,632,514
Less amounts not available to be used within one year:	
Subject to appropriation and satisfaction of donor restrictions	886,676
Donor designated endowment	<u>233,071</u>
Financial assets not available to be used within one year	<u>1,119,747</u>
Financial assets available to meet general expenditures within one year	<u>\$ 512,767</u>

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 2. AVAILABILITY AND LIQUIDITY (Continued)

The Organization regularly monitors liquidity required to meet its operating needs while also striving to maximize the investment of its available funds. The Organization manages its liquidity and reserves following three guiding principles: operating within a prudent range of financial soundness and stability, maintaining adequate liquid assets to fund near-term operating needs, and maintaining sufficient reserves to provide reasonable assurance that long-term obligations will be met.

The Organization has a goal to maintain an operating reserve at a minimum of 3 months of average operating expenses. To achieve this target, the Organization forecasts its future cash flows, monitors its liquidity routinely and monitors its reserves at least annually. During the year ended June 30, 2022, the level of liquidity and reserves was managed within the policy requirements.

NOTE 3. PAYROLL PROTECTION PROGRAM

The Organization received its first Payroll Protection Program (PPP) funding of \$258,729 during the year ended June 30, 2020. The terms of the funding agreement indicated that the Organization must utilize the proceeds to fund/offset qualifying expenses over a twenty-four-week period. The terms of the agreement specified that the Organization must repay the principal of the loan back plus interest, which accrued at 1% semi-annually and matured in two years. The loan may be forgiven if the Organization fulfills the agreed to terms. When it applied for the loan, the Organization believed it would qualify to have the loan forgiven under the terms of PPP, and therefore considered the loan to be substantively a conditional government grant.

The Organization received full forgiveness of its first PPP loan from the U.S. Small Business Administration (SBA) in May 2021. To the extent qualifying expenses were incurred, \$176,831 and \$81,898 was recognized as income in the statements of activities during the years ended June 30, 2020 and 2021, respectively.

The Organization received its second PPP loan of \$220,570 in February 11, 2021. The loan was forgiven in September 2021. To the extent qualifying expenses were incurred, \$151,642 and \$68,928 was recognized as income in the statements of activities during the years ended June 30, 2021 and 2022, respectively.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 4. GRANTS RECEIVABLE

For the year ended June 30, 2022, grants receivable are collectible as follows:

Receivable in less than one year	\$ 467,566
Receivable in one to five years	<u>118,768</u>
	586,334
Less: Discount to net present value	<u>(6,818)</u>
Total grants receivable	<u>\$ 579,516</u>

Long-term grants are recorded after discounting to the present value of future cash flows using a discount rate of 3%.

NOTE 5. CONCENTRATION OF CREDIT RISK

The Organization maintains balances in cash and interest-bearing deposit accounts at various financial institutions and, from time to time during the year, the cash balances may be in excess of the amount insured by the Federal Deposit Insurance Corporation (FDIC). In the event of insolvency by the financial institution, deposits in excess of insured amounts are potentially subject to unrecoverable loss.

NOTE 6. CONCENTRATION OF REVENUE

The Organization 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 Organization 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 Organization's programs and activities.

For the year ended June 30, 2022, approximately 49% of the Organization's total support came from four organizations. At June 30, 2022, a balance of \$398,768 was included in grants receivable from those organizations.

NOTE 7. EMPLOYEE BENEFIT PLAN

The Organization sponsors a tax-deferred annuity plan under Section 403(b) of the Internal Revenue Code. The plan covers all full-time employees of the Organization. The Organization has discretion to vary the contribution rate from year to year. For the year ended June 30, 2022, the Organization made no contributions. Employees may make contributions to the plan up to the maximum amount allowed by the Internal Revenue Code if they wish.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 8. NET ASSETS WITHOUT DONOR RESTRICTIONS, BOARD DESIGNATED FUNDS

As of the year ended June 30, 2022, 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 fiscal years in annual increments of \$25,000. As of June 30, 2021, designated operating reserve was \$200,000. The governing body released \$200,000 from the operating reserve to support near term operating cash flow in the year ended June 30, 2022. As of June 30, 2022, remaining designated operating reserve was \$0.

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 a portion of the reserve leaving a remaining reserve of \$161,075. During the year ended June 30, 2019 the reserve was increased by \$40,000 to a balance of \$201,075. The governing body released \$58,000 from the facilities reserve due to capital replacements made in the year ended June 30, 2021. As of June 30, 2022, remaining designated facilities reserve was \$143,075.

Publications Fund: The Organization has a Publications Fund for the purpose of setting aside funds for future publications. As of June 30, 2022, the balance was \$23,570.

NOTE 9. NET ASSETS WITH DONOR RESTRICTIONS

For the year ended June 30, 2022, activity in net assets with donor restrictions was as follows:

	Beginning 6/30/2021	Additions	Satisfied	Ending 6/30/2022
Evergreen Cemetery	\$ 150,000	\$ 2,500	\$ 2,184	\$ 150,316
Exhibitions and programs	79,168	339,797	84,356	334,609
Others	1,901	--	1,901	--
Subject to the passage of time	89,993	310,000	126,660	273,333
Donor-restricted endowments	233,071	--	--	233,071
Endowment accumulated earnings	217,153	(63,034)	25,701	128,418
	<u>\$ 771,286</u>	<u>\$ 589,263</u>	<u>\$ 240,802</u>	<u>\$ 1,119,747</u>

Grants and contracts awarded to the Organization 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. The Organization 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.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 10. LEASE COMMITMENT

The Organization 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, 2013. 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 12) 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 29, 2023, the Organization is requesting clarity from the County of Santa Cruz regarding the commencement date of rental payments.

NOTE 11. BENEFICIAL INTEREST IN ASSETS HELD BY OTHERS

Amounts reported in the statement of financial position as beneficial interest in assets held by others represent the net cumulative transfers by the Organization to the Community Foundation Santa Cruz County (the Foundation), as well as earnings thereon. Funds are invested in a long-term portfolio of assets, which are valued at the net asset value ("NAV") of shares held by the Foundation at year end. The amount totaled \$49,036 at June 30, 2022. Those investments are not covered under FDIC, it is possible that the value of the investments and total net assets balance could fluctuate materially. The Foundation holds and invests the funds on behalf of the Organization. The Foundation has no variance power over the funds. The funds are distributed to the Organization upon request to the Foundation.

NOTE 12. NOTE PAYABLE

The Organization entered into a note payable with Santa Cruz County Bank on April 29, 2016. The note has a current maturity date of June 29, 2023 and bears interest at 4.1% per annum. Monthly payments of principal and interest amount to \$11,586. The loan is secured by a blank UCC-1 lien. The remaining balance of \$136,086 is recognized as current. Interest expense for the year ended June 30, 2022 was \$8,450.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 13. RENTAL INCOME

McPherson Center rental and trash service fees, for the year ended June 30, 2022, consisted of the following:

Rent	\$	702,373
Operating costs charges		137,335
Trash district fees		136,766
		<u>136,766</u>
	\$	<u>976,474</u>

As of June 30, 2022, rent from three tenants in the office/retail building represented the majority of the 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	31%
Tenant C	13%

Minimum future rental receipts are due as follows:

2023	\$	604,358
2024		387,053
2025		272,898
2026		251,976
Thereafter		<u>125,090</u>
	\$	<u>1,641,375</u>

NOTE 14. FAIR VALUE MEASUREMENTS

The Fair Value Measurements Topic of the FASB Accounting Standards Codification establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 14. FAIR VALUE MEASUREMENTS (Continued)

The three levels of the fair value hierarchy are briefly described below:

- Level 1: Unadjusted quoted market prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.
- Level 2: Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly.
- Level 3: Prices or valuations that require inputs that are both significant to the fair value measurement and are unobservable.

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

Following is a description of the valuation methodology used for assets measured at fair value:

- Investments – Endowment Fund: Represents assets invested in a mix of funds in a brokerage account. Valuation is based on unadjusted quoted market prices for identical assets in active markets as of the measurement date.
- Interest in assets held at Community Foundation Santa Cruz County: Beneficial interests in assets held by the Foundation - are held in an investment pool (long term portfolio), which are valued at the net asset value (“NAV”) of shares held by the Foundation at year end.

The preceding method described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Organization believes its valuation method is appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table sets forth by level, within the fair value hierarchy, the Organization's assets at fair value at June 30, 2022:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Endowment fund - exchange traded funds	<u>\$ 361,489</u>	<u>\$ --</u>	<u>\$ --</u>	<u>\$ 361,489</u>
Beneficial interest in assets held by others	<u>\$ --</u>	<u>\$ --</u>	<u>\$ 49,036</u>	<u>\$ 49,036</u>

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 14. FAIR VALUE MEASUREMENTS (Continued)

The following is a reconciliation of the beginning and ending balance of assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended June 30, 2022:

Beginning balance	\$ 55,874
Distribution	(1,916)
Investment loss	(4,372)
Administration fees	<u>(550)</u>
Ending balance	<u>\$ 49,036</u>

NOTE 15. PROPERTY, EQUIPMENT AND IMPROVEMENTS

Details of property, equipment and improvements as of June 30, 2022, and related depreciation expense for the year 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	--	4,175,389	4,175,389
	<u>7,461,985</u>	<u>4,436,271</u>	<u>11,898,256</u>
Less: Accumulated depreciation	<u>(3,782,311)</u>	<u>(3,288,332)</u>	<u>(7,070,643)</u>
	<u>\$ 3,679,674</u>	<u>\$ 1,147,939</u>	<u>\$ 4,827,613</u>

Depreciation expense for the year ended June 30, 2022 totaled \$380,491 and consisted of \$255,574 included in expenses, and \$124,917 included in expenses related to rents.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 16. REVOLVING LINE OF CREDIT

The Organization 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, 2022. 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, 2022, no balance is due on the line.

NOTE 17. RELATED PARTY TRANSACTIONS

The following related party transactions occurred with the Organization and its Board of Trustees. Contributions received for the year ended June 30, 2022 was \$18,469.

NOTE 18. SELF-INSURED FOR UNEMPLOYMENT INSURANCE

The Organization is a member of Unemployment Services Trust (UST) which enable the Organization to be self-insured for unemployment claims. As such, the Organization 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 Organization and specifies the recommended reserve the Organization maintains. The reserve account is held by UST. The Organization has reserved the amount recommended by UST, and at June 30, 2022, the Organization has \$20,186 on deposit with UST as a reserve to fund future claims. The Organization could be required to make additional payments if claims exceed the reserve account.

NOTE 19. 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 Organization 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 Organization in a manner consistent with the standard of prudence prescribed by UPMIFA.

THE MUSEUM OF ART AND HISTORY AT THE MCPHERSON CENTER

Notes to Financial Statements
Year Ended June 30, 2022

NOTE 19. ENDOWMENT FUND (Continued)

Investment Return Objectives, Risk Parameters and Strategies: The Organization 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 take precedence as an investment objective.

Spending Policy: The Organization spending policy is to transfer as a distribution to the Organization 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, 2022 amounts held in the endowment fund at fair value totaled \$361,489 and consist of the following:

Donor-restricted for general operations	\$ 233,071
Net unrealized gain, net of distributions	<u>128,418</u>
Ending balance	<u>\$ 361,489</u>

NOTE 20. DEFERRED REVENUE

Deferred revenue at June 30, 2022, consisted of the following:

Membership dues to be recognized as revenue over the membership period	\$ 37,788
Facility rental to be recognized when the event is held	<u>43,555</u>
	<u>\$ 81,343</u>

NOTE 21. SUBSEQUENT EVENTS

Management has evaluated its June 30, 2022 financial statements for subsequent events through November 21, 2022, the date of issuance of the financial statements. The Organization is not aware of any subsequent events that would require recognition or disclosure in the financial statements.