

**THE HEARD MUSEUM AND AFFILIATE**  
**CONSOLIDATED FINANCIAL STATEMENTS**  
**YEARS ENDED SEPTEMBER 30, 2017 AND 2016**

**THE HEARD MUSEUM AND AFFILIATE  
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## INDEPENDENT AUDITORS' REPORT

The Board of Trustees  
The Heard Museum and Affiliate  
Phoenix, Arizona

We have audited the accompanying consolidated financial statements of The Heard Museum and Affiliate, which comprise the consolidated statements of financial position as of September 30, 2017 and 2016, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

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

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditors' Responsibility**

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

The Board of Trustees  
The Heard Museum and Affiliate

***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Heard Museum and Affiliate as of September 30, 2017 and 2016, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*CliftonLarsonAllen LLP*

**CliftonLarsonAllen LLP**

Phoenix, Arizona  
February 21, 2018

**THE HEARD MUSEUM AND AFFILIATE  
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION  
SEPTEMBER 30, 2017 AND 2016**

	2017	2016
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and Cash Equivalents	\$ 461,830	\$ 383,429
Receivables	15,075	23,167
Pledges Receivable	96,000	150,000
Merchandise Inventories, Net	1,252,997	1,610,461
Prepaid Expenses	135,164	218,663
Total Current Assets	1,961,066	2,385,720
<b>PLEDGES RECEIVABLE, Net</b>	175,915	289,602
<b>INVESTMENTS</b>	11,084,583	5,311,086
<b>ASSETS RESTRICTED TO INVESTMENT IN PROPERTY AND EQUIPMENT</b>		
Cash	1,455,283	2,173,132
<b>PROPERTY AND EQUIPMENT, Net</b>	17,171,766	16,471,182
<b>OTHER ASSETS, Net</b>	3,544	8,728
Total Assets	\$ 31,852,157	\$ 26,639,450
<b>LIABILITIES AND NET ASSETS</b>		
<b>CURRENT LIABILITIES</b>		
Accounts Payable and Accrued Expenses	\$ 527,609	\$ 1,129,239
Deferred Income	504,112	442,043
Lines of Credit	800,536	1,097,709
Current Maturities of Note Payable	-	28,674
Deposits	70,455	59,055
Total Current Liabilities	1,902,712	2,756,720
<b>GIFT ANNUITY PAYABLE</b>	22,678	26,586
Total Liabilities	1,925,390	2,783,306
<b>NET ASSETS</b>		
Unrestricted Net Assets:		
Undesignated	17,133,596	14,769,813
Board Designated for Endowment	2,191,828	245,127
Board-Designated Reserves	1,404,536	-
Total Unrestricted Net Assets	20,729,960	15,014,940
Restricted Net Assets:		
Temporarily	1,831,478	3,635,875
Permanently	7,365,329	5,205,329
Total Restricted Net Assets	9,196,807	8,841,204
Total Net Assets	29,926,767	23,856,144
Total Liabilities and Net Assets	\$ 31,852,157	\$ 26,639,450

See accompanying Notes to Consolidated Financial Statements.

**THE HEARD MUSEUM AND AFFILIATE  
CONSOLIDATED STATEMENT OF ACTIVITIES  
YEAR ENDED SEPTEMBER 30, 2017**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>OPERATING REVENUES AND SUPPORT</b>				
Revenues:				
Museum Shop and Bookstore Sales	\$ 3,521,406	\$ -	\$ -	\$ 3,521,406
Membership Dues	766,654	-	-	766,654
Admissions	2,368,801	-	-	2,368,801
Private Use Fees	505,660	-	-	505,660
Café Revenue	844,100	-	-	844,100
Educational Programs	3,279	-	-	3,279
Other Revenues	36,606	-	-	36,606
Total Revenues	<u>8,046,506</u>	<u>-</u>	<u>-</u>	<u>8,046,506</u>
Public Support:				
Individuals	4,033,535	410,425	2,410,000	6,853,960
Foundations	1,293	741,816	-	743,109
Government	83,218	21,828	-	105,046
Corporate Sponsorship	71,420	287,621	-	359,041
Contributed Goods and Services	214,005	-	-	214,005
Guild Event Revenue	478,171	-	-	478,171
Total Public Support	<u>4,881,642</u>	<u>1,461,690</u>	<u>2,410,000</u>	<u>8,753,332</u>
Special Events:				
Revenues from Special Events	526,640	-	-	526,640
Less: Costs of Direct Donor Benefits	<u>(107,737)</u>	<u>-</u>	<u>-</u>	<u>(107,737)</u>
Gross Profit from Special Events	<u>418,903</u>	<u>-</u>	<u>-</u>	<u>418,903</u>
Total Revenues and Support	13,347,051	1,461,690	2,410,000	17,218,741
Net Assets Released from Restriction	4,032,318	(3,782,318)	(250,000)	-
<b>OPERATING EXPENSES</b>				
Cost of Goods Sold	1,994,889	-	-	1,994,889
Education Costs	946,087	-	-	946,087
Shop Operations	630,496	-	-	630,496
Curatorial Costs	680,633	-	-	680,633
Exhibit Costs	1,030,709	-	-	1,030,709
Café Operations	735,871	-	-	735,871
Members Programs	284,969	-	-	284,969
Admissions	219,901	-	-	219,901
Facilities	1,291,062	-	-	1,291,062
Depreciation and Amortization	1,727,321	-	-	1,727,321
Administration	1,464,822	-	-	1,464,822
Development	410,100	-	-	410,100
Marketing	337,279	-	-	337,279
Private Use	269,327	-	-	269,327
Total Operating Expenses	<u>12,023,466</u>	<u>-</u>	<u>-</u>	<u>12,023,466</u>
<b>CHANGE IN OPERATING NET ASSETS</b>	5,355,903	(2,320,628)	2,160,000	5,195,275
<b>NONOPERATING ACTIVITIES</b>				
Investment Income	359,117	521,454	-	880,571
Change in Value of Gift Annuity	-	(5,223)	-	(5,223)
	<u>359,117</u>	<u>516,231</u>	<u>-</u>	<u>875,348</u>
<b>CHANGES IN NET ASSETS</b>	5,715,020	(1,804,397)	2,160,000	6,070,623
Net Assets - Beginning of Year	<u>15,014,940</u>	<u>3,635,875</u>	<u>5,205,329</u>	<u>23,856,144</u>
<b>NET ASSETS - END OF YEAR</b>	<u>\$ 20,729,960</u>	<u>\$ 1,831,478</u>	<u>\$ 7,365,329</u>	<u>\$ 29,926,767</u>

See accompanying Notes to Consolidated Financial Statements.

**THE HEARD MUSEUM AND AFFILIATE  
CONSOLIDATED STATEMENT OF ACTIVITIES  
YEAR ENDED SEPTEMBER 30, 2016**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>OPERATING REVENUES AND SUPPORT</b>				
Revenues:				
Museum Shop and Bookstore Sales	\$ 3,063,948	\$ -	\$ -	\$ 3,063,948
Membership Dues	796,596	-	-	796,596
Admissions	1,004,040	-	-	1,004,040
Private Use Fees	456,243	-	-	456,243
Café Revenue	667,067	-	-	667,067
Educational Programs	6,860	-	-	6,860
Other Revenues	39,497	-	-	39,497
Total Revenues	<u>6,034,251</u>	<u>-</u>	<u>-</u>	<u>6,034,251</u>
Public Support:				
Individuals	264,197	251,131	321,321	836,649
Foundations	138,831	1,579,746	-	1,718,577
Government	211,364	(100)	-	211,264
Corporate Sponsorship	12,500	20,000	-	32,500
Contributed Goods and Services	239,873	-	-	239,873
Guild Event Revenue	546,623	-	-	546,623
Total Public Support	<u>1,413,388</u>	<u>1,850,777</u>	<u>321,321</u>	<u>3,585,486</u>
Special Events:				
Revenues from Special Events	319,968	-	-	319,968
Less: Costs of Direct Donor Benefits	<u>(154,031)</u>	<u>-</u>	<u>-</u>	<u>(154,031)</u>
Gross Profit from Special Events	<u>165,937</u>	<u>-</u>	<u>-</u>	<u>165,937</u>
Total Revenues and Support	7,613,576	1,850,777	321,321	9,785,674
Net Assets Released from Restriction	1,045,677	(1,045,677)	-	-
<b>OPERATING EXPENSES</b>				
Cost of Goods Sold	1,642,139	-	-	1,642,139
Education Costs	925,992	-	-	925,992
Shop Operations	655,273	-	-	655,273
Curatorial Costs	745,641	-	-	745,641
Exhibit Costs	632,532	-	-	632,532
Café Operations	664,681	-	-	664,681
Members Programs	250,740	-	-	250,740
Admissions	169,774	-	-	169,774
Facilities	1,245,390	-	-	1,245,390
Depreciation and Amortization	1,621,708	-	-	1,621,708
Administration	1,321,080	-	-	1,321,080
Development	378,414	-	-	378,414
Marketing	410,096	-	-	410,096
Private Use	278,619	-	-	278,619
Total Operating Expenses	<u>10,942,079</u>	<u>-</u>	<u>-</u>	<u>10,942,079</u>
<b>CHANGE IN OPERATING NET ASSETS</b>	(2,282,826)	805,100	321,321	(1,156,405)
<b>NONOPERATING ACTIVITIES</b>				
Investment Income	267,428	187,818	-	455,246
Change in Value of Gift Annuity	<u>-</u>	<u>(5,584)</u>	<u>-</u>	<u>(5,584)</u>
	<u>267,428</u>	<u>182,234</u>	<u>-</u>	<u>449,662</u>
<b>CHANGES IN NET ASSETS</b>	(2,015,398)	987,334	321,321	(706,743)
Net Assets - Beginning of Year	<u>17,030,338</u>	<u>2,648,541</u>	<u>4,884,008</u>	<u>24,562,887</u>
<b>NET ASSETS - END OF YEAR</b>	<u>\$ 15,014,940</u>	<u>\$ 3,635,875</u>	<u>\$ 5,205,329</u>	<u>\$ 23,856,144</u>

See accompanying Notes to Consolidated Financial Statements.

**THE HEARD MUSEUM AND AFFILIATE  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
YEARS ENDED SEPTEMBER 30, 2017 AND 2016**

	2017	2016
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in Net Assets	\$ 6,070,623	\$ (706,743)
Adjustments to Reconcile Change in Net Assets to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	1,727,321	1,621,708
Contributions Restricted for Investment in Endowments	(2,410,000)	(321,321)
Unrealized and Realized Gain on Investments	(785,839)	(360,649)
Change in Allowance for Doubtful Pledges Receivable	-	(18,000)
Changes in Value of Gift Annuity Payable, Net of Payments	(3,908)	(3,566)
Increase (Decrease) in Cash Resulting from Changes In:		
Receivables	8,092	7,954
Pledges Receivable	167,687	(66,025)
Merchandise Inventories	357,464	943,022
Prepaid Expenses	83,499	(38,875)
Accounts Payable and Accrued Expenses	(601,630)	442,141
Deferred Income	62,069	(42,343)
Deposits	11,400	(34,325)
Net Cash Provided by Operating Activities	4,686,778	1,422,978
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Proceeds from Sales of Investments	8,166,823	1,633,014
Purchase of Investments	(13,154,481)	(1,572,307)
Purchases of Property and Equipment	(2,422,721)	(956,257)
Increase in Cash Restricted to Investment in Property and Equipment	717,849	(923,132)
Net Cash Used by Investing Activities	(6,692,530)	(1,818,682)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Contributions Restricted for Investment in Endowments	2,410,000	321,321
Net Change in Lines of Credit	(297,173)	(402,291)
Repayments on Notes Payable	(28,674)	(25,926)
Net Cash Provided (Used) by Financing Activities	2,084,153	(106,896)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	78,401	(502,600)
Cash and Cash Equivalents - Beginning of Year	383,429	886,029
<b>CASH AND CASH EQUIVALENTS - END OF YEAR</b>	\$ 461,830	\$ 383,429
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Cash Paid for Interest	\$ 47,822	\$ 48,427
Purchase of Software via a Contract	\$ -	\$ 54,600

See accompanying Notes to Consolidated Financial Statements.



**THE HEARD MUSEUM AND AFFILIATE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 2017 AND 2016**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations**

The Heard Museum is an institution incorporated in 1929 as an Arizona nonprofit corporation. The Heard Museum creates and presents exhibitions that are drawn from or inspired by American Indian art and culture, that are visually and intellectually stimulating, cost-effective and that attract the broadest possible audience both in Phoenix and abroad whilst setting new standards for excellence in scholarship, educational programming, community outreach, and visitor experience. The Heard Museum Guild and the Heard Museum Council are volunteer organizations that support and aid the work of the board of trustees and the staff of The Heard Museum and which are included in the records of The Heard Museum and are not separate legal entities.

Heard Family Trust (the Trust) is an irrevocable perpetual trust that was created by the Heard family for the benefit of The Heard Museum. The Trust is administered by JP Morgan Chase, an outside trustee. Effective October 2015, the administration of the Trust was moved to Texas. The Trust has elected to be classified as a private foundation and is subject to excise taxes.

The significant accounting policies are as follows:

**Consolidated Financial Statements**

The consolidated financial statements include the accounts of The Heard Museum, Guild, Council, and the Trust (collectively referred to as the Museum). All of the financial activities and balances of these organizations are included in these consolidated financial statements. All significant interorganization accounts and transactions have been eliminated in consolidation.

**Basis of Presentation**

The Museum's consolidated financial statements have been prepared in accordance with the American Institute of Certified Public Accountants (AICPA) Not-For-Profit Industry Guidance within the Financial Accounting Standards Board (FASB) Codification (Guidance). Under the Guidance, the Museum is required to provide financial statements which are prepared to focus on the Museum as a whole and to present balances and transactions according to the existence or absence of donor-imposed restrictions in three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets as follows:

Unrestricted Net Assets – Unrestricted net assets are not subject to donor-imposed stipulations and are those currently available at the discretion of the board of trustees for use in the Museum's operations, in accordance with its bylaws.

Temporarily Restricted Net Assets – Temporarily restricted net assets are those whose uses are subject to donor-imposed stipulations that will be met by the Museum and/or the passage of time.

**THE HEARD MUSEUM AND AFFILIATE**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2017 AND 2016**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Basis of Presentation (Continued)**

Permanently Restricted Net Assets – Permanently restricted net assets are those which represent permanent endowments where it is stipulated by donors that the principal remain in perpetuity and only the income is available as unrestricted or temporarily restricted, as per the endowment agreements.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted explicitly by donor stipulation or by law. Expirations of temporary restrictions on net assets, i.e., the donor stipulated purpose has been fulfilled and/or the stipulated time period has elapsed, are reported as reclassifications to unrestricted net assets.

**Use of Estimates in the Preparation of Consolidated Financial Statements**

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

**Cash and Cash Equivalents**

Cash and cash equivalents consist of highly liquid financial instruments purchased with original maturities of three months or less.

**Receivables**

Receivables are stated at the amount management expects to collect. Management provides for probable uncollectible amounts through a charge to earnings and an increase to a valuation allowance based upon its assessment of the current status of individual balances. Account balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a reduction of accounts receivables. At September 30, 2017 and 2016, the allowance for doubtful accounts was \$-0-.

**THE HEARD MUSEUM AND AFFILIATE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 2017 AND 2016**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Pledges Receivable**

Unconditional promises to give (pledges receivable) that are to be collected within one year are recorded at net realizable value. Unconditional promises to give that are expected to be collected in future years are initially recorded at the fair value, calculated as the net present value of their estimated future cash flows as of the date of the promise to give.

**Merchandise Inventories**

Merchandise inventories consist of books, gift items, and art-related objects held for resale and are carried at the lower of cost as determined by the specific identification method or market for purchased goods. Contributed goods held for sale are recorded at fair value. Inventory consists of the following:

	2017	2016
Jewelry	\$ 556,154	\$ 797,218
Kachinas	98,704	113,553
Pottery and Baskets	129,588	182,208
Textiles	158,139	152,331
Publications	105,442	129,222
Other	283,541	259,348
Nonaccessed Inuit Collection	-	53,789
Inventory Valuation Reserve	(78,571)	(77,208)
Total	<u>\$ 1,252,997</u>	<u>\$ 1,610,461</u>

Inventory items, with the exception of publications and some sundries, are purchased from American Indian artists. In addition, the Museum shop sells American Indian art items on consignment; such consignment items are not reflected in the inventory balance. At September 30, 2017 and 2016, the shop held \$1,312,615 and \$1,686,246, of consignments respectively.

During 2012, the Museum received an art collection of North American indigenous items (Inuit Collection). During the fiscal year 2014, management of the Museum decided to record a portion of the collection as inventory during the year ended September 30, 2014 representing a conservative estimate of the nonaccessed portion of the collection that the Museum expects to sell. During the fiscal year 2015, management of the Museum reached an agreement with a third party auction house for the consignment and sale of the items on behalf of the Museum. The agreement will remain in effect for four years and the Museum will retain ownership of the pieces in the Inuit collection until time of sale. The Museum transferred these items to the third party auction house for sale during fiscal year 2015. Sales of the items began during fiscal year 2016 and continued through the fiscal year ended September 30, 2017. Upon sale, the items have been relieved from inventory. The remaining book value of the collection at September 30, 2017 and 2016 was \$-0- and \$53,789, respectively.

**THE HEARD MUSEUM AND AFFILIATE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 2017 AND 2016**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Investments**

Investments, consisting primarily of equity securities, corporate bonds, and mutual funds with readily determinable market values are measured at fair value as of year-end in the consolidated statements of financial position. Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) are recognized in the consolidated statements of activities. Investments in equity securities with readily determinable fair values and all investments in debt securities are presented at fair value in the consolidated statements of financial position as determined by available market prices.

Investments are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in risk in the near term could materially affect account balances and the amounts reported in the accompanying consolidated financial statements.

**Assets Restricted to Investment in Property and Equipment**

Certain contributions of cash and pledges receivable were restricted by the donors for investment in exhibits and various property improvements.

**Property and Equipment**

Purchased property and equipment is stated at cost. Maintenance and repairs are charged to operations when incurred. Betterments and renewals in excess of \$2,000 are capitalized. When property and equipment is sold or otherwise disposed of, the asset and related accumulated depreciation and amortization accounts are relieved, and any gain or loss is included in operations. Leasehold improvements are amortized over the shorter of the useful lives of the improvements or the lease terms. Depreciation and amortization of property and equipment are computed on a straight-line basis over the respective useful lives of the assets, which range from 3 to 40 years, as follows:

Buildings	35 to 40 Years
Building Improvements	2 to 20 Years
Furniture, Fixtures, and Equipment	3 to 10 Years
Long-Term Exhibits	5 to 15 Years
Software	3 to 5 Years

Donations of property and equipment are recorded as contributions at their estimated fair value at the date of donation.

**THE HEARD MUSEUM AND AFFILIATE**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**SEPTEMBER 30, 2017 AND 2016**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Impairment of Long-Lived Assets**

The Museum reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. Management does not believe impairment indicators are present.

**Revenue Recognition**

Admissions revenue consists of ticket sales and is recognized when the tickets are sold. Museum shop and bookstore sales consist of retail sales which are recognized when goods are sold. Private use fees consist of rentals of the Museum facilities for private functions and are recognized as the events occur. Educational programs revenue consists of educational program income and publication sales and is recognized as the events occur or when publications are sold. Café revenue consists of food and beverage sales in the Museum cafes which are recognized at the time of sale.

**Membership Dues**

Membership dues, which are assessed annually, are recorded as deferred membership income at the renewal period and accreted as revenue ratably over the membership period.

**Contributions**

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. All donor-restricted support is reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions.

**Special Events Revenue**

The Museum conducts special events in which a portion of the gross proceeds paid by the participant represents payments for the benefits received by the participant at the event. The fair value of meals and entertainment provided at special events is generally measured at the actual cost to the Museum. The direct costs of the special events which ultimately benefit the donor rather than the Museum are recorded as special events costs, specifically direct donor benefits. All proceeds received in excess of the direct costs are recorded as gross profit from special events in the accompanying consolidated statements of activities.

**THE HEARD MUSEUM AND AFFILIATE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
SEPTEMBER 30, 2017 AND 2016**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Collections**

The collections of the Museum include several categories of Native American art, primarily kachina dolls, baskets, jewelry, textiles, ceramics, and fine art, as well as collections from other indigenous peoples of Latin America, Africa and Oceania, and are expensed in the period purchased. In conformity with the practice followed by many museums, art objects contributed to the Museum are not included in the accompanying consolidated financial statements. Furthermore, in conformity with industry practice, the Museum has not recorded the value of its collections on the consolidated statements of financial position. The fair value of certain collections is determined based on third-party evidence of comparable art sold through auction houses. The fair value of collections contributed to the Museum during the years ended September 30, 2017 and 2016 were \$446,780 and \$1,221,022, respectively.

**Donated Services**

Donated professional services are recorded as contributions in the accompanying consolidated financial statements at their estimated fair value if the services (a) enhance the Museum's nonfinancial assets or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased if not provided by donation. No amounts have been reflected in the consolidated financial statements for certain donated volunteer services because they did not qualify for recording under the generally accepted accounting principle guidelines; however, a substantial number of volunteers have donated significant amounts of their time to the Museum's program services and fundraising campaigns, primarily through the Heard Museum Guild and the Heard Museum Council.

**Advertising**

The Museum uses advertising to promote its programs to the various groups it serves. The advertising costs are charged to operations as incurred. Advertising expense charged to operations for the years ended September 30, 2017 and 2016 were \$296,652 and \$269,171, respectively.

**Income Taxes**

The Heard Museum qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code (IRC) and the Trust qualifies as a charitable trust under Section 4947(a)(i) of the IRC and accordingly, there is no provision for income taxes. In addition, The Heard Museum qualifies for the charitable contribution deduction under Section 170 of the IRC and has been classified as an organization that is not deemed to be a private foundation. Income determined to be unrelated business taxable income (UBTI) would be taxable.

The Museum evaluates its uncertain tax positions, if any, on a continual basis through review of its policies and procedures, review of its regular tax filings, and discussions with outside experts. Management believes that the Heard Museum and the Trust have no uncertain tax positions as of September 30, 2017 and 2016.

**THE HEARD MUSEUM AND AFFILIATE  
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**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**Reclassification**

Certain items in the prior year consolidated financial statements have been reclassified to conform to the current year's presentation. These reclassifications had no effect on total assets or changes in net assets as previously reported.

**Subsequent Events**

Management has evaluated subsequent events through February 21, 2018, the date the consolidated financial statements were available to be issued. There were no material subsequent events that required recognition or additional disclosure in these financial statements.

**NOTE 2 PLEDGES RECEIVABLE**

Pledges receivable consist of unconditional promises to give as follows:

	2017	2016
Unconditional Promises to Give Due in Less Than One Year	\$ 96,000	\$ 150,000
Unconditional Promises to Give Due in Two to Five Years	203,000	324,000
	299,000	474,000
Less: Discount to Present Value	(27,085)	(34,398)
	271,915	439,602
Current Portion	(96,000)	(150,000)
Noncurrent Portion	\$ 175,915	\$ 289,602

The estimated cash flows for pledges were discounted over the collection period using a management determined discount rate of 5.98%. As of September 30, 2017 and 2016, the allowance for uncollectible pledges was \$-0-.

**NOTE 3 INVESTMENTS**

Investments consist of the following:

	2017	2016
Equity Securities	\$ 4,174,903	\$ 1,744,466
Mutual Funds	5,098,507	2,131,948
Cash and Cash Equivalents Held for Reinvestment	646,706	226,086
Corporate Bonds	1,074,866	1,124,613
Investment Held by Arizona Community Foundation	89,601	83,973
Total	\$ 11,084,583	\$ 5,311,086

**THE HEARD MUSEUM AND AFFILIATE  
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**NOTE 3 INVESTMENTS (CONTINUED)**

Investment income, which includes realized and unrealized gains and losses that are included as part of the change in unrestricted net assets consist of the following:

	2017	2016
Net Realized/Unrealized Investment Gains	\$ 785,839	\$ 360,649
Dividend and Interest Income	162,725	149,780
Investment Advisory Fees	(67,993)	(55,183)
Total	\$ 880,571	\$ 455,246

**NOTE 4 FAIR VALUE OF FINANCIAL INSTRUMENTS**

In determining fair value, the Museum uses various valuation approaches within the fair value measurement framework. That framework provides 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 three levels of the fair value hierarchy are described as follows:

*Level 1* – Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Museum has the ability to access.

*Level 2* – Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

*Level 3* – Valuations derived from valuation techniques in which one or more significant inputs or significant value drivers are unobservable, such as pricing models, discounted cash flow models and similar techniques not based on market, exchange, dealer or broker-traded transactions.

The asset 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 measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.



**THE HEARD MUSEUM AND AFFILIATE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 4 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)**

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

*Equity Securities and Corporate Bonds:* Valued at the closing price reported on the active market on which the individual securities are traded.

*Mutual Funds:* Valued at the net asset value (NAV) of shares held by the Museum at year-end or the closing price reported on the active market on which the individual shares are traded.

The following table presents assets and liabilities measured at fair value by classification within the fair value hierarchy as of September 30, 2017:

	Level 1	Level 2	Level 3	Total
Equity Securities	\$ 4,174,903	\$ -	\$ -	\$ 4,174,903
Mutual Funds:				
Equity Funds	1,704,576	-	-	1,704,576
Bond Funds	3,393,931	-	-	3,393,931
Corporate Bonds				
Net of Cash Equivalents	1,065,685	9,181	-	1,074,866
Investment Held by Arizona Community Foundation	-	-	89,601	89,601
Total	<u>\$ 10,339,095</u>	<u>\$ 9,181</u>	<u>\$ 89,601</u>	<u>\$ 10,437,877</u>

The following table presents assets and liabilities measured at fair value by classification within the fair value hierarchy as of September 30, 2016:

	Level 1	Level 2	Level 3	Total
Equity Securities	\$ 1,744,466	\$ -	\$ -	\$ 1,744,466
Mutual Funds:				
Equity Funds	1,541,080	-	-	1,541,080
Bond Funds	590,868	-	-	590,868
Corporate Bonds	1,114,883	9,730	-	1,124,613
Investment Held by Arizona Community Foundation	-	-	83,973	83,973
Total	<u>\$ 4,991,297</u>	<u>\$ 9,730</u>	<u>\$ 83,973</u>	<u>\$ 5,085,000</u>

The Museum did not have any other assets or liabilities subject to fair value measurement at September 30, 2017 and 2016.

**THE HEARD MUSEUM AND AFFILIATE  
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SEPTEMBER 30, 2017 AND 2016**

**NOTE 4 FAIR VALUE OF FINANCIAL INSTRUMENTS (CONTINUED)**

For investments classified within the Level 3 fair value hierarchy, The Arizona Community Foundation uses the NAV to determine the fair value of the Museum's investments, which does not have a readily determinable fair value. The Museum used the investee's NAV as a practical expedient for measuring fair value. The investment held by Arizona Community Foundation does not have any unfunded commitments as of September 30, 2017. At least annually, management determines if the current valuation technique is appropriate.

The table below presents the change in fair value measurements that used Level 3 inputs during the year ended September 30:

	2017	2016
Balance on October 1,	\$ 83,973	\$ 83,041
Net Realized/Unrealized Investment Gains	8,716	5,149
Dividend and Interest Income	1,262	808
Investment Advisory Fees	(650)	(625)
Investment Draw	(3,700)	(4,400)
Balance on September 30	\$ 89,601	\$ 83,973

**NOTE 5 PROPERTY AND EQUIPMENT**

Property and equipment consist of the following:

	2017	2016
Land and Buildings	\$ 22,512,378	\$ 22,512,378
Buildings Improvements	6,746,972	4,136,202
Furniture, Fixtures, and Equipment	3,694,309	3,303,016
Long-Term Exhibits	9,492,774	9,492,774
Software	130,472	130,472
Construction in Progress	9,588	588,930
Total	42,586,493	40,163,772
Less: Accumulated Depreciation and Amortization	(25,414,727)	(23,692,590)
Total Property and Equipment, Net	\$ 17,171,766	\$ 16,471,182

Depreciation and amortization expense charged to operations for the year ended September 30, 2017 and 2016 was \$1,727,321 and \$1,621,708, respectively.

Construction in progress as of September 30, 2017 relates primarily to upgrades in the boarding school exhibit. Construction in progress as of September 30, 2016 relates to upgrades of the Museum's exhibits and security system projects for 2016. Interest expense has not been capitalized on the construction in progress due to its immateriality.

**THE HEARD MUSEUM AND AFFILIATE  
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SEPTEMBER 30, 2017 AND 2016**

**NOTE 6 LINES OF CREDIT, BANK**

As of September 30, 2017, the Museum had a revolving line of credit with a maximum borrowing limit of \$800,000 and a nonrevolving line of credit with a maximum borrowing limit of \$603,541. The lines of credit were set to mature March 2018 and were secured by receivables, merchandise inventory, and property and equipment, and interest was payable monthly at a rate equal to the index (prime rate). The index for the year ended September 30, 2017 was 4.25%. The lines of credit were subject to certain financial covenants. As of September 30, 2017, management believes the Museum was in compliance with these covenants. The outstanding balance on the revolving line of credit and the nonrevolving line of credit was \$300,000 and \$500,536 at September 30, 2017, respectively, and \$300,000 and \$797,709 at September 30, 2016, respectively.

Subsequent to year-end, on January 31, 2018, the lines of credit were refinanced with a different lender and the previous lines of credit were closed. The Museum established a revolving line of credit with a maximum borrowing limit of \$800,000 and interest only payments due monthly until maturity in January 2019 at which time any outstanding advances and accrued interest are due in full. Additionally, a term loan was established in the amount of \$369,000 with interest only payments due for one year and then principal and interest payments due for five years until maturity in December 2024. Interest on both the revolving line of credit and term loan is based on a floating rate equal to the Wall Street Journal prime rate minus 0.75%. The line of credit and term loan are secured by a first priority lien on all chattel paper, accounts, equipment, fixtures, general intangibles, and all nonaccessioned shop inventory and are subject to certain financial covenants.

**NOTE 7 NOTE PAYABLE**

During 2016, the Museum executed a financing agreement for purchase of software for \$57,349. The agreement is noninterest bearing. The agreement matured in April 2017 and had an outstanding balance of \$0- and \$28,674 at September 30, 2017 and 2016, respectively.

**NOTE 8 SPLIT-INTEREST AGREEMENTS**

Charitable gift annuities are arrangements between a donor and the Museum in which the donor contributes assets in exchange for a promise from the Museum to pay the donor a fixed amount for a specified period of time. Assets received have been recognized at fair value, and an annuity payment liability has been recognized at the present value of the future cash flows expected to be paid. Contribution support is recognized as the difference between these two amounts. The life expectancy tables published by the Internal Revenue Service and a 3.20% discount rate were used to calculate the present value of the charitable gift annuities.

**THE HEARD MUSEUM AND AFFILIATE  
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**NOTE 8 SPLIT-INTEREST AGREEMENTS (CONTINUED)**

During 2011, the Museum recognized and recorded split-interest agreements classified as charitable gift annuities, which are reported separately as assets and liabilities in the accompanying consolidated statements of financial position. The gift annuity agreements were to provide funds for operations. The assets received by the Museum are included in investments. As of September 30, 2017 and 2016, the annuity payable was \$22,678 and \$26,586, respectively.

The Museum reports contribution support from split-interest agreements in contributions and donations in the accompanying consolidated statements of activities. The change in investment valuation of split-interest agreements is reported in investment income in the accompanying consolidated statements of activities.

**NOTE 9 UNRESTRICTED BOARD-DESIGNATED NET ASSETS**

Unrestricted board-designated net assets consist of amounts designated as long-term investments for the purpose of building an endowment fund to secure the future of the Museum's mission. The earnings from the long-term investments are currently being reinvested and are also designated for this purpose. Additionally, unrestricted board-designated net assets consist of amounts that are held in investment accounts for purposes as designated by the board. Interest income earned on these accounts is also designated for this purpose.

**NOTE 10 TEMPORARILY RESTRICTED NET ASSETS**

Temporarily restricted net assets consist of amounts restricted for the following:

	2017	2016
Collections	\$ 346,918	\$ 158,973
Nichols Publications	64,136	210,386
Building Improvements	16,976	2,163,290
Exhibits and Events	917,129	1,001,165
Gift Annuities	22,678	26,586
Heard Perpetual Trust Accumulated Earnings	241,373	75,475
Other Accumulated Earnings	222,268	-
Total Temporarily Restricted Net Assets	<u>\$ 1,831,478</u>	<u>\$ 3,635,875</u>

**THE HEARD MUSEUM AND AFFILIATE  
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**NOTE 11 PERMANENTLY RESTRICTED NET ASSETS**

Permanently restricted net assets consist of amounts restricted for the following:

	2017	2016
Collections Endowment	\$ 579,906	\$ 579,906
Endowment	351,202	351,202
Whiteman Fund	-	250,000
Heard Tomorrow Endowment	298,189	298,189
Hearst Fund	200,000	200,000
Roger Lyon Scholarship Fund	131,100	131,100
S D O'Conner Publishing Fund	190,000	190,000
Steele Foundation fund	100,000	100,000
Heard Perpetual Trust	2,642,288	2,642,288
Nichols Collection Fund	301,321	301,321
Cowie Heard North Programming Endowment	105,000	95,000
Baguley Fund	50,661	50,661
Jay Kahn Memorial Fund	15,662	15,662
Dickey Family Director Endowment	2,400,000	-
Total Permanently Restricted Net Assets	\$ 7,365,329	\$ 5,205,329

Permanently restricted net assets consist of funds for which the donors stipulated the principal is to be maintained in perpetuity. The earnings on these funds are temporarily restricted for specific purposes by the endowment donors and are unrestricted once appropriated for expenditure. Net appreciation on permanently restricted funds is included as a change in unrestricted and temporarily restricted net assets.

**NOTE 12 ENDOWMENTS**

The Museum's endowments consist of several funds established for a variety of purposes. The endowment funds include both donor-restricted and board-designated endowment funds. As required by generally accepted accounting principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The executive committee of the board of trustees of the Museum has interpreted the State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Museum classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Museum in a manner consistent with the standard of prudence prescribed by SPMIFA.

**THE HEARD MUSEUM AND AFFILIATE  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**NOTE 12 ENDOWMENTS (CONTINUED)**

In accordance with SPMIFA, the Museum considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds are as follows:

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

As of September 30, 2017, endowment net assets consisted of the following:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor Restricted Endowment Net Assets	\$ -	\$ 463,641	\$ 7,365,329	\$ 7,828,970
Board-Designated Endowment Net Assets	2,191,828	-	-	2,191,828
Total	<u>\$ 2,191,828</u>	<u>\$ 463,641</u>	<u>\$ 7,365,329</u>	<u>\$ 10,020,798</u>

As of September 30, 2016, endowment net assets consisted of the following:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor Restricted Endowment Net Assets	\$ -	\$ 75,475	\$ 5,205,329	\$ 5,280,804
Board-Designated Endowment Net Assets	245,127	-	-	245,127
Total	<u>\$ 245,127</u>	<u>\$ 75,475</u>	<u>\$ 5,205,329</u>	<u>\$ 5,525,931</u>

Changes in endowment net assets for the year ended September 30, 2017, are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Net Assets - Beginning of Year	\$ 245,127	\$ 75,475	\$ 5,205,329	\$ 5,525,931
Contributions	1,850,566	-	2,410,000	4,260,566
Change in Donor Intent	-	-	(250,000)	(250,000)
Investment Returns:	-	-	-	-
Investment Income and Gains and Losses	96,135	521,454	-	617,589
Appropriation of Assets for Expenditures	-	(133,288)	-	(133,288)
Endowment Net Assets - End of Year	<u>\$ 2,191,828</u>	<u>\$ 463,641</u>	<u>\$ 7,365,329</u>	<u>\$ 10,020,798</u>

**THE HEARD MUSEUM AND AFFILIATE  
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**NOTE 12 ENDOWMENTS (CONTINUED)**

Changes in endowment net assets for the year ended September 30, 2016, are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment Net Assets - Beginning of Year, as Restated	\$ 316,401	\$ -	\$ 4,884,008	\$ 5,200,409
Contributions	-	-	321,321	321,321
Investment Returns:				
Investment Income	253,126	187,818	-	440,944
Appropriation of Assets for Expenditure	(324,400)	(112,343)	-	(436,743)
Endowment Net Assets - End of Year	<u>\$ 245,127</u>	<u>\$ 75,475</u>	<u>\$ 5,205,329</u>	<u>\$ 5,525,931</u>

From time-to-time, the fair value of assets associated with individual donor-restricted endowment funds may exceed or fall below the level that the donor or SPMIFA requires the Museum to retain as a fund of perpetual duration. There were no deficiencies of this nature that are reported in unrestricted or temporarily restricted net assets as of September 30, 2017 and 2016.

The Museum has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowments. Under this policy, the endowment assets are invested in a manner that is intended to produce results while assuming a moderate level of investment risk.

To satisfy its long-term rate-of-return objectives, the Museum relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Museum targets a diversified asset allocation that consists of equity-based investments and fixed-income funds.

The Museum's annual appropriations are at the discretion of the board of trustees unless specific instructions were provided by the endowment donors.

**NOTE 13 FUNCTIONAL EXPENSES**

The costs of providing various programs and other activities consist of the following:

	2017	2016
Program	\$ 8,636,423	\$ 7,693,741
Management and General	2,524,186	2,439,859
Fundraising	862,857	808,479
Total Functional Expenses	<u>\$ 12,023,466</u>	<u>\$ 10,942,079</u>

**THE HEARD MUSEUM AND AFFILIATE  
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**NOTE 13 FUNCTIONAL EXPENSES (CONTINUED)**

Certain costs have been allocated among program and supporting services benefited in the table above. Management and general include those expenses that are not directly identifiable with any specific program, but provide for the overall support and direction of the Museum. Any expenditure not directly chargeable to a functional expense category is allocated based on personnel activity and other appropriate allocation methods.

**NOTE 14 LEASES**

The Museum leases equipment under noncancellable operating leases with no renewal options maturing through August 2021.

Minimum future rental payments under noncancellable operating leases in excess of one year are as follows:

<u>Year Ending September 30,</u>	<u>Amount</u>
2018	\$ 17,352
2019	16,768
2020	15,600
2021	14,300
Total Minimum Future Rental Payments	<u><u>\$ 64,020</u></u>

Total rental expense was \$21,403 and \$17,270 for the years ended September 30, 2017 and 2016, respectively.

**NOTE 15 DEFINED CONTRIBUTION PLAN**

The Museum has a discretionary employer contribution plan covering all employees who have completed one year of at least 1,000 hours of service. The Museum contributes to the plan an amount determined by the board of trustees on an annual basis. The total employer contribution is allocated to the participants pro-rata based on the ratio that their eligible compensation bears to total eligible compensation for the plan year. The participants are not required to make contributions to the plan. There were no employer contributions for 2017 and 2016, respectively.

**NOTE 16 RELATED PARTIES**

During 2017 and 2016, the Museum received contributions from board members totaling \$5,277,358 and \$292,352, respectively.



**THE HEARD MUSEUM AND AFFILIATE**  
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**NOTE 17 CONCENTRATION OF CREDIT RISKS**

The Museum maintains all of its cash with banks located in Arizona. Balances on deposits are insured by the Federal Deposit Insurance Corporation (FDIC) up to specified limits. Balances in excess of FDIC limits are uninsured. The Museum, in the normal course of business, periodically maintains account balances in excess of the FDIC's insurance coverage limit.

Contributions totaling \$5,000,000 and \$1,100,000, were received from single donors for the years ended September 30, 2017 and 2016, respectively, which represents 28% and 11%, respectively, of total revenues. Should these contribution levels decrease, the Museum may be adversely affected.

**NOTE 18 CONTINGENCIES**

From time-to-time, the Museum is contingently liable in respect to claims incidental to the ordinary course of its operations. In the opinion of management, the effect of such matters will not have a material adverse effect on the Museum's financial position, results of operations, or liquidity. Therefore, no provision has been made in the accompanying consolidated financial statements for losses, if any, that might result from the ultimate outcome of these matters.