

FINANCIAL STATEMENTS

The Cleveland Museum of Art  
Years Ended June 30, 2015 and 2014  
With Report of Independent Auditors

Ernst & Young LLP



Building a better  
working world

The Cleveland Museum of Art

Financial Statements

Years Ended June 30, 2015 and 2014

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## Report of Independent Auditors

The Board of Trustees  
The Cleveland Museum of Art

We have audited the accompanying financial statements of The Cleveland Museum of Art, which comprise the statements of financial position as of June 30, 2015 and 2014, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

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

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

### **Auditor's Responsibility**

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

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

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



## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Cleveland Museum of Art as of June 30, 2015 and 2014, and the changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

*Ernst + Young LLP*

November 25, 2015

The Cleveland Museum of Art

Statements of Financial Position  
(In Thousands)

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 4,094	\$ 4,713
Investments for current use	769	4,488
Accounts receivable	426	222
Inventories	1,035	1,181
Other current assets	1,980	2,300
Total current assets	<u>8,304</u>	12,904
Investments:		
Endowment investments	444,100	449,833
Other investments	42,356	27,957
Buildings and equipment:		
Buildings and improvements	386,621	372,658
Equipment	22,664	21,659
Construction-in-progress	1,437	14,904
	<u>410,722</u>	409,221
Less accumulated depreciation	92,138	81,128
Total buildings and equipment – net	<u>318,584</u>	328,093
Other assets:		
Charitable perpetual trusts	315,215	323,061
Pledges receivable	24,582	10,639
Other	1,566	1,725
	<u>341,363</u>	335,425
Total assets	<u><u>\$ 1,154,707</u></u>	<u><u>\$ 1,154,212</u></u>

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
<b>Liabilities and net assets</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 3,235	\$ 3,653
Deferred revenue	623	378
Other current liabilities	203	191
Total current liabilities	<u>4,061</u>	4,222
Long-term debt	163,473	163,997
Other liabilities:		
Accrued postretirement medical benefits	699	711
Accrued pension obligation	10,207	7,496
Other	12,276	11,304
	<u>23,182</u>	19,511
Total liabilities	<u>190,716</u>	187,730
Net assets:		
Unrestricted	105,497	110,852
Temporarily restricted	461,586	452,072
Permanently restricted	396,908	403,558
Total net assets	<u>963,991</u>	966,482
Total liabilities and net assets	<u><u>\$ 1,154,707</u></u>	<u><u>\$ 1,154,212</u></u>

*See accompanying notes.*

# The Cleveland Museum of Art

## Statement of Activities (In Thousands)

Year Ended June 30, 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Revenues and support</b>				
Endowment and trust income	\$ 13,029	\$ 9,630	\$ -	\$ 22,659
Contributions and membership	4,734	27,550	-	32,284
Gifts, grants, and other revenue for special exhibitions	404	2	-	406
Program revenues and other support	4,292	996	-	5,288
Stores, café, parking, and products	2,754	-	-	2,754
Net assets released from restrictions used for operations	28,083	(28,083)	-	-
Total revenues and support	53,296	10,095	-	63,391
<b>Expenses</b>				
Curatorial, conservation, and registrar	7,938	-	-	7,938
Special exhibitions	1,534	-	-	1,534
Education, library, and community programs	4,892	-	-	4,892
Marketing and communications	1,985	-	-	1,985
Development and membership services	4,476	-	-	4,476
General and administrative	5,665	-	-	5,665
Building, facilities, and security	13,888	-	-	13,888
Stores, café, parking, and products	1,777	-	-	1,777
Depreciation	11,010	-	-	11,010
Total expenses	53,165	-	-	53,165
Excess of revenues and support over expenses before other changes in net assets	131	10,095	-	10,226
<b>Other changes in net assets</b>				
Trust revenue designated for art purchases	-	5,248	-	5,248
Investment return designated for art purchase	-	6,256	-	6,256
Net assets released from restrictions used to fund acquisition of art objects	5,652	(5,652)	-	-
Expenditures for acquisition of art objects	(6,302)	-	-	(6,302)
Gifts and contributions	17	687	1,196	1,900
Investment return after amounts designated	(2,357)	(7,120)	-	(9,477)
Change in fair value of derivative instruments	401	-	-	401
Change in fair value of charitable perpetual trusts	-	-	(7,846)	(7,846)
Changes in funded status of pension benefits	(2,495)	-	-	(2,495)
Changes in funded status of postretirement medical benefits	(402)	-	-	(402)
(Decrease) increase in net assets	(5,355)	9,514	(6,650)	(2,491)
Net assets at beginning of year	110,852	452,072	403,558	966,482
Net assets at end of year	\$ 105,497	\$ 461,586	\$ 396,908	\$ 963,991

See accompanying notes.

# The Cleveland Museum of Art

## Statement of Activities (In Thousands)

Year Ended June 30, 2014

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Revenues and support</b>				
Endowment and trust income	\$ 13,067	\$ 10,110	\$ –	\$ 23,177
Contributions and membership	4,615	10,529	–	15,144
Gifts, grants, and other revenue for special exhibitions	1,018	–	–	1,018
Program revenues and other support	4,011	789	–	4,800
Stores, café, parking, and products	2,727	–	–	2,727
Net assets released from restrictions used for operations	28,090	(28,090)	–	–
Total revenues and support	53,528	(6,662)	–	46,866
<b>Expenses</b>				
Curatorial, conservation, and registrar	7,060	–	–	7,060
Special exhibitions	3,785	–	–	3,785
Education, library, and community programs	4,546	–	–	4,546
Marketing and communications	2,504	–	–	2,504
Development and membership services	4,272	–	–	4,272
General and administrative	5,365	–	–	5,365
Building, facilities, and security	13,434	–	–	13,434
Stores, café, parking, and products	1,771	–	–	1,771
Depreciation	10,769	–	–	10,769
Total expenses	53,506	–	–	53,506
Excess (deficit) of revenues and support over expenses before other changes in net assets	22	(6,662)	–	(6,640)
<b>Other changes in net assets</b>				
Trust revenue designated for art purchases	–	4,826	–	4,826
Investment return designated for art purchase	–	9,319	–	9,319
Net assets released from restrictions used to fund acquisition of art objects	17,762	(17,762)	–	–
Expenditures for acquisition of art objects	(17,762)	–	–	(17,762)
Proceeds from the deaccession of art	–	7,952	–	7,952
Gifts and contributions	–	94	8,795	8,889
Other changes	(64)	(112)	54	(122)
Investment return after amounts designated	4,905	30,500	–	35,405
Change in fair value of derivative instruments	356	–	–	356
Change in fair value of charitable perpetual trusts	–	–	30,105	30,105
Changes in funded status of pension benefits	(1,908)	–	–	(1,908)
Changes in funded status of postretirement medical benefits	(290)	–	–	(290)
Increase in net assets	3,021	28,155	38,954	70,130
Net assets at beginning of year	107,831	423,917	364,604	896,352
Net assets at end of year	\$ 110,852	\$ 452,072	\$ 403,558	\$ 966,482

See accompanying notes.



# The Cleveland Museum of Art

## Statements of Cash Flows (In Thousands)

	<b>Year Ended June 30</b>	
	<b>2015</b>	<b>2014</b>
<b>Operating activities</b>		
Reconciliation of (decrease) increase in net assets to net cash used in operating activities:		
(Decrease) increase in net assets	\$ (2,491)	\$ 70,130
Adjustments to reconcile (decrease) increase in net assets to cash used in operating activities:		
Depreciation and amortization	11,010	10,769
Amortization of bond premiums	(524)	(505)
Change in fair value of derivative instruments	(401)	(356)
Net realized and unrealized gains on long-term investments	(6,309)	(53,347)
Contributions restricted for long-term purposes	(27,550)	(10,529)
Increase (decrease) in fair value of charitable perpetual trusts	7,846	(30,105)
Acquisitions and sales of art, net	5,652	9,810
Changes in funded status of pension and postretirement medical benefits	2,897	2,198
Changes provided by (used in) operating assets and liabilities:		
Accounts receivable	(204)	(110)
Inventories and other current assets	466	1,617
Pledges receivable	(13,943)	2,159
Other assets	159	132
Accounts payable and accrued expenses	(418)	(5,058)
Deferred revenue	245	(23)
Other current liabilities	12	(11)
Other liabilities	1,175	(357)
Net cash used in operating activities	<u>(22,378)</u>	<u>(3,586)</u>
<b>Financing activities</b>		
Contributions restricted for long-term purposes	27,550	10,529
Net cash provided by financing activities	<u>27,550</u>	<u>10,529</u>
<b>Investing activities</b>		
Purchases of buildings and equipment	(1,501)	(3,121)
Acquisition of art objects	(5,652)	(17,762)
Proceeds from the deaccession of art	-	7,952
Proceeds from sales and maturities of investments	30,896	37,205
Purchases of investments	(29,534)	(35,656)
Net cash used in investing activities	<u>(5,791)</u>	<u>(11,382)</u>
Net decrease in cash and cash equivalents	(619)	(4,439)
Cash and cash equivalents at beginning of year	4,713	9,152
Cash and cash equivalents at end of year	<u>\$ 4,094</u>	<u>\$ 4,713</u>

See accompanying notes.

# The Cleveland Museum of Art

## Notes to Financial Statements *(In Thousands, Unless Noted)*

June 30, 2015

### **1. Organization**

The Cleveland Museum of Art (the Museum) maintains in the City of Cleveland a museum of art of the widest scope for the benefit of the public.

### **2. Significant Accounting Policies**

#### **Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### **Temporarily and Permanently Restricted Net Assets**

Temporarily restricted net assets are used to differentiate resources, the use of which is restricted by donors or grantors to a specific time period or for a specific purpose, from resources on which no restrictions have been placed or that arise from the general operations of the Museum. Temporarily restricted gifts, grants, and bequests are recorded as additions to temporarily restricted net assets in the period received. When restricted net assets are expended for their stipulated purpose or time restriction expires, temporarily restricted net assets become unrestricted net assets and are reported in the statements of activities as net assets released from restrictions. For temporarily restricted net assets restricted for major capital projects, the Museum has adopted a policy of implying a time restriction on the use of such assets that expires over the assets' useful lives. The Museum records a reclassification to unrestricted net assets as net assets released from restrictions for an amount equal to annual depreciation for building and improvements constructed with restricted funds. Reclassifications of \$14,944 and \$14,945 in fiscal 2015 and 2014, respectively, are reflected in the statements of activities in net assets released from restrictions used for operations.

Permanently restricted net assets consist of amounts held in perpetuity as designated by the donors. Earnings on investments are included in temporarily restricted revenues and other changes in net assets until appropriated for expenditure by the Museum in accordance with the donors' specifications. The Museum is the income beneficiary of several charitable perpetual trusts. Because the trusts are not controlled by the Museum and the trust assets are held in perpetuity, the assets are classified as permanently restricted net assets. The Museum records its interest in charitable perpetual trusts at its pro rata share of the fair value of the underlying assets.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **2. Significant Accounting Policies (continued)**

Income distributed to the Museum by the trusts of \$14,219 and \$13,716 in fiscal 2015 and 2014, respectively, is included in endowment and trust income and trust revenue designated for art purchases on the statements of activities.

During fiscal 2010, the Museum received approval from the Court of Common Pleas, Probate Division to appropriate a percentage of the income restricted for art purchases generated from four charitable perpetual trusts for the purpose of funding the project costs and debt service costs associated with the expansion project recently completed by the Museum. The total appropriated is not to exceed \$75,000. During fiscal 2015 and 2014, the Museum appropriated approximately \$5,889 and \$5,500, respectively, for said purpose from the temporarily restricted income from the four charitable perpetual trusts.

### **Art Collection**

The Museum's collections are made up of art objects and artifacts of historical significance that are held for educational, research, scientific, and curatorial purposes. Each of the items is cataloged, preserved, and cared for, and activities verifying their existence and assessing their condition are performed continuously.

Purchases for the collection are recorded as expenditures for the acquisition of art objects in the statements of activities in the year in which the objects are acquired. Proceeds from the deaccession of art objects are recorded as temporarily restricted net assets and are restricted to the acquisition of other art objects. In keeping with standard museum practice, the collections, which were acquired via purchases and contributions, are not recognized as assets on the statements of financial position. Art purchases included in accounts payable and accrued expenses and thus not presented in the statements of cash flows are \$650 and \$0 for the years ended June 30, 2015 and 2014, respectively.

### **Cash Equivalents**

Cash equivalents are highly liquid investments with a maturity of three months or less when purchased. Cash equivalents are measured at fair value in the statements of financial position and exclude amounts limited to use by donor or board designation.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **2. Significant Accounting Policies (continued)**

#### **Inventories**

Inventories consist of merchandise available for sale and are stated at the lower of average cost or market.

#### **Investments and Investment Income**

Endowment investments include both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. Other investments are primarily funds designated by the Board of Trustees for specific purposes.

Realized investment gains or losses are determined by comparison of the carrying value to net proceeds received on the settlement date. Unrealized gains or losses are determined by the difference between carrying value and fair value as of year-end. Investment income, including dividends and interest, and realized and unrealized gains (losses), is added to (deducted from) the appropriate net assets class (Note 8).

Investment income generated by permanently restricted net assets for which use of the income is restricted by the donor is reported as temporarily restricted until the program restriction of the donor is met. Investment income on temporarily restricted net assets for which use of the income is restricted by the donor is reported as temporarily restricted until the program restriction of the donor is met. Net unrealized and realized investment gains and losses are reported as unrestricted, temporarily restricted, or permanently restricted based upon the absence or presence of a restriction on the underlying asset.

#### **Donated Services**

No amounts have been reflected in the financial statements for donated services. The Museum pays for most services requiring specific expertise. However, many individuals volunteer their time and perform a variety of tasks that assist the Museum with various programs.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **2. Significant Accounting Policies (continued)**

#### **Special Exhibitions**

Other current assets and deferred revenue include expenditures and revenues in connection with the development of special exhibitions. Revenues and expenses are recognized pro rata over the life of the exhibition. Revenues include such items as corporate and individual sponsorships. The expenditures generally include such items as research, travel, insurance, transportation, and other costs related to the development and installation of the exhibition.

#### **Contributions**

Unconditional pledges to give cash, marketable securities, and other assets are discounted to present value at the date the pledge is made to the extent estimated to be collectible by the Museum. Unconditional pledges are classified as other assets on the statements of financial position. Conditional promises to give and indications of intentions to give are not recognized until the condition is satisfied. Pledges received with donor restrictions that limit use are reported as either temporarily or permanently restricted support, or other changes in net assets if designated for long-term investment. When a donor 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 statements of activities as net assets released from restrictions.

#### **Buildings and Equipment**

Buildings and equipment are carried at cost. Expenditures that substantially increase the useful lives of existing assets are capitalized. Routine maintenance and repairs are expensed as incurred. Depreciation is computed by the straight-line method using the estimated useful lives of the assets. Buildings and improvements are assigned a useful life of up to 40 years. Equipment is assigned a useful life ranging from three to five years. Net interest cost incurred on borrowed funds during the period of construction of capital assets is capitalized as a component of the cost of acquiring those assets.

The Museum recently completed a major construction, renovation, and expansion project. Included in construction-in-progress are \$343 related to gallery renovations and the construction of the maintenance facility, and \$12,280 related to the expansion and renovation project at June 30, 2015 and 2014, respectively. Capital expenditures included in accounts payable and accrued expenses and thus not presented in the statements of cash flows are \$0 and \$373 for the years ended June 30, 2015 and 2014, respectively.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

### 2. Significant Accounting Policies (continued)

On January 10, 2013, the Museum entered into an agreement with another party to jointly purchase property. A payment of \$500 was deposited with an escrow agent and was held by the agent until the closing date of the transaction, which was September 30, 2015. The Museum made the final payment of \$4,100 on the closing date. The deposit is included in investments in the statements of financial position at June 30, 2015 and 2014.

### Derivative Instruments

The Museum recognizes its derivative instruments as either an asset or liability in the statements of financial position at fair value. The change in fair value of the derivative instruments is recognized in the statements of activities as other changes in net assets in the period of change.

### Recent Accounting Pronouncement

In April 2015, the FASB issued ASU No. 2015-03, *Interest – Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs*, requiring that debt issuance costs related to a recognized debt liability be presented as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 is effective for fiscal years beginning after December 15, 2015 with early adoption permitted. The Museum is currently evaluating the new guidance and will adopt the provisions as required upon the effective date.

In May 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2015-07, *Fair Value Measurement (ASC 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*. This ASU eliminates the requirement to categorize within the fair value hierarchy investments whose fair values are measured at net asset value (NAV) as a practical expedient. The amendment within this ASU is effective for reporting periods beginning after December 15, 2015 with early adoption permitted retrospectively. The Museum is currently evaluating the new guidance and will adopt the provisions as required upon the effective date.

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**3. Pledges Receivable**

Outstanding pledges receivable from various corporations, foundations, and individuals are expected to be realized as follows:

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
Pledges due:		
In less than one year	\$ 3,435	\$ 4,039
In one to five years	10,276	6,288
Greater than five years	15,064	1,144
	<u>28,775</u>	<u>11,471</u>
Present value discount on pledges (1.80%–5.38% discount rate)	(4,193)	(832)
	<u>\$ 24,582</u>	<u>\$ 10,639</u>

**4. Temporarily Restricted Net Assets**

Temporarily restricted net assets are available for the following purposes:

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
Acquisition of art	\$ 167,771	\$ 169,051
Specific operating activities:		
Curatorial and conservation	6,277	5,783
Education, library, and community programs	8,906	9,190
Buildings, grounds, and protection services	197,554	180,540
General operating and other	81,078	87,508
Total temporarily restricted net assets	<u>\$ 461,586</u>	<u>\$ 452,072</u>

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**5. Permanently Restricted Net Assets**

Permanently restricted net assets are amounts held in perpetuity, the income from which is expendable to support the following purposes:

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
Purchase of art	\$ 143,514	\$ 144,800
Specific operating activities	30,876	28,850
General operating activities	222,518	229,908
Total permanently restricted net assets	<u>\$ 396,908</u>	<u>\$ 403,558</u>

**6. Net Assets Released From Restrictions**

Net assets were released from restrictions by incurring expenses or making capital expenditures satisfying the restricted purposes as follows:

	<b>Year Ended June 30</b>	
	<b>2015</b>	<b>2014</b>
Acquisition of art	<u>\$ 5,652</u>	<u>\$ 17,762</u>
Specific operating activities:		
Curatorial and conservation	\$ 1,638	\$ 1,295
Education, library, and community programs	898	982
Buildings, grounds, and protection services	20,811	20,826
General operating and other	4,736	4,987
Net assets released from restrictions used for operations	<u>\$ 28,083</u>	<u>\$ 28,090</u>



# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **7. Fair Value Measurements**

Accounting Standards Codification (ASC) 820, *Fair Value Measurement*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establishes a framework for measuring fair value. ASC 820 establishes a three-level hierarchy for fair value measurement based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date, as follows:

- Level 1 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 – Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the same term of the financial instrument.
- Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

## The Cleveland Museum of Art

### Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

#### 7. Fair Value Measurements (continued)

The following table presents the financial instruments carried at fair value at June 30, 2015, by the ASC 820 valuation hierarchy defined above:

	Level 1	Level 2	Level 3	Total Fair Value
<b>Assets</b>				
Investments for current use:				
Commercial paper	\$           –	\$        769	\$           –	\$        769
Endowment investments:				
Cash and cash equivalents	15,082	–	–	15,082
Equities:				
Common stocks, primarily U.S.	67,390	–	–	67,390
Collective equity funds	–	101,321	–	101,321
Equity mutual funds	125,029	–	–	125,029
American depository receipts	7,487	–	–	7,487
Real estate investment trust	421	–	–	421
Fixed income securities:				
Corporate bonds	–	12,610	–	12,610
Asset-backed securities	–	3,253	–	3,253
Mortgage-backed securities	–	9,237	–	9,237
Government bonds	–	1,224	–	1,224
Fixed income mutual fund	8,928	–	–	8,928
Alternative investments:				
Absolute return	–	–	49,581	49,581
Private equity	–	–	42,537	42,537
Total endowment investments	224,337	127,645	92,118	444,100
Other investments:				
Cash and cash equivalents	7,269	–	–	7,269
Commercial paper	–	35,087	–	35,087
Total other investments	7,269	35,087	–	42,356
Charitable perpetual trusts	–	–	315,215	315,215
Total assets at fair value	\$   231,606	\$   163,501	\$   407,333	\$   802,440
<b>Liabilities</b>				
Interest rate swap	\$           –	\$       7,863	\$           –	\$       7,863
Total liabilities at fair value	\$           –	\$       7,863	\$           –	\$       7,863

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### 7. Fair Value Measurements (continued)

The following table presents the financial instruments carried at fair value at June 30, 2014, by the ASC 820 valuation hierarchy defined above:

	Level 1	Level 2	Level 3	Total Fair Value
<b>Assets</b>				
Investments for current use:				
Commercial paper	\$           –	\$       4,488	\$           –	\$       4,488
Endowment investments:				
Cash and cash equivalents	16,525	–	–	16,525
Equities:				
Common stocks, primarily U.S.	64,088	–	–	64,088
Collective equity funds	–	99,454	–	99,454
Equity mutual funds	118,734	–	–	118,734
American depository receipts	7,130	–	–	7,130
Real estate investment trust	331	–	–	331
Fixed income securities:				
Corporate bonds	–	10,626	–	10,626
Asset-backed securities	–	2,444	–	2,444
Mortgage-backed securities	–	11,757	–	11,757
Government bonds	–	465	–	465
Fixed income mutual fund	8,775	–	–	8,775
Alternative investments:				
Absolute return	–	–	61,013	61,013
Private equity	–	–	48,491	48,491
Total endowment investments	215,583	124,746	109,504	449,833
Other investments:				
Commercial paper	–	27,957	–	27,957
Charitable perpetual trusts	–	–	323,061	323,061
Total assets at fair value	<u>\$   215,583</u>	<u>\$   157,191</u>	<u>\$   432,565</u>	<u>\$   805,339</u>
<b>Liabilities</b>				
Interest rate swap	\$           –	\$       8,264	\$           –	\$       8,264
Total liabilities at fair value	<u>\$           –</u>	<u>\$       8,264</u>	<u>\$           –</u>	<u>\$       8,264</u>

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **7. Fair Value Measurements (continued)**

The following is a description of the Museum's valuation methodologies for assets and liabilities measured at fair value. Fair value for Level 1 is based upon quoted market prices. Fair value for Level 2 is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Inputs are obtained from various sources including market participants, dealers, and brokers. Fair value for Level 2 investments in collective equity funds are valued at net asset value (NAV).

Fixed income securities include debt obligations of the U.S. government and various agencies, U.S. corporations, and other fixed income instruments such as asset-backed and mortgage-backed securities. The composition of these securities represents an expected return and risk profile that is commensurate with broadly defined fixed income indexes such as the Barclays Capital U.S. Aggregate Index. Additionally, fixed income securities include fixed income mutual funds that may also invest opportunistically in mortgage-backed and asset-backed securities as well as non-U.S. and high-yield debt instruments.

Equities include investments of publicly traded common stocks of both U.S. and international corporations, the majority of which represent actively traded and liquid securities that are traded on many of the world's major exchanges and include large-, mid-, and small-capitalization securities. The composition of these securities represents an expected return and risk profile that is commensurate with broadly defined equity indexes such as the Russell 3000 Index. Included in Level 2 are equity investments that reside in commingled equity funds whose underlying assets may include publicly traded equity securities.

Level 3 assets consist of charitable perpetual trusts and alternative investments. The Museum is the sole income beneficiary of several charitable perpetual trusts and a partial income beneficiary of other charitable perpetual trusts. The charitable perpetual trusts are presented at the fair value of the Museum's portion of the underlying trust assets. Since the Museum has no right to the underlying investments, the charitable perpetual trusts have been classified as Level 3. Fair value of alternative investments (principally limited partnership interests in absolute return and private equity) represent the Museum's ownership interest in the NAV of the respective partnership. Investments held by the partnerships consist of marketable securities as well as securities that do not have readily determinable fair values. The fair values of the securities held by limited partnerships that do not have readily determinable fair values are determined by the general

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **7. Fair Value Measurements (continued)**

partner and are based on historical cost, appraisals, or other estimates that require varying degrees of judgment. If no public market exists for the investment securities, the fair value is determined by the general partner, taking into consideration, among other things, the cost of the securities, prices of recent significant placements of securities of the same issuer, and subsequent developments concerning the companies to which the securities relate. Because alternative investments are not readily marketable, their estimated fair value is subject to uncertainty and therefore may differ from the value that would have been used had a ready market for such investments existed. Such differences could be material. At June 30, 2015, the Museum is committed to invest an additional \$39,449 in alternative investments. However, it is uncertain as to the timing or level of additional contributions that will ultimately be made.

Alternative investments are diversified across various strategies and may consist of absolute return funds, long/short funds, and other opportunistic funds. The underlying investments in such funds may include publicly traded and privately held equity and debt instruments issued by U.S. and international corporations as well as various derivatives based on these securities. Private equity investments generally consist of limited partnerships formed to invest in equity and debt investments in operating companies that are not publicly traded. Investment strategies in this category may include buyouts, distressed debt, and venture capital.

The fair value of the interest rate swaps was determined based on the present value of expected future cash flows using discount rates appropriate with risks involved and adjusted for a credit adjustment to reflect nonperformance risk.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Museum believes its valuation methods are 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 estimate of fair value at the reporting date.

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**7. Fair Value Measurements (continued)**

The following table is a rollforward of financial instruments classified by the Museum within Level 3 of the valuation hierarchy defined above:

	<b>Absolute Return</b>	<b>Private Equity</b>	<b>Charitable Perpetual Trusts &amp; Other</b>	<b>Total</b>
Fair value at July 1, 2013	\$ 54,159	\$ 48,247	\$ 292,956	\$ 395,362
Net realized gains	1,114	4,497	–	5,611
Net unrealized gains	13,570	3,016	30,105	46,691
Purchases	7,738	7,543	–	15,281
Distributions	(131)	(14,812)	–	(14,943)
Settlements	(15,437)	–	–	(15,437)
Fair value at June 30, 2014	61,013	48,491	323,061	432,565
Net realized gains (losses)	<b>(926)</b>	<b>2,089</b>		<b>1,163</b>
Net unrealized gains (losses)	<b>2,103</b>	<b>(3,978)</b>	<b>(7,846)</b>	<b>(9,721)</b>
Purchases	–	<b>7,925</b>	–	<b>7,925</b>
Distributions	<b>(71)</b>	<b>(11,990)</b>	–	<b>(12,061)</b>
Settlements	<b>(12,538)</b>	–	–	<b>(12,538)</b>
Fair value at June 30, 2015	<b>\$ 49,581</b>	<b>\$ 42,537</b>	<b>\$ 315,215</b>	<b>\$ 407,333</b>

At June 30, 2015, the Museum's alternative investments are subject to various liquidity restrictions as follows:

Available for redemption:	
Quarterly	\$ 13,155
Semi-annual	3,019
Subject to remaining lock-up provisions:	
One to three years	33,294
More than three years	42,650
Total alternatives	<u>\$ 92,118</u>

## The Cleveland Museum of Art

### Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

#### **7. Fair Value Measurements (continued)**

Investments that are available for redemption may be redeemed by the Museum generally with a 60-day to 120-day advance notice on a quarterly or semi-annual basis subject to the terms of the investment agreement.

Investments subject to lock-up provisions cannot be redeemed by the Museum currently without incurring a penalty. After expiration of the lock-up provisions, the funds may be redeemed by the Museum on a monthly, quarterly, or annual redemption basis subject to the terms of the investment agreement.

ASC 825, *Financial Instruments*, provides an option to elect fair value as an alternative measurement for selected financial assets and liabilities not previously recorded at fair value. The Museum did not elect fair value accounting for any assets or liabilities that are not currently required to be measured at fair value.

The carrying values of cash and cash equivalents, accounts receivable, accounts payable, and accrued expenses are reasonable estimates of their fair value due to the short-term nature of these financial instruments. The carrying value of pledges receivable approximates fair value as these donations are recorded at the net present value of the amount pledged. The carrying value of the Museum's variable rate long-term debt approximates fair value. The Museum's fixed rate long-term debt had a carrying value of \$70,430 and a fair value of \$79,953 at June 30, 2015, and a carrying value of \$70,430 and a fair value of \$72,701 at June 30, 2014. The fair value of the fixed rate long-term debt is estimated by discounted cash flow analyses using current borrowing rates for similar types of borrowing arrangements and adjusted for credit and would be classified as Level 2 inputs in the fair value hierarchy.

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**8. Investments and Charitable Perpetual Trusts**

The following summarizes returns from the Museum's investments and charitable perpetual trusts and the related classifications in the statements of activities:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>
<b>Year ended June 30, 2015</b>			
Dividends and interest	\$ 905	\$ 5,507	\$ –
Realized and unrealized gains, net of realized and unrealized losses	979	3,091	–
Change in fair value of charitable perpetual trusts	–	–	(7,846)
Investment return	1,884	8,598	(7,846)
Investment return designated for current operations (included in endowment and trust income)	(4,241)	(9,462)	–
Investment return designated for art purchase	–	(6,256)	–
Investment return after amounts designated	\$ (2,357)	\$ (7,120)	\$ (7,846)
<b>Year ended June 30, 2014</b>			
Dividends and interest	\$ 857	\$ 4,704	\$ –
Realized and unrealized gains, net of realized and unrealized losses	8,396	45,056	–
Change in fair value of charitable perpetual trusts	–	–	30,105
Investment return	9,253	49,760	30,105
Investment return designated for current operations (included in endowment and trust income)	(4,348)	(9,941)	–
Investment return designated for art purchase	–	(9,319)	–
Investment return after amounts designated	\$ 4,905	\$ 30,500	\$ 30,105



# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **8. Investments and Charitable Perpetual Trusts (continued)**

Investment return is net of investment-related expenses of \$2,249 and \$2,442 for the years ended June 30, 2015 and 2014, respectively. The Museum's investments and charitable perpetual trusts are exposed to various risks, such as interest rate, market, and credit risks.

### **9. Endowment**

On February 3, 2012, the Museum and the John Huntington Art and Polytechnic Trust (Trust), referred to collectively as the Members, entered into an operating agreement with CleveHunt LLC (the Company), an Ohio limited liability company. CleveHunt was formed for the objective and purpose of investing certain property of the Company. The investments of the Company are directed by an investment committee consisting of the members of the Museum's Investment Committee and the Trustees of the Trust.

Initial contributions to the Company consisted of substantially all of the Museum's endowment assets and all of the assets of the Trust. In exchange for these contributions, the Museum and Trust received a 73.77% and 26.23% ownership share in the Company, respectively. The contributed assets are unitized and profits and losses, including income, are allocated according to the proportion of the Members' percentage interest. Capital contributions and withdrawals adjust the Members' percentage interest. As the Museum has a controlling interest in the Company, the Museum has included all of the net assets and changes in net assets in its statements of financial position, statements of activities and statements of cash flows in either investments (including realized and unrealized gains and losses on investments) for the Museum's ownership share of the Company or charitable perpetual trusts and related changes for the Trust's ownership share in the Company. The Museum has not reported noncontrolling interest for the Trust's ownership share in the Company, as the Museum continues to be the sole beneficiary of the Trust.

At June 30, 2015, the total net assets of the Company were \$572,247. Based on the Museum's ownership percentage at June 30, 2015, of 76.80%, the Museum's share of the net assets amounted to \$439,458 and are included in endowment investments in the Museum's statement of financial position. The Trust's share of the Company's net assets of \$132,789 at June 30, 2015, are included in charitable perpetual trusts in the Museum's statement of financial position. At June 30, 2014, the total net assets of the Company were \$581,938. Based on the Museum's ownership percentage at June 30, 2014, of 76.42%, the Museum's share of the net assets amounted to \$444,739 and are included in endowment investments in the Museum's statement of financial position. The Trust's share of the Company's net assets of \$137,199 at June 30, 2014, are included in charitable perpetual trusts in the Museum's statement of financial position.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **9. Endowment (continued)**

The Museum endowment consists of approximately 340 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

### **Interpretation of Relevant Law**

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

- The duration and preservation of the fund
- The purposes of the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Museum
- The investment policies of the Museum

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **9. Endowment (continued)**

#### **Return Objectives and Risk Parameters**

The Museum has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Museum must hold in perpetuity or for a donor-specific period(s) as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce a real return, net of inflation and investment management costs, of at least 7% over the long term. Actual returns in any given year may vary from this amount.

#### **Strategies Employed for Achieving Objectives**

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

#### **Spending Policy and How the Investment Objectives Relate to Spending Policy**

The Museum uses the spending rule concept in making distributions from its investments. In doing so, the Museum takes into account the distributions from the charitable perpetual trusts. The amount of investment income used by the Museum for its operations and purchases of art is calculated using a spending rate of between 4.5% to 5.5% of the market value of the investments for the prior 20-quarter average ended March 31, 2013 and 2012, for the fiscal years ended June 30, 2015 and 2014, as adjusted (subject to certain limitations) for inflation and additional contributions. For fiscal 2015 and 2014, the calculations resulted in an annual spending rate of approximately 5.0%. Investment returns in excess of (less than) amounts designated for current operations are classified as other changes in net assets in the statements of activities. Accordingly, over the long-term, the Museum expects the current spending policy to allow its endowment to grow at an average of 1.5% to 2.5% annually. This is consistent with the Museum's objective to maintain the purchasing power of the endowment assets held in perpetuity.

The Cleveland Museum of Art

Notes to Financial Statements (continued)  
(In Thousands, Unless Noted)

**9. Endowment (continued)**

**Endowment Net Asset Composition by Type of Fund at June 30**

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
<b>2015</b>				
Donor restricted	\$ –	\$ 254,980	\$ 81,243	\$ 336,223
Charitable perpetual trusts	–	–	315,215	315,215
Board-designated	<b>107,877</b>	–	–	<b>107,877</b>
Total endowment	<b>\$ 107,877</b>	<b>\$ 254,980</b>	<b>\$ 396,458</b>	<b>\$ 759,315</b>
<b>2014</b>				
Donor restricted	\$ –	\$ 260,312	\$ 79,664	\$ 339,976
Charitable perpetual trusts	–	–	323,061	323,061
Board-designated	109,857	–	–	109,857
Total endowment	<b>\$ 109,857</b>	<b>\$ 260,312</b>	<b>\$ 402,725</b>	<b>\$ 772,894</b>

Changes in endowment net assets for the fiscal year ended June 30, 2015, consisted of the following:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Endowment net assets, beginning of year	\$ 109,857	\$ 260,312	\$ 402,725	\$ 772,894
Investment return:				
Investment income	905	5,047	–	5,952
Net appreciation (realized and unrealized)	979	5,334	(7,846)	(1,533)
Total investment income	<b>1,884</b>	<b>10,381</b>	<b>(7,846)</b>	<b>4,419</b>
Contributions	308	231	1,579	2,118
Appropriation of endowment assets for expenditure	(4,172)	(15,944)	–	(20,116)
Endowment net assets, end of year	<b>\$ 107,877</b>	<b>\$ 254,980</b>	<b>\$ 396,458</b>	<b>\$ 759,315</b>

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**9. Endowment (continued)**

Changes in endowment net assets for the fiscal year ended June 30, 2014, consisted of the following:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Endowment net assets, beginning of year	\$ 104,936	\$ 227,921	\$ 363,255	\$ 696,112
Investment return:				
Investment income	857	4,704	–	5,561
Net appreciation (realized and unrealized)	8,396	45,056	30,105	83,557
Total investment income	9,253	49,760	30,105	89,118
Contributions	16	94	9,365	9,475
Appropriation of endowment assets for expenditure	(4,348)	(17,463)	–	(21,811)
Endowment net assets, end of year	<u>\$ 109,857</u>	<u>\$ 260,312</u>	<u>\$ 402,725</u>	<u>\$ 772,894</u>

**Funds With Deficiencies**

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Museum to retain as a fund of perpetual duration. These deficiencies result from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the Museum. There were eight endowment funds considered deficient as of June 30, 2015, with deficiencies totaling approximately \$0.1 million.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **10. Benefit Plans**

The Museum converted from a contributory defined benefit pension plan for eligible employees to a noncontributory defined benefit pension plan (the Pension Plan) on January 1, 2002. Eligible participants in the contributory defined benefit pension plan on December 31, 2001, were given the option of continuing to contribute to this plan until July 1, 2009. For those employees not making this election, their accumulated benefit was converted to the noncontributory defined benefit pension plan. For either contributing or noncontributing participants, benefits under the Pension Plan are based on years of service and the final five-year average compensation. It is the policy of the Museum to fund with an insurance company at least the minimum amounts required by the Employee Retirement Income Security Act of 1974. Pension Plan assets are invested in group annuity contracts.

Effective July 1, 2009, the Museum modified the Pension Plan, eliminating the contributory portion of the plan, and the benefit calculation is based on career years of service. Effective December 31, 2010, the Museum modified the Pension Plan to allow participants meeting certain eligibility requirements to elect to accrue additional benefits in the current defined benefit plan. Those participants not meeting the eligibility requirements cease to accrue additional benefits under the plan. For those participants not meeting eligibility requirements or who elected not to accrue additional benefits in the defined benefit plan, the Museum provides an enhanced contribution to the participant's 401(k) account for employees meeting defined eligibility requirements.

The Museum provides health care benefits upon retirement to certain employees meeting eligibility requirements as of December 31, 2001, and contractually required additions. No other employees are eligible to receive these postretirement health care benefits. The Museum's policy is to fund the annual costs of these benefits from unrestricted net assets of the Museum.

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**10. Benefit Plans (continued)**

Included in unrestricted net assets at June 30, 2015 and 2014, are the following amounts that have not yet been recognized in net periodic benefit cost:

	<b>Pension Plan</b>		<b>Other Postretirement</b>	
	<b>2015</b>	<b>2014</b>	<b>2015</b>	<b>2014</b>
Actuarial loss (gain)	\$ 12,315	\$ 9,878	\$ (1,510)	\$ (1,716)
Net prior service (credit)	(453)	(511)	(406)	(602)
Total unrecognized amounts included in unrestricted net assets	<b>\$ 11,862</b>	<b>\$ 9,367</b>	<b>\$ (1,916)</b>	<b>\$ (2,318)</b>

The actuarial loss and prior service (credit) for the Pension Plan that will be amortized from unrestricted net assets into periodic benefit cost over the next fiscal year are \$850 and \$(58), respectively. There are no actuarial gains and prior service (credits) for the postretirement medical plan that will be amortized from unrestricted net assets into periodic benefit cost over the next fiscal year.

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**10. Benefit Plans (continued)**

The following table sets forth the actuarial present value of benefit obligations and aggregate funded status of the Pension Plan:

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
Change in benefit obligation:		
Benefit obligation at beginning of fiscal year	\$ 34,863	\$ 32,202
Service cost	500	408
Interest cost	1,362	1,411
Actuarial losses	1,220	2,220
Benefits paid	(1,501)	(1,378)
Benefit obligation at end of fiscal year	<u>36,444</u>	<u>34,863</u>
Change in plan assets:		
Fair value of plan assets at beginning of fiscal year	27,367	26,614
Actual return on plan assets	(278)	1,366
Employer contributions	649	765
Benefits paid	(1,501)	(1,378)
Fair value of plan assets at end of fiscal year	<u>26,237</u>	<u>27,367</u>
Underfunded status of the plan and accrued pension obligation	<u>\$ (10,207)</u>	<u>\$ (7,496)</u>
Accumulated benefit obligation	<u>\$ 36,229</u>	<u>\$ 34,676</u>



The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**10. Benefit Plans (continued)**

Weighted-average assumptions for the Pension Plan are as follows:

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
Discount rate – liability	<b>4.15%</b>	4.00%
Discount rate – cost	<b>4.00</b>	4.50
Expected rate of return on plan assets	<b>5.25</b>	5.75
Compensation growth rate – liability	<b>3.00</b>	3.00
Compensation growth rate – cost	<b>3.00</b>	3.00

The assumptions used in the actuarial valuations were established by the Museum in conjunction with its actuary. The expected long-term rate of return on plan assets was established using the Museum’s target asset allocation for equity and fixed income securities and the historical average rates of return for equity and fixed income securities adjusted by an assessment of possible future influences that could cause the returns to trail long-term patterns. The weighted-average rates of increase in compensation were established based upon the Museum’s long-term internal compensation plans.

	<b>Year Ended June 30</b>	
	<b>2015</b>	<b>2014</b>
Components of net periodic benefit cost recognized in the statements of activities:		
Service cost	\$ <b>500</b>	\$ 408
Interest cost	<b>1,362</b>	1,411
Expected return on plan assets	<b>(1,549)</b>	(1,444)
Amortization of prior service cost	<b>(58)</b>	(58)
Recognized net actuarial loss	<b>610</b>	449
	<b>\$ 865</b>	\$ 766

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**10. Benefit Plans (continued)**

The Pension Plan invests in an unallocated immediate participation guarantee group annuity contract with John Hancock Life Insurance Company (the Insurer), which is considered a Level 3 investment in the fair value hierarchy. The investment balances and related investment results are based on information provided by the Insurer, which considers significant inputs for the unallocated insurance contract, including specific terms and contractual provisions outlined in the contract, such as the effective interest rate. The Insurer credits the Pension Plan's deposits that are intended to provide future benefits to present employees to an account that is invested with other assets of the Insurer. The account is credited with its share of the Insurer's actual investment income. The investment in the group annuity contract is designed to grow at a rate consistent with the underlying obligation. The actual asset allocations by asset category are consistent with its targets and are as follows:

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
Debt securities	<b>95%</b>	87%
Equity securities	<b>1</b>	1
Other	<b>4</b>	12
Total	<b>100%</b>	100%

The Museum expects to make a contribution of \$1,375 to the Pension Plan in fiscal year 2016. The Museum reserves the right to contribute more or less than this amount but not less than any minimum contribution requirement under the Pension Protection Act (PPA). Benefit payments over the next five fiscal years are estimated as follows:

Years ending:	
2016	\$ 1,774
2017	1,832
2018	1,884
2019	1,955
2020	2,040
Five years thereafter	10,982

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**10. Benefit Plans (continued)**

In addition, the Museum sponsors a 401(k) savings plan. The Museum matches employee contributions at a rate of 50% of the first 4% of total compensation. The Museum's contributions to the 401(k) plan were \$288 and \$236 for the years ended June 30, 2015 and 2014, respectively.

The following information is provided for the Museum's postretirement medical benefits plan:

	<b>June 30</b>	
	<b>2015</b>	<b>2014</b>
Change in benefit obligation:		
Benefit obligation at beginning of fiscal year	\$ 772	\$ 890
Interest cost	26	33
Actuarial gain	16	(97)
Benefits paid	(120)	(124)
Participant contributions	61	70
Benefit obligation at end of fiscal year	<u>755</u>	<u>772</u>
Change in plan assets:		
Fair value of plan assets at beginning of fiscal year	-	-
Participant contributions	61	70
Employer contributions	59	54
Benefits paid	(120)	(124)
Fair value of plan assets at end of fiscal year	<u>-</u>	<u>-</u>
Underfunded status of the plan and accrued postretirement medical benefits	<u>\$ (755)</u>	<u>\$ (772)</u>

Approximately \$(56) and \$(61) of the accrued postretirement medical benefit liability is included in accounts payable and accrued expenses on the statements of financial position as of June 30, 2015 and 2014, respectively.

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

**10. Benefit Plans (continued)**

The discount rate used in determining the accumulated postretirement benefit obligation at June 30, 2015 and 2014, was 3.6% and 3.45%, respectively. The discount rate used in determining the net periodic benefit cost was 3.45% and 3.85% at June 30, 2015 and 2014, respectively. The health care cost trend rate used is 9.00% for fiscal year 2015, declining to 5.50% by 2022. A one-percentage-point increase or decrease in the health care cost trend would have increased or decreased the fiscal 2015 and 2014 interest costs in total by \$2 and \$2, respectively, and would have increased or decreased the accumulated postretirement benefit obligation by \$73 and \$50, respectively.

	<b>Year Ended June 30</b>	
	<b>2015</b>	<b>2014</b>
Components of net periodic benefit credit recognized in the statements of activities:		
Interest cost	\$ 25	\$ 33
Amortization of prior service credit	(196)	(196)
Recognized net actuarial gain	(190)	(191)
	<u>\$ (361)</u>	<u>\$ (354)</u>

The benefits expected to be paid in each year for the fiscal years 2016–2020 are \$56, \$59, \$61, \$62, and \$62, respectively. The anticipated benefits to be paid in the five years from 2021 to 2025 are \$289.

**11. Financing Arrangements and Long-Term Obligations**

**Operating Leases**

The Museum has an operating lease for warehouse space that can be terminated at its discretion. Total rental expense for the years ended June 30, 2015 and 2014, was \$103 and \$124, respectively.

The Cleveland Museum of Art

Notes to Financial Statements (continued)  
*(In Thousands, Unless Noted)*

**11. Financing Arrangements and Long-Term Obligations (continued)**

**Cultural Facility Revenue Bonds**

Cultural Facility Revenue Bonds consist of the following:

	Interest Rates	Final Fiscal Year Maturity	Amount Outstanding at June 30	
			2015	2014
Series 2005	Variable rate	2037–2041	\$ 90,000	\$ 90,000
Series 2010	3% to 5%	2019–2023	70,430	70,430
			<b>160,430</b>	160,430
Unamortized premium			3,043	3,567
Current portion			–	–
			<b>\$ 163,473</b>	\$ 163,997

**Series 2005**

In October 2005, pursuant to certain agreements between the Museum and the Cleveland-Cuyahoga Port Authority, the Cleveland-Cuyahoga Port Authority issued \$90,000 in variable rate, tax-exempt Cultural Facility Revenue Bonds (The Cleveland Museum of Art Project), Series 2005, payable October 1, 2040 (the 2005 Bonds). The proceeds of the 2005 Bonds were used to finance the Museum’s construction, renovation, and expansion project. The 2005 Bonds were issued in four series: (i) the Series A Bonds in the principal amount of \$30,000, (ii) the Series B Bonds in the principal amount of \$20,000, (iii) the Series C Bonds in the principal amount of \$20,000, and (iv) the Series D Bonds in the principal amount of \$20,000. The 2005 Bonds have adjustable methods of interest rate determination and interest payment dates, and were in weekly variable rate mode based on a tax-free LIBOR on June 30, 2015, bearing interest at .07% and .09% (range from .02% to .13% during the year ended June 30, 2015), and on June 30, 2014, bearing interest at 0.05% and 0.06% (range from 0.03% to 0.12% during the year ended June 30, 2014). The interest rate is determined by an external agent.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **11. Financing Arrangements and Long-Term Obligations (continued)**

The 2005 Bonds are secured by a standby bond purchase agreement, with an expiration date of December 31, 2017. Under the terms of this agreement, in the event of a failed remarketing, the bank will provide liquidity to make payment to the bond holders. Fees incurred related to the remarketing of the bonds were \$445 and \$449 during the years ended June 30, 2015 and 2014, respectively, and are included in general and administrative expense in the statements of activities.

#### **Series 2010**

On July 1, 2010, pursuant to certain agreements between the Museum and the Cleveland-Cuyahoga Port Authority, the Cleveland-Cuyahoga Port Authority issued \$70,430 in fixed rate, tax-exempt Cultural Facility Revenue Bonds, Series 2010 (The Cleveland Museum of Art Project). The proceeds of the 2010 Bonds are being used to finance the Museum's ongoing construction project. The 2010 Bonds were issued at a premium with varying maturity dates ranging from October 2018 to 2022 and with coupon rates ranging from 3.00% to 5.00%.

While these Cultural Facility Revenue Bonds are not a direct indebtedness of the Museum, the loan agreement with the Cleveland-Cuyahoga Port Authority obligates the Museum to make payments equal to the principal of and premium, if any, and interest on the respective Bonds, whether at maturity, upon acceleration or upon redemption. Bond service charges due on the Bonds will be required to be made by the Museum as loan payments under the agreement. Interest-only payments are required to be made until October 1, 2036, for the Series 2005 Bonds and October 1, 2018, for the Series 2010 Bonds.

The Museum is subject to certain restrictive covenants, including provisions relating to maintaining certain debt ratios and other matters. The Museum was in compliance with these covenants at June 30, 2015.

#### **Unamortized Financing Costs**

Unamortized financing costs are amortized over the period the obligation is outstanding using the effective interest method. Included in general and administrative expense on the statements of activities was \$126 of amortization of deferred financing costs during each of the years ended June 30, 2015 and 2014. Unamortized financing costs of \$1,105 and \$1,231 are included in other long-term assets on the statements of financial position at June 30, 2015 and 2014, respectively.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **11. Financing Arrangements and Long-Term Obligations (continued)**

#### **Interest Rate Swap**

In connection with the 2005 Bonds, the Museum entered into a floating-to-fixed rate swap to manage the risk of increased debt service costs resulting from rising variable interest rates. The swap consists of a \$90,000, eight-year floating-to-fixed rate swap whereby the Museum paid a fixed rate of 3.341% and received 70% of one-month LIBOR. The notional amount of the swap declined each year until its maturity on January 1, 2014. The notional value of the swap was \$0 and \$0 at June 30, 2015 and 2014, respectively. This derivative instrument was not designated as a hedging instrument. At June 30, 2015 and 2014, the fair value of the swap agreement as of the close of business that day, was \$0 and \$0, respectively, owed to the counterparty and is recorded in other liabilities on the statements of financial position. The change in fair value of the swap agreement is recorded in other changes in net assets on the statements of activities. Net interest cost incurred under the swap agreement was \$0 and \$24 for fiscal 2015 and 2014, respectively, and is included in general and administrative expense on the statements of activities.

In December 2009, the Museum entered into a floating-to-fixed rate swap to hedge the unhedged principal amount of the 2005 Bonds, due to the declining notional amount of the previous swap. The effective date of the swap was January 3, 2011, with an initial notional amount of \$63,500, increasing to \$90,000 on January 2, 2014, when the original swap matures. The swap matures on January 1, 2021, and consists of a floating-to-fixed rate swap whereby the Museum pays a fixed rate of 2.8623% and receives 70% of one-month LIBOR. This derivative instrument is not designated as a hedging instrument. At June 30, 2015 and 2014, the fair value of the swap agreement as of the close of business that day, was \$(7,863) and \$(8,264), respectively, owed to the counterparty and has been recorded in other liabilities on the statements of financial position. The change in fair value of the swap agreement is recorded in other changes in net assets on the statements of activities. Net interest cost incurred under the swap agreement was \$2,471 and \$2,448 for fiscal 2015 and 2014, respectively, and is included in general and administrative expense on the statements of activities.

# The Cleveland Museum of Art

## Notes to Financial Statements (continued)

*(In Thousands, Unless Noted)*

### **11. Financing Arrangements and Long-Term Obligations (continued)**

#### **Interest**

Interest expense on the 2005 Bonds was approximately \$43 and \$53 in fiscal years 2015 and 2014, respectively, and is included in general and administrative expense on the statements of activities. Interest expense on the 2010 Bonds was approximately \$3,155 in fiscal 2015 and 2014, and is included in general and administrative expense on the statements of activities. No interest expense was capitalized in fiscal 2015 and 2014. Interest paid on the 2005 and 2010 Bonds was \$3,198 and \$3,208 in fiscal years 2015 and 2014, respectively.

#### **Line of Credit**

The Museum has a line of credit with a financial institution totaling \$20,000. The line is intended to meet the short-term financing needs of the Museum. There were no amounts borrowed on the line of credit during fiscal 2015 or 2014 and no amounts outstanding as of June 30, 2015 or 2014.

### **12. Income Taxes**

The Museum is a nonprofit organization and is exempt from federal income taxes on related income under Section 501(c)(3) of the Internal Revenue Code. There were no amounts recorded for uncertain tax positions as of June 30, 2015 and 2014.

### **13. Subsequent Events**

The Museum has evaluated subsequent events through November 25, 2015, the date the financial statements were issued.



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