

FINANCIAL STATEMENTS

The Cleveland Museum of Art
Years Ended June 30, 2020 and 2019
With Report of Independent Auditors

Ernst & Young LLP



The Cleveland Museum of Art

Financial Statements

Years Ended June 30, 2020 and 2019

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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, 2020 and 2019, 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 at June 30, 2020 and 2019, 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 30, 2020

The Cleveland Museum of Art

Statements of Financial Position

(In Thousands)

| | June 30 | |
|-------------------------------------|----------------------------|----------------------------|
| | 2020 | 2019 |
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 7,449 | \$ 7,630 |
| Investments for current use | 46,255 | 19,845 |
| Accounts receivable | 12 | 205 |
| Inventories | 1,040 | 1,053 |
| Other current assets | 2,434 | 2,627 |
| Total current assets | <u>57,190</u> | <u>31,360</u> |
| Investments: | | |
| Endowment investments | 457,954 | 469,101 |
| Other investments | 5,961 | 41,305 |
| Buildings and equipment: | | |
| Buildings and improvements | 392,216 | 391,966 |
| Equipment | 31,004 | 29,451 |
| Construction-in-progress | 7,913 | 4,521 |
| | <u>431,133</u> | <u>425,938</u> |
| Less accumulated depreciation | 144,905 | 134,289 |
| Total buildings and equipment – net | <u>286,228</u> | <u>291,649</u> |
| Other assets: | | |
| Charitable perpetual trusts | 315,011 | 328,324 |
| Pledges receivable | 12,795 | 16,064 |
| Other | 425 | 425 |
| | <u>328,231</u> | <u>344,813</u> |
| Total assets | <u><u>\$ 1,135,564</u></u> | <u><u>\$ 1,178,228</u></u> |

| | June 30 | |
|---|----------------------------|----------------------------|
| | 2020 | 2019 |
| Liabilities and net assets | | |
| Current liabilities: | | |
| Accounts payable and accrued expenses | \$ 4,632 | \$ 5,112 |
| Deferred revenue | 1,226 | 1,276 |
| Current portion of long-term debt | 42,255 | 14,085 |
| Other current liabilities | 5,872 | 206 |
| Total current liabilities | <u>53,985</u> | <u>20,679</u> |
| Long-term debt | 90,000 | 132,499 |
| Other liabilities: | | |
| Accrued postretirement medical benefits | 376 | 357 |
| Accrued pension obligation | 16,243 | 13,099 |
| Other | 15,331 | 8,602 |
| | <u>31,950</u> | <u>22,058</u> |
| Total liabilities | <u>175,935</u> | <u>175,236</u> |
| Net assets: | | |
| Without donor restrictions | 269,921 | 292,174 |
| With donor restrictions | 689,708 | 710,818 |
| Total net assets | <u>959,629</u> | <u>1,002,992</u> |
| | | |
| Total liabilities and net assets | <u><u>\$ 1,135,564</u></u> | <u><u>\$ 1,178,228</u></u> |

See accompanying notes.

The Cleveland Museum of Art

Statement of Activities (In Thousands)

Year Ended June 30, 2020

| | Without Donor Restrictions | With Donor Restrictions | Total |
|---|-------------------------------|----------------------------|------------|
| Revenues and support | | | |
| Endowment and trust income | \$ 13,404 | \$ 10,450 | \$ 23,854 |
| Contributions and membership | 7,029 | - | 7,029 |
| Gifts, grants, and other revenue for special exhibitions | 1,407 | - | 1,407 |
| Program revenues and other support | 6,846 | 3,113 | 9,959 |
| Stores, café, parking, and products | 1,720 | - | 1,720 |
| Net assets released from restrictions used for operations | 12,797 | (12,797) | - |
| Total revenues and support | 43,203 | 766 | 43,969 |
| Expenses | | | |
| Curatorial, conservation, and registrar | 11,088 | - | 11,088 |
| Special exhibitions | 2,956 | - | 2,956 |
| Education, library, and community programs | 2,974 | - | 2,974 |
| Marketing and communications | 1,177 | - | 1,177 |
| Development and membership services | 4,542 | - | 4,542 |
| General and administrative | 6,402 | - | 6,402 |
| Building, facilities, and security | 8,245 | - | 8,245 |
| Stores, café, parking, and products | 1,391 | - | 1,391 |
| Depreciation | 2,120 | - | 2,120 |
| Total expenses | 40,895 | - | 40,895 |
| Excess of revenues and support over expenses before other | 2,308 | 766 | 3,074 |
| Other | | | |
| Depreciation on building expansion project | (8,496) | - | (8,496) |
| Interest expense | (4,950) | - | (4,950) |
| Net periodic benefit cost other than service cost | (906) | - | (906) |
| Trust revenue designated for art purchases | - | 5,670 | 5,670 |
| Investment return designated for art purchase | - | 5,680 | 5,680 |
| Net assets released from restrictions used to fund debt service of building project | 4,350 | (4,350) | - |
| Net assets released from restrictions used to fund acquisition of art objects | 7,792 | (7,792) | - |
| Expenditures for acquisition of art objects | (8,531) | - | (8,531) |
| Gifts and contributions | - | 5,027 | 5,027 |
| Investment return after amounts designated | (2,788) | (12,798) | (15,586) |
| Change in fair value of derivative instruments | (7,694) | - | (7,694) |
| Change in fair value of charitable perpetual trusts | - | (13,313) | (13,313) |
| Changes in funded status of pension benefits | (3,144) | - | (3,144) |
| Changes in funded status of postretirement medical benefits | (194) | - | (194) |
| Decrease in net assets | (22,253) | (21,110) | (43,363) |
| Net assets at beginning of year | 292,174 | 710,818 | 1,002,992 |
| Net assets at end of year | \$ 269,921 | \$ 689,708 | \$ 959,629 |

See accompanying notes.

The Cleveland Museum of Art

Statement of Activities (In Thousands)

Year Ended June 30, 2019

| | Without Donor Restrictions | With Donor Restrictions | Total |
|---|-------------------------------|----------------------------|--------------|
| Revenues and support | | | |
| Endowment and trust income | \$ 12,249 | \$ 9,139 | \$ 21,388 |
| Contributions and membership | 7,101 | – | 7,101 |
| Gifts, grants, and other revenue for special exhibitions | 3,912 | 131 | 4,043 |
| Program revenues and other support | 7,612 | 3,123 | 10,735 |
| Stores, café, parking, and products | 3,311 | – | 3,311 |
| Net assets released from restrictions used for operations | 11,497 | (11,497) | – |
| Total revenues and support | 45,682 | 896 | 46,578 |
| Expenses | | | |
| Curatorial, conservation, and registrar | 10,472 | – | 10,472 |
| Special exhibitions | 5,171 | – | 5,171 |
| Education, library, and community programs | 2,869 | – | 2,869 |
| Marketing and communications | 1,207 | – | 1,207 |
| Development and membership services | 4,567 | – | 4,567 |
| General and administrative | 7,934 | – | 7,934 |
| Building, facilities, and security | 8,229 | – | 8,229 |
| Stores, café, parking, and products | 2,079 | – | 2,079 |
| Depreciation | 2,076 | – | 2,076 |
| Total expenses | 44,604 | – | 44,604 |
| Excess of revenues and support over expenses before other | 1,078 | 896 | 1,974 |
| Other | | | |
| Depreciation on building expansion project | (8,505) | – | (8,505) |
| Interest expense | (5,315) | – | (5,315) |
| Net periodic benefit cost other than service cost | (1,037) | – | (1,037) |
| Trust revenue designated for art purchases | – | 5,627 | 5,627 |
| Investment return designated for art purchase | – | 9,458 | 9,458 |
| Net assets released from restrictions used to fund debt service of building project | 6,350 | (6,350) | – |
| Net assets released from restrictions used to fund acquisition of art objects | 11,279 | (11,279) | – |
| Expenditures for acquisition of art objects | (11,500) | – | (11,500) |
| Gifts and contributions | 286 | 6,235 | 6,521 |
| Investment return after amounts designated | 470 | 483 | 953 |
| Change in fair value of derivative instruments | (4,338) | – | (4,338) |
| Change in fair value of charitable perpetual trusts | – | (886) | (886) |
| Changes in funded status of pension benefits | (1,583) | – | (1,583) |
| Changes in funded status of postretirement medical benefits | (48) | – | (48) |
| (Decrease) increase in net assets | (12,863) | 4,184 | (8,679) |
| Net assets at beginning of year | 305,037 | 706,634 | 1,011,671 |
| Net assets at end of year | \$ 292,174 | \$ 710,818 | \$ 1,002,992 |

See accompanying notes.

The Cleveland Museum of Art

Statements of Cash Flows (In Thousands)

| | Year Ended June 30 | |
|---|---------------------------|-----------------|
| | 2020 | 2019 |
| Operating activities | | |
| Decrease in net assets | \$ (43,363) | \$ (8,679) |
| Adjustments to reconcile decrease in net assets to cash provided by operating activities: | | |
| Depreciation | 10,616 | 10,581 |
| Net accretion of bond premiums and financing costs | (244) | (386) |
| Change in fair value of derivative instruments | 7,694 | 4,338 |
| Net realized and unrealized losses (gains) on long-term investments | 2,121 | (18,227) |
| Contributions restricted for long-term purposes | (1,150) | (3,685) |
| Decrease in fair value of charitable perpetual trusts | 13,313 | 886 |
| Acquisition of art objects, net | 8,504 | 11,500 |
| Changes in funded status of pension and postretirement medical benefits | 3,338 | 1,631 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 193 | 7 |
| Inventories and other current assets | 206 | 60 |
| Pledges receivable | 3,269 | 1,892 |
| Accounts payable and accrued expenses | (492) | 341 |
| Deferred revenue | (50) | 89 |
| Other current liabilities | 21 | (7) |
| Other liabilities | 331 | 104 |
| Net cash provided by operating activities | <u>4,307</u> | <u>445</u> |
| Financing activities | | |
| Repayment of debt | (14,085) | (14,090) |
| Contributions restricted for long-term purposes | 1,150 | 3,685 |
| Proceeds from forgivable PPP loan | 4,174 | - |
| Net cash used in financing activities | <u>(8,761)</u> | <u>(10,405)</u> |
| Investing activities | | |
| Purchases of buildings and equipment | (5,195) | (2,469) |
| Acquisition of art objects | (8,519) | (10,984) |
| Proceeds from the deaccession of art | 27 | - |
| Proceeds from sales and maturities of investments | 126,919 | 49,856 |
| Purchases of investments | (108,959) | (25,177) |
| Net cash provided by investing activities | <u>4,273</u> | <u>11,226</u> |
| Net (decrease) increase in cash and cash equivalents | (181) | 1,266 |
| Cash and cash equivalents at beginning of year | 7,630 | 6,364 |
| Cash and cash equivalents at end of year | <u>\$ 7,449</u> | <u>\$ 7,630</u> |

See accompanying notes.

The Cleveland Museum of Art

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

June 30, 2020 and 2019

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

Novel Coronavirus Disease 2019 Pandemic

In March 2020, the World Health Organization designated the novel coronavirus disease 2019 (COVID-19) outbreak as a global pandemic. The Museum experienced and responded to significant operational challenges related to the COVID-19 pandemic during the last two quarters of the fiscal year ended June 30, 2020. In response to the COVID-19 pandemic, the Museum took steps to provide near-term financial stability and operational flexibility. On April 13, 2020, the Museum received loan proceeds in the amount of \$4,174 under the Paycheck Protection Program (PPP). The PPP, established as part of the Coronavirus Aid, Relief and Economic Security Act (CARES Act), was implemented by the Small Business Administration, with support from the U.S. Department of the Treasury. The Museum applied debt accounting guidance and has reflected the proceeds in other current liabilities at June 30, 2020. The loan forgiveness requirements have certain terms and conditions, including retaining employees and payroll at certain specified levels during a stated period. The amount of loan forgiveness can be up to the full amount of principal and any accrued interest. Subsequent to year end, the Museum intends to seek loan forgiveness by submitting requests to its lender with documentation of employee headcounts and payment of eligible expenses. When the Museum is legally released from being the primary obligor, the forgivable loan will be recognized as an extinguishment of debt in the statement of activities. The Museum will continue to monitor compliance with the terms and conditions of the PPP. If it is determined that the Museum is unable to comply with current or future terms and conditions, the Museum will repay the unforgiven balance. While the unforgiven portion of the loan is payable over two years at an interest rate of 1%, the Museum expects to pay off any portion not forgiven by June 30, 2021.

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.

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

2. Significant Accounting Policies (continued)

Net Assets

Generally accepted accounting principles require that resources be classified for reporting purposes into two categories based upon the presence or absence of donor restrictions – with donor restrictions or without donor restrictions. Net assets without donor restrictions represent resources available for the general support of the Museum’s activities and may be designated by the Museum’s Board of Trustees for specific purposes. Net assets with donor restrictions are those whose use has been limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled by actions of the Museum and donor-restricted endowment funds. As restrictions expire, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statements of activities as net assets released from restrictions.

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 with donor restrictions. The Museum records its interest in charitable perpetual trusts at its pro rata share of the fair value of the underlying assets. Income distributed to the Museum by the trusts of \$14,410 and \$14,539 in fiscal 2020 and 2019, respectively, is included in endowment and trust income and trust revenue designated for art purchase 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 completed by the Museum in 2014. The total appropriated is not to exceed \$75,000. During fiscal 2020 and 2019, the Museum appropriated \$4,350 and \$6,350, respectively, for said purpose from the 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.

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

2. Significant Accounting Policies (continued)

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 net assets with donor restrictions 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 \$12 and \$516 for the years ended June 30, 2020 and 2019, 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.

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.

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 cost 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 based upon the absence or presence of a restriction on the underlying asset (Note 7).

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. Contributions and pledges received with donor restrictions that limit use are reported as with donor restricted contributions and membership, or other 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, net assets with donor restrictions are reclassified to net assets without donor restrictions 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.

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 in net assets in the period of change.

The Cleveland Museum of Art

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

2. Significant Accounting Policies (continued)

Accounting Pronouncements Adopted

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-02, *Leases*. This ASU requires lessees to recognize assets and liabilities on the statement of financial position for leases with lease terms greater than twelve months. The recognition, measurement and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a finance or operating lease. This amends current guidance that requires only capital leases to be recognized on the lessee's statement of financial position. The Museum adopted ASU 2016-02 on July 1, 2019 using a modified retrospective approach. The Museum also elected the package of practical expedients permitted under the new standard that allowed the Museum to carry forward historical lease classification. The Museum's operating leases are all short-term (less than twelve months), so the Museum was not required to record a right of use asset or liability upon adoption of ASU 2016-02. The adoption of ASU 2016-02 also did not impact total revenues and support, excess of revenues and support over expenses before other, or total net assets.

In November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows*. This ASU requires entities to show the changes in the total of cash, cash equivalents, and restricted cash on the statement of cash flows and reconcile those amounts to the statement of financial position. The Museum adopted ASU 2016-18 on June 30, 2020 and applied the provisions retrospectively to all periods presented in the financial statements. The adoption of ASU 2016-18 had no impact on total revenues and support, excess of revenues and support over expenses before other, or total net assets.

In March 2017, the FASB issued ASU 2017-07, *Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. This ASU requires the service cost component of net periodic benefit cost related to defined benefit pension and postretirement benefit plans to be reported in the same financial statement line as other compensation costs arising from services rendered during the period. The other components of net periodic benefit cost are required to be presented separately from service costs and outside of operating income in the statement of activities. Only the service cost component of net periodic benefit cost will be eligible for capitalization in assets. The Museum adopted ASU 2017-07 on July 1, 2019 and applied it retrospectively to all periods presented in the financial statements. The adoption and retrospective application of ASU 2016-02 had no impact on the increase (decrease) in net assets on the statement of activities or on total net assets.

The Cleveland Museum of Art

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

2. Significant Accounting Policies (continued)

Accounting Pronouncements Not Yet Adopted

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement*. This ASU eliminates the requirement for entities to disclose the amount of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy. It also modifies certain disclosure requirements for nonpublic entities to make them less burdensome. ASU 2018-13 is effective for all entities for annual reporting periods beginning after December 15, 2019. The Museum is currently evaluating the impact that ASU 2018-13 will have on its financial statements and will adopt the provisions upon the effective date.

In March 2019, the FASB issued ASU 2019-03, *Not-for-Profit Entities (Topic 958): Updating the Definition of Collections*. This ASU improves the definition of collections by realigning it with the definition in the American Alliance of Museums' *Code of Ethics for Museums*. It also requires the collection-holding entity to disclose its policy for the use of proceeds from when collection items are deaccessioned. ASU 2019-03 is effective for all entities for annual reporting periods beginning after December 15, 2019. The Museum is currently evaluating the impact that ASU 2019-03 will have on its financial statements and will adopt the provisions upon the effective date.

3. Pledges Receivable

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

| | June 30 | |
|--|------------------|------------------|
| | 2020 | 2019 |
| Pledges due: | | |
| In less than one year | \$ 863 | \$ 2,523 |
| In one to five years | 5,936 | 6,813 |
| Greater than five years | 9,500 | 10,450 |
| | <u>16,299</u> | <u>19,786</u> |
| Present value discount on pledges (1.60%–2.20% discount rate) | <u>(3,504)</u> | <u>(3,722)</u> |
| | <u>\$ 12,795</u> | <u>\$ 16,064</u> |

The Cleveland Museum of Art

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

4. Net Assets With Donor Restrictions

Net assets with donor restrictions are available for the following purposes:

| | June 30 | |
|---|-------------------|-------------------|
| | 2020 | 2019 |
| Acquisition of art | \$ 314,597 | \$ 326,176 |
| Specific operating activities: | | |
| Curatorial and conservation | 35,894 | 35,814 |
| Education, library, and community programs | 26,110 | 22,948 |
| Buildings, grounds, and protection services | 7,390 | 6,984 |
| General operating and other | 305,717 | 318,896 |
| Total net assets with donor restrictions | <u>\$ 689,708</u> | <u>\$ 710,818</u> |

5. Net Assets Released From Restrictions

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

| | Year Ended June 30 | |
|---|---------------------------|------------------|
| | 2020 | 2019 |
| Acquisition of art | <u>\$ 7,792</u> | <u>\$ 11,279</u> |
| Debt service on building project | <u>\$ 4,350</u> | <u>\$ 6,350</u> |
| Specific operating activities: | | |
| Curatorial and conservation | 1,332 | 1,376 |
| Education, library, and community programs | 1,091 | 1,071 |
| Buildings, grounds, and protection services | 8,569 | 7,909 |
| General operating and other | 1,805 | 1,141 |
| Net assets released from restrictions used for operations | <u>\$ 12,797</u> | <u>\$ 11,497</u> |

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

6. 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)

6. Fair Value Measurements (continued)

The following table presents the financial instruments carried at fair value at June 30, 2020, by the ASC 820 valuation hierarchy defined above:

| | Total | Level 1 | Level 2 | Level 3 |
|-----------------------------------|-------------------|-------------------|------------------|-------------------|
| Assets | | | | |
| Investments for current use: | | | | |
| Money market funds | \$ 11,293 | \$ 11,293 | \$ – | \$ – |
| Corporate bonds | 34,962 | – | 34,962 | – |
| Total investments for current use | 46,255 | 11,293 | 34,962 | – |
| Endowment investments: | | | | |
| Money market funds | 19,272 | 19,272 | – | – |
| Equities: | | | | |
| Common stocks, primarily U.S. | 27,997 | 27,997 | – | – |
| Collective equity funds | 118,167 | – | – | – |
| Equity mutual funds | 137,610 | 137,610 | – | – |
| Fixed income mutual fund | 9,966 | 9,966 | – | – |
| American depository receipts | 5,951 | 5,951 | – | – |
| Fixed income securities: | | | | |
| Corporate bonds | 28,578 | – | 28,578 | – |
| Asset-backed securities | 3,791 | – | 3,791 | – |
| Mortgage-backed securities | 7,165 | – | 7,165 | – |
| Government bonds | 1,483 | – | 1,483 | – |
| Alternative investments: | | | | |
| Absolute return | 19,367 | – | – | – |
| Private equity | 58,149 | – | – | – |
| Hedged equity | 20,458 | – | – | – |
| Total endowment investments | 457,954 | 200,796 | 41,017 | – |
| Other investments: | | | | |
| Corporate bonds | 5,961 | – | 5,961 | – |
| Total other investments | 5,961 | – | 5,961 | – |
| Charitable perpetual trusts | 315,011 | – | – | 315,011 |
| Total assets at fair value | <u>\$ 825,181</u> | <u>\$ 212,089</u> | <u>\$ 81,940</u> | <u>\$ 315,011</u> |
| Liabilities | | | | |
| Interest rate swap | | | | |
| Total liabilities at fair value | <u>\$ 14,159</u> | <u>\$ –</u> | <u>\$ 14,159</u> | <u>\$ –</u> |

The Cleveland Museum of Art

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

6. Fair Value Measurements (continued)

The following table presents the financial instruments carried at fair value at June 30, 2019, by the ASC 820 valuation hierarchy defined above:

| | <u>Total</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|-----------------------------------|-------------------|-------------------|------------------|-------------------|
| Assets | | | | |
| Investments for current use: | | | | |
| Money market funds | \$ 13,120 | \$ 13,120 | \$ – | \$ – |
| Corporate bonds | 6,725 | – | 6,725 | – |
| Total investments for current use | 19,845 | 13,120 | 6,725 | – |
| Endowment investments: | | | | |
| Money market funds | 15,081 | 15,081 | – | – |
| Equities: | | | | |
| Common stocks, primarily U.S. | 51,561 | 51,561 | – | – |
| Collective equity funds | 124,009 | – | – | – |
| Equity mutual funds | 121,306 | 121,306 | – | – |
| Fixed income mutual fund | 9,673 | 9,673 | – | – |
| American depository receipts | 5,168 | 5,168 | – | – |
| Real estate investment trust | 714 | 714 | – | – |
| Fixed income securities: | | | | |
| Corporate bonds | 25,159 | – | 25,159 | – |
| Asset-backed securities | 3,465 | – | 3,465 | – |
| Mortgage-backed securities | 7,721 | – | 7,721 | – |
| Government bonds | 7,979 | – | 7,979 | – |
| Alternative investments: | | | | |
| Absolute return | 19,276 | – | – | – |
| Private equity | 58,235 | – | – | – |
| Hedged equity | 19,754 | – | – | – |
| Total endowment investments | 469,101 | 203,503 | 44,324 | – |
| Other investments: | | | | |
| Corporate bonds | 41,305 | – | 41,305 | – |
| Total other investments | 41,305 | – | 41,305 | – |
| Charitable perpetual trusts | 328,324 | – | – | 328,324 |
| Total assets at fair value | <u>\$ 858,575</u> | <u>\$ 216,623</u> | <u>\$ 92,354</u> | <u>\$ 328,324</u> |
| Liabilities | | | | |
| Interest rate swap | | | | |
| Total liabilities at fair value | \$ 6,465 | \$ – | \$ 6,465 | \$ – |
| | <u>\$ 6,465</u> | <u>\$ –</u> | <u>\$ 6,465</u> | <u>\$ –</u> |

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

6. 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.

Equities include investments of publicly traded common stocks of both U.S. and international corporations and mutual funds, 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. These investments are classified as Level 1, because quoted prices in active markets are available.

Collective equity funds include the Museum's interest in non-publicly traded, liquid commingled funds which are recorded at net asset value (NAV). The investment objective for collective equity funds is long-term total return equal to or better than market returns.

Fixed income securities include debt obligations of U.S. corporations, the U.S. government and various agencies, and other fixed income instruments, such as asset-backed and mortgage-backed securities. Because the evaluated prices are based on observable inputs, such as available trade information, spreads, bids and offers, prepayment speeds, U.S. Treasury curves and interest rate movements, securities in this category are generally classified as Level 2.

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 NAV based on the Museum's portion of the underlying trust's net assets. The underlying net assets of the charitable perpetual trusts are composed of cash equivalents, equities, fixed income securities, and alternative investments. Since the Museum has no rights to the underlying investments, the charitable perpetual trusts have been classified as Level 3.

The Cleveland Museum of Art

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

6. Fair Value Measurements (continued)

Alternative investments (principally limited partnership interests in absolute return, private and hedged equity) represent the Museum's ownership interest in the NAV of the respective partnership as a practical expedient. 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 limited partnerships are determined by the general 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, 2020, the Museum is committed to invest an additional \$76,733 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 investment objective for absolute return funds is long-term capital appreciation with less volatile and/or uncorrelated returns. Absolute return funds include investment strategies where a majority of the underlying securities may or may not be traded on public exchanges. This asset class includes a variety of active strategies, including arbitrage, event-driven, market neutral, long-short equity and distressed investing.

The investment objective for private equity funds is long-term capital appreciation in excess of what is available in the public markets. Private equity funds generally hold illiquid debt and equity securities of public and/or privately held companies. This asset class includes venture capital, secondary, mezzanine, buyout, and distressed funds.

The Cleveland Museum of Art

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

6. Fair Value Measurements (continued)

The investment objective for hedged equity is long-term capital appreciation with low volatility. Hedged equity funds include investment strategies where the majority of the underlying securities are traded on public exchanges. Managers in this asset class may hold long or short equity positions and utilize options, futures, and other derivatives.

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

| | Charitable Perpetual Trusts |
|-----------------------------|--|
| Fair value at July 1, 2018 | \$ 329,210 |
| Net unrealized losses | (886) |
| Fair value at June 30, 2019 | 328,324 |
| Net unrealized losses | (13,313) |
| Fair value at June 30, 2020 | <u>\$ 315,011</u> |

The Cleveland Museum of Art

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

6. Fair Value Measurements (continued)

At June 30, 2020, the Museum's alternative investments within endowment investments are subject to various liquidity restrictions, as follows:

| | |
|--|------------------|
| Available for redemption: | |
| Monthly | \$ 7,668 |
| Quarterly | <u>19,352</u> |
| | 27,020 |
| | |
| Subject to distribution of fund | 58,149 |
| | |
| Subject to remaining lock-up provisions: | |
| One year | 12,789 |
| More than one year | <u>16</u> |
| Total alternatives | <u>\$ 97,974</u> |

Investments that are available for redemption may be redeemed by the Museum generally with a 30-day to 90-day advance notice on a monthly or quarterly basis, subject to the terms of the investment agreement.

Investments subject to distribution cannot be redeemed by the Museum, but rather will be distributed by the investment fund or limited partnership upon the liquidation of the underlying assets of the fund or limited partnership. Distributions are generally expected, but not guaranteed, over the next three to ten years.

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.

The Cleveland Museum of Art

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

6. Fair Value Measurements (continued)

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 \$42,255 and a fair value of \$42,692 at June 30, 2020, and a carrying value of \$56,340 and a fair value of \$59,583 at June 30, 2019. 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 is classified as Level 2 inputs in the fair value hierarchy.

7. Investments and Investment Income

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

| | Without Donor Restrictions | With Donor Restrictions |
|---|---------------------------------------|------------------------------------|
| Year ended June 30, 2020 | | |
| Dividends and interest | \$ 2,120 | \$ 6,093 |
| Realized and unrealized gains, net of realized and unrealized losses | (671) | (2,187) |
| Investment return | 1,449 | 3,906 |
| Investment return designated for current operations (included in endowment and trust income) | (4,237) | (11,024) |
| Investment return designated for art purchase | - | (5,680) |
| Investment return after amounts designated | <u>\$ (2,788)</u> | <u>\$ (12,798)</u> |

The Cleveland Museum of Art

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

7. Investments and Investment Income (continued)

| | Without Donor Restrictions | With Donor Restrictions |
|--|---------------------------------------|------------------------------------|
| Year ended June 30, 2019 | | |
| Dividends and interest | \$ 2,303 | \$ 5,716 |
| Realized and unrealized gains, net of realized and unrealized losses | 2,215 | 14,530 |
| Investment return | 4,518 | 20,246 |
| Investment return designated for current operations (included in endowment and trust income) | (4,048) | (10,305) |
| Investment return designated for art purchase | – | (9,458) |
| Investment return after amounts designated | \$ 470 | \$ 483 |

Investment return is net of investment-related expenses of \$1,910 and \$2,973 for the years ended June 30, 2020 and 2019, respectively. The Museum's investments and charitable perpetual trusts are exposed to various risks, such as interest rate, market, and credit risks.

8. 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 financial statements 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 Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

8. Endowment (continued)

the Trust's ownership share in the Company. The Museum has not reported a 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, 2020, the total net assets of the Company were \$580,343. Based on the Museum's ownership percentage at June 30, 2020 of 76.79%, the Museum's share of the net assets amounted to \$445,654 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 \$134,689 at June 30, 2020 are included in charitable perpetual trusts in the Museum's statement of financial position. At June 30, 2019, the total net assets of the Company were \$597,409. Based on the Museum's ownership percentage at June 30, 2019 of 76.67%, the Museum's share of the net assets amounted to \$458,022 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 \$139,387 at June 30, 2019 are included in charitable perpetual trusts in the Museum's statement of financial position.

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 net assets with donor restrictions (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. Net assets with donor restrictions remain under restriction 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 Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

8. Endowment (continued)

- The duration and preservation of the fund
- The purposes of the donor-restricted endowment fund
- General economic conditions
- The possible effects 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

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.

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.

The Cleveland Museum of Art

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

8. Endowment (continued)

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, 2019 and 2018 for the fiscal years ended June 30, 2020 and 2019, as adjusted (subject to certain limitations) for inflation and additional contributions. For fiscal 2020 and 2019, 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 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.

Endowment Net Asset Composition by Type of Fund at June 30

| | Without Donor Restrictions | With Donor Restrictions | Total |
|-----------------------------|---|------------------------------------|-------------------|
| 2020 | | | |
| Donor-restricted | \$ — | \$ 354,640 | \$ 354,640 |
| Charitable perpetual trusts | — | 315,011 | 315,011 |
| Board-designated | 103,314 | — | 103,314 |
| Total endowment | \$ 103,314 | \$ 669,651 | \$ 772,965 |
| 2019 | | | |
| Donor-restricted | \$ — | \$ 362,043 | \$ 362,043 |
| Charitable perpetual trusts | — | 328,324 | 328,324 |
| Board-designated | 107,058 | — | 107,058 |
| Total endowment | \$ 107,058 | \$ 690,367 | \$ 797,425 |

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

8. Endowment (continued)

Changes in endowment net assets for the fiscal year ended June 30, 2020 consisted of the following:

| | Without Donor Restrictions | With Donor Restrictions | Total |
|--|---|------------------------------------|-------------------|
| Endowment net assets, beginning of year | \$ 107,058 | \$ 690,367 | \$ 797,425 |
| Investment return: | | | |
| Investment income | 779 | 4,504 | 5,283 |
| Net depreciation (realized and unrealized) | (393) | (15,041) | (15,434) |
| Total investment income | 386 | (10,537) | (10,151) |
| Contributions | 107 | 5,763 | 5,870 |
| Appropriation of endowment assets for expenditure | (4,237) | (15,942) | (20,179) |
| Endowment net assets, end of year | <u>\$ 103,314</u> | <u>\$ 669,651</u> | <u>\$ 772,965</u> |

The Cleveland Museum of Art

Notes to Financial Statements (continued)

(In Thousands, Unless Noted)

8. Endowment (continued)

Changes in endowment net assets for the fiscal year ended June 30, 2019 consisted of the following:

| | Without Donor Restrictions | With Donor Restrictions | Total |
|--|---|------------------------------------|-------------------|
| Endowment net assets, beginning of year | \$ 107,933 | \$ 688,909 | \$ 796,842 |
| Investment return: | | | |
| Investment income | 515 | 2,920 | 3,435 |
| Net appreciation (realized and unrealized) | 2,708 | 14,632 | 17,340 |
| Total investment income (loss) | 3,223 | 17,552 | 20,775 |
| Contributions | 50 | 2,678 | 2,728 |
| Appropriation of endowment assets for expenditure | (4,148) | (18,772) | (22,920) |
| Endowment net assets, end of year | <u>\$ 107,058</u> | <u>\$ 690,367</u> | <u>\$ 797,425</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 restricted contributions and continued appropriation for certain programs that was deemed prudent by the Museum. There were twenty-one endowment funds considered deficient as of June 30, 2020, with deficiencies totaling \$359. As of June 30, 2019, there were six endowment funds considered deficient, with deficiencies totaling \$83.

The Cleveland Museum of Art

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

9. 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 Pension Plan. For either contributing or noncontributing participants, benefits under the Pension Plan were 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 Pension 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 ceased to accrue additional benefits under the defined benefit 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)

9. Benefit Plans (continued)

Included in net assets without donor restrictions at June 30, 2020 and 2019 are the following amounts that have not yet been recognized in net periodic benefit cost:

| | Pension Plan | | Other Postretirement | |
|--|---------------------|------------------|-----------------------------|-------------------|
| | 2020 | 2019 | 2020 | 2019 |
| Actuarial loss (gain) | \$ 18,274 | \$ 15,189 | \$ (927) | \$ (1,116) |
| Net prior service credit | (160) | (219) | (34) | (39) |
| Total unrecognized amounts included in net assets without donor restrictions | <u>\$ 18,114</u> | <u>\$ 14,970</u> | <u>\$ (961)</u> | <u>\$ (1,155)</u> |

Changes in plan assets and benefit obligations, recognized in net assets without donor restrictions for the years ended June 30, 2020 and 2019, are as follows:

| | Pension Plan | | Other Postretirement | |
|---|---------------------|-----------------|-----------------------------|--------------|
| | 2020 | 2019 | 2020 | 2019 |
| Net loss (gain) | \$ 4,253 | \$ 2,538 | \$ 46 | \$ (55) |
| Amortization | (1,109) | (955) | 148 | 103 |
| Total recognized amounts in net assets without donor restrictions | <u>\$ 3,144</u> | <u>\$ 1,583</u> | <u>\$ 194</u> | <u>\$ 48</u> |

The estimated net loss and prior service cost for the Pension Plan that will be amortized from net assets without donor restrictions into net periodic benefit cost over the next fiscal year are \$1,450 and \$(58), respectively. The estimated net gain and prior service cost for the other postretirement plan that will be amortized from net assets without donor restrictions into net periodic benefit cost over the next fiscal year are \$(130) and \$(5), respectively.

The Cleveland Museum of Art

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

9. Benefit Plans (continued)

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

| | June 30 | |
|---|--------------------|--------------------|
| | 2020 | 2019 |
| Change in benefit obligation: | | |
| Benefit obligation at beginning of fiscal year | \$ 43,314 | \$ 39,581 |
| Service cost | 414 | 423 |
| Interest cost | 1,418 | 1,584 |
| Actuarial loss | 5,433 | 3,605 |
| Benefits paid | <u>(1,940)</u> | <u>(1,879)</u> |
| Benefit obligation at end of fiscal year | 48,639 | 43,314 |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of fiscal year | 30,215 | 28,065 |
| Actual return on plan assets | 2,664 | 2,446 |
| Employer contributions | 1,457 | 1,583 |
| Benefits paid | <u>(1,940)</u> | <u>(1,879)</u> |
| Fair value of plan assets at end of fiscal year | 32,396 | 30,215 |
| Underfunded status of the plan and accrued pension obligation | <u>\$ (16,243)</u> | <u>\$ (13,099)</u> |
| Accumulated benefit obligation | <u>\$ 48,251</u> | <u>\$ 42,958</u> |

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

| | June 30 | |
|--|----------------|-------------|
| | 2020 | 2019 |
| Discount rate – liability | 2.50% | 3.35% |
| Discount rate – cost | 3.35 | 4.10 |
| Expected rate of return on plan assets | 5.00 | 5.00 |
| Compensation growth rate – liability | 2.78 | 3.00 |
| Compensation growth rate – cost | 3.00 | 3.00 |

The Cleveland Museum of Art

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

9. Benefit Plans (continued)

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.

| | Year Ended June 30 | |
|--|---------------------------|-----------------|
| | 2020 | 2019 |
| Components of net periodic benefit cost recognized in the statements of activities: | | |
| Service cost | \$ 414 | \$ 423 |
| Interest cost | 1,418 | 1,584 |
| Expected return on plan assets | (1,484) | (1,379) |
| Amortization of prior service cost | (58) | (58) |
| Recognized net actuarial loss | 1,167 | 1,013 |
| | <u>\$ 1,457</u> | <u>\$ 1,583</u> |

The service cost component of net periodic benefit cost is included as salaries and benefits in the applicable expense caption on the statements of activities. The components of net periodic benefit cost other than service cost are included in other on the statements of activities.

The Cleveland Museum of Art

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

9. 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:

| | June 30 | |
|-------------------|----------------|-------------|
| | 2020 | 2019 |
| Debt securities | 99% | 99% |
| Equity securities | 1 | 1 |
| Total | 100% | 100% |

The Museum expects to make a contribution of \$1,394 to the Pension Plan in fiscal year 2021. 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 and thereafter are estimated as follows:

| | |
|-----------------------|----------|
| Years ending: | |
| 2021 | \$ 2,121 |
| 2022 | 2,185 |
| 2023 | 2,245 |
| 2024 | 2,322 |
| 2025 | 2,405 |
| Five years thereafter | 12,616 |

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 \$277 and \$260 for the years ended June 30, 2020 and 2019, respectively.

The Cleveland Museum of Art

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

9. Benefit Plans (continued)

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

| | June 30 | |
|--|-----------------|-----------------|
| | 2020 | 2019 |
| Change in benefit obligation: | | |
| Benefit obligation at beginning of fiscal year | \$ 390 | \$ 509 |
| Interest cost | 11 | 18 |
| Actuarial loss (gain) | 46 | (94) |
| Benefits paid | (84) | (87) |
| Participant contributions | 52 | 44 |
| Benefit obligation at end of fiscal year | <u>415</u> | <u>390</u> |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of fiscal year | — | — |
| Participant contributions | 52 | 44 |
| Employer contributions | 32 | 43 |
| Benefits paid | (84) | (87) |
| 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>\$ (415)</u> | <u>\$ (390)</u> |

\$39 and \$33 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, 2020 and 2019, respectively.

The discount rate used in determining the accumulated postretirement benefit obligation at June 30, 2020 and 2019 was 1.85% and 3.00%, respectively. The discount rate used in determining the net periodic benefit cost was 3.00% and 3.85% at June 30, 2020 and 2019, respectively. The health care cost trend rate used is 6.5% for fiscal year 2020, declining to 4.8% by 2024. A one-percentage-point increase in the health care cost trend rate would have increased the fiscal 2020 and 2019 interest costs in total by \$1 and \$2, respectively, and would have increased the accumulated postretirement benefit obligation by \$40 and \$41, respectively. A one-percentage-point decrease in the health care cost trend rate would have decreased the fiscal 2020 and 2019 interest costs in total by \$1 and \$1, respectively, and would have decreased the accumulated postretirement benefit obligation by \$36 and \$38, respectively.

The Cleveland Museum of Art

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

9. Benefit Plans (continued)

| | Year Ended June 30 | |
|---|---------------------------|-----------------|
| | 2020 | 2019 |
| Components of net periodic benefit credit recognized in the statements of activities: | | |
| Interest cost | \$ 11 | \$ 19 |
| Amortization of prior service credit | (5) | — |
| Recognized net actuarial gain | (143) | (142) |
| | <u>\$ (137)</u> | <u>\$ (123)</u> |

The components of net periodic benefit cost (credit) are included in other on the statements of activities.

The benefits expected to be paid in each year for the fiscal years 2021-2025 are \$39, \$39, \$39, \$37, and \$35, respectively. The anticipated benefits to be paid in the five years from 2026 to 2030 are \$142.

10. Financing Arrangements and Long-Term Obligations

Operating Leases

The Museum has a short-term lease for warehouse space that can be terminated at its discretion and is therefore not recorded on the statements of financial position. Total rental expense for the years ended June 30, 2020 and 2019 was \$79.

The Cleveland Museum of Art

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

10. 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 | |
|-----------------------------|----------------|----------------------------|-------------------------------|-------------------|
| | | | 2020 | 2019 |
| Series 2005 | Variable rate | 2037–2041 | \$ 90,000 | \$ 90,000 |
| Series 2010 | 3% to 5% | 2019–2023 | 42,255 | 56,340 |
| | | | 132,255 | 146,340 |
| Unamortized premium | | | 476 | 845 |
| Unamortized financing costs | | | (476) | (601) |
| Current portion | | | (42,255) | (14,085) |
| Long-term debt | | | \$ 90,000 | \$ 132,499 |

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, bearing interest at .13% at June 30, 2020 (range from .10% to 6.9% during the year ended June 30, 2020), and on June 30, 2019, bearing interest at 1.90% (range from 0.93% to 2.37% during the year ended June 30, 2019). The interest rate is determined by an external agent.

The Cleveland Museum of Art

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

10. Financing Arrangements and Long-Term Obligations (continued)

The 2005 Bonds are secured by a standby bond purchase agreement, with an expiration date of January 31, 2024. 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 \$486 and \$473 during the years ended June 30, 2020 and 2019, 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 were used to finance the Museum's construction, renovation, and expansion 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.

Annual maturities of Cultural Facility Revenue Bonds are \$14,085 in 2020, 2021 and 2022. The Bonds maturing in 2021 and 2020 are subject to optional redemption prior to maturity, at the direction of the Museum, on or after October 1, 2020, at a redemption price of 100% of the principal amount redeemed, plus interest accrued to the redemption date. The Museum voluntarily redeemed the Series 2010 Bonds on October 1, 2020. The bonds are presented in the current portion of long-term debt.

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, 2020.

The Cleveland Museum of Art

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

10. Financing Arrangements and Long-Term Obligations (continued)

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 \$125 of amortization of deferred financing costs during each of the years ended June 30, 2020 and 2019.

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 consisted 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.

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 matured. 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, 2020, the fair value of the swap agreement was \$(1,471) owed to the counterparty and has been recorded in other current liabilities on the statements of financial position. At June 30, 2019, the fair value of the swap agreement was \$(2,230) owed to the counterparty and has been recorded in other liabilities on the statement of financial position.

In April 2019, the Museum entered into a floating-to-fixed rate swap to hedge the variable rate bonds. This swap terminates on January 1, 2031 and will replace the swap maturing on January 1, 2021. The Museum pays a fixed rate of 2.041% and receives the weighted average of the weekly USD_SIFMA Municipal Swap Index. This derivative instrument is not designated as a hedging instrument. At June 30, 2020 and 2019, the fair value of the swap agreement was \$(12,688) and \$(4,235), respectively, owed to the counterparty and has been recorded in other liabilities on the statements of financial position.

The Cleveland Museum of Art

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

10. Financing Arrangements and Long-Term Obligations (continued)

The change in fair value of the swap agreement is recorded in other on the statements of activities. Net interest cost incurred under the swap agreement was \$1,571 and \$1,080 for fiscal 2020 and 2019, respectively, and is included in interest expense on the statements of activities.

Interest

Interest expense on the 2005 Bonds was \$1,048 and \$1,402 in fiscal years 2020 and 2019, respectively. Interest expense on the 2010 Bonds was \$2,259 and \$2,870 in fiscal years 2020 and 2019, respectively. Interest paid on the 2005 and 2010 Bonds was \$3,307 and \$4,272 in fiscal years 2020 and 2019, respectively.

Line of Credit

The Museum maintains a line of credit with a financial institution for \$10,000, expiring on February 5, 2021. The balance of the line of credit as of June 30, 2020 and 2019 was zero.

11. Liquidity and Availability of Resources

The Museum's liquidity management policy is to structure its financial assets to be available as its general expenditures, liabilities and other obligations become due.

The Museum's financial assets available within one year for general expenditures are as follows:

| | June 30 | |
|--|------------------|------------------|
| | 2020 | 2019 |
| Cash and cash equivalents | \$ 7,449 | \$ 7,630 |
| Investments for current use | 46,255 | 19,845 |
| Accounts receivable | 12 | 205 |
| Endowment investments | 457,954 | 469,101 |
| Other investments | 5,961 | 41,305 |
| | 517,631 | 538,086 |
| Less amounts unavailable for general expenditures: | | |
| Donor-restricted endowment | (354,640) | (362,043) |
| Board-designated endowment | (103,314) | (107,058) |
| | \$ 59,677 | \$ 68,985 |

The Cleveland Museum of Art

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

11. Liquidity and Availability of Resources (continued)

The Museum's endowment investments consist of donor-restricted and board-designated endowments. Income from the donor-restricted endowment is restricted for specific purposes and, therefore, is not available for general expenditures. As described in Note 8, a portion of endowment investments are available for general expenditures in the next year through the spending policy. In addition, the Museum has the ability to access additional board-designated investments by authorization of the Board of Trustees, if necessary.

12. Functional Expenses

The following table presents expenses by both their nature and their function for the years ended June 30, 2020 and 2019:

| | 2020 | | | |
|--|--------------------|------------------|-----------------------|------------------|
| | Program Expense | Administration | Auxiliary Services | Total |
| Salaries and benefits | \$ 16,467 | \$ 7,214 | \$ 857 | \$ 24,538 |
| Cost of goods sold | 1 | – | 569 | 570 |
| Outside services | 2,889 | 1,424 | 42 | 4,355 |
| Advertising | 526 | – | – | 526 |
| Repairs and maintenance | 188 | 509 | 11 | 708 |
| Supplies and printing | 1,680 | 146 | 46 | 1,872 |
| Utilities | 1,330 | 610 | 59 | 1,999 |
| Professional development | 397 | 427 | 3 | 827 |
| Hospitality | 118 | 343 | 230 | 691 |
| Miscellaneous | 561 | 348 | – | 909 |
| Art transportation, rental fees and insurance | 1,780 | – | – | 1,780 |
| Depreciation | 8,748 | 1,477 | 391 | 10,616 |
| Interest expense | 4,090 | 690 | 170 | 4,950 |
| Net periodic benefit cost other than service cost | 747 | 126 | 33 | 906 |
| | <u>\$ 39,522</u> | <u>\$ 13,314</u> | <u>\$ 2,411</u> | <u>\$ 55,247</u> |

The Cleveland Museum of Art

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

12. Functional Expenses (continued)

| | 2019 | | | |
|--|--------------------|----------------|-----------------------|-----------|
| | Program Expense | Administration | Auxiliary Services | Total |
| Salaries and benefits | \$ 15,465 | \$ 8,418 | \$ 826 | \$ 24,709 |
| Cost of goods sold | 4 | – | 1,194 | 1,198 |
| Outside services | 3,668 | 1,235 | 86 | 4,989 |
| Advertising | 635 | – | – | 635 |
| Repairs and maintenance | 257 | 472 | 18 | 747 |
| Supplies and printing | 1,556 | 174 | 71 | 1,801 |
| Utilities | 1,561 | 675 | 65 | 2,301 |
| Professional development | 677 | 357 | 3 | 1,037 |
| Hospitality | 265 | 732 | 340 | 1,337 |
| Miscellaneous | 488 | 295 | – | 783 |
| Art transportation, rental fees and insurance | 2,991 | – | – | 2,991 |
| Depreciation | 8,722 | 1,473 | 386 | 10,581 |
| Interest expense | 4,381 | 740 | 194 | 5,315 |
| Net periodic benefit cost other than service cost | 855 | 144 | 38 | 1,037 |
| | \$ 41,525 | \$ 14,715 | \$ 3,221 | \$ 59,461 |

The financial statements report certain categories of expenses that are attributable to more than one function. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include expenses related to facilities, depreciation, and protection services, which are allocated on the basis of square footage of the Museum.

13. 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, 2020 and 2019.

14. Subsequent Events

The Museum has evaluated subsequent events through November 30, 2020, the date the financial statements were issued.

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