



THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

CONSOLIDATED FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2019



SKODA MINOTTI

CPAs, BUSINESS & FINANCIAL ADVISORS

Delivering on the Promise.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

YEAR ENDED JUNE 30, 2019

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INDEPENDENT AUDITORS' REPORT

TO THE BOARD OF TRUSTEES
THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of The Western Reserve Historical Society and Subsidiary (a nonprofit organization), which comprise the consolidated statement of financial position as of June 30, 2019, and the related consolidated statements of activities and changes in net assets, functional expenses, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Western Reserve Historical Society and Subsidiary as of June 30, 2019, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

SKODA MINOTTI & CO.

Cleveland, Ohio
November 11, 2019

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

JUNE 30, 2019

ASSETS:

Cash and cash equivalents	\$ 1,068,809
Accounts receivable	98,575
Prepaid expenses	19,549
Inventory	100,667
Pledges receivable, net	1,039,230
Pledges receivable - related parties	171,566
Property and equipment, net of accumulated depreciation	13,784,374
Assets held for investment in property and equipment	142,908
Investments	16,916,441
Investment, other	195,000
Beneficial interests in trusts	<u>6,394,677</u>
 Total assets	 <u><u>\$ 39,931,796</u></u>

LIABILITIES:

Accounts payable	\$ 164,758
Accrued expenses	26,325
Capital accounts payable	176,875
Deferred revenue	734,333
Line of credit	600,197
Gift annuity obligations	<u>40,314</u>
Total liabilities	<u><u>1,742,802</u></u>

NET ASSETS:

Without donor restrictions	14,620,477
With donor restrictions	<u>23,568,517</u>
Total net assets	<u><u>38,188,994</u></u>
 Total liabilities and net assets	 <u><u>\$ 39,931,796</u></u>

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

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY
CONSOLIDATED STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS
YEAR ENDED JUNE 30, 2019

	Without Donor Restrictions	With Donor Restrictions	Total
OPERATING REVENUES AND SUPPORT			
Gifts, grants and project support	\$ 1,414,750	\$ 1,990,938	\$ 3,405,688
Admissions and memberships	903,981	-	903,981
Endowment support for current operations	41,520	743,256	784,776
Earned income	989,735	-	989,735
Net assets released from donor restrictions	2,566,979	(2,566,979)	-
	<u>5,916,965</u>	<u>167,215</u>	<u>6,084,180</u>
OPERATING EXPENSES			
Program services			
Library, archives, and museums	3,591,811	-	3,591,811
Hale Farm & Village	1,458,674	-	1,458,674
Other historic properties	116,530	-	116,530
Total program services	<u>5,167,015</u>	<u>-</u>	<u>5,167,015</u>
Management and general	935,705	-	935,705
Fundraising	347,817	-	347,817
	<u>6,450,537</u>	<u>-</u>	<u>6,450,537</u>
CHANGE IN NET ASSETS FROM OPERATIONS	<u>(533,572)</u>	<u>167,215</u>	<u>(366,357)</u>
NON-OPERATING CHANGES			
Net investment return	56,540	782,446	838,986
Less: endowment support for current operations	(41,520)	(743,256)	(784,776)
Proceeds from sales of gifts-in-kind	7,000	-	7,000
Change in beneficial interests in trusts	-	(97,897)	(97,897)
Change in fair value of split-interest agreements	(6,275)	-	(6,275)
TOTAL NON-OPERATING CHANGES	<u>15,745</u>	<u>(58,707)</u>	<u>(42,962)</u>
CHANGE IN NET ASSETS	<u>(517,827)</u>	<u>108,508</u>	<u>(409,319)</u>
NET ASSETS - BEGINNING	15,121,930	23,476,383	38,598,313
Adjustment to beginning net assets due to adoption of new accounting standard	16,374	(16,374)	-
NET ASSETS - ENDING	<u>\$ 14,620,477</u>	<u>\$ 23,568,517</u>	<u>\$ 38,188,994</u>

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

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

CONSOLIDATED STATEMENT OF CASH FLOWS

YEAR ENDED JUNE 30, 2019

CASH FLOWS FROM OPERATING ACTIVITIES:

Change in net assets	\$ (409,319)	
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Add back (deduct):		
Contributions restricted for long-term purposes	(805,988)	
Depreciation	1,294,463	
Net realized and unrealized gains on investments	(347,781)	
Change in beneficial interest in trusts	130,952	
Cash provided by (used in) changes in the following items:		
Increase in accounts receivable	(69,514)	
Increase in prepaid expenses	(17,770)	
Decrease in inventory	6,458	
Decrease in pledges receivable	110,984	
Decrease in pledges receivable - related parties	38,550	
Increase in accounts payable	61,746	
Decrease in accrued expenses	(16,288)	
Decrease in deferred revenue	(58,390)	
Decrease in gift annuity obligations	<u>(1,993)</u>	
Net cash used in operating activities		(83,890)

CASH FLOWS FROM INVESTING ACTIVITIES:

Purchases of property and equipment	(699,435)	
Purchases of assets held for investment in property and equipment	(142,908)	
Purchases of long-term investments	(4,255,910)	
Proceeds from sale of long-term investments	<u>4,451,733</u>	
Net cash used in investing activities		(646,520)

CASH FLOWS FROM FINANCING ACTIVITIES:

Collection of contributions restricted for long-term purposes	805,988	
Net payments on line of credit	<u>(75,000)</u>	
Net cash provided by financing activities		<u>730,988</u>

NET INCREASE IN CASH AND CASH EQUIVALENTS 578

CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR 1,068,231

CASH AND CASH EQUIVALENTS - END OF YEAR \$ 1,068,809

SUPPLEMENTARY DISCLOSURES OF CASH FLOW INFORMATION

CASH PAID DURING THE YEAR FOR INTEREST \$ 28,698

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

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

YEAR ENDED JUNE 30, 2019

	Library, Archives and Museums	Hale Farm & Village	Other Historic Properties	Total Program Services	Management and General	Fundraising	Total
Salaries and related costs	\$ 1,448,224	\$ 700,864	\$ 18,300	\$ 2,167,388	\$ 613,287	\$ 235,361	\$ 3,016,036
Exhibit and educational programming materials	235,947	106,478	13,800	356,225	582	641	357,448
Merchandise	45,398	70,289	-	115,687	-	-	115,687
Event catering	17,957	31,498	-	49,455	-	119,510	168,965
Purchased services and office expenses	110,829	74,514	88	185,431	223,157	64,400	472,988
Occupancy	620,604	128,093	18,462	767,159	9,162	4,132	780,453
Liability insurance	91,889	10,533	7,381	109,803	7,956	-	117,759
Advertising	18,122	54,965	-	73,087	18,116	18,116	109,319
Other operating expenses	64,160	28,022	85	92,267	46,390	19,029	157,686
Interest expense	25,254	-	-	25,254	3,444	-	28,698
Depreciation	931,384	284,916	58,414	1,274,714	13,611	6,138	1,294,463
Overall expenses	<u>3,609,768</u>	<u>1,490,172</u>	<u>116,530</u>	<u>5,216,470</u>	<u>935,705</u>	<u>467,327</u>	<u>6,619,502</u>
Less expenses netted against revenues within:							
Gifts, grants, and project support	-	-	-	-	-	119,510	119,510
Earned income	<u>17,957</u>	<u>31,498</u>	<u>-</u>	<u>49,455</u>	<u>-</u>	<u>-</u>	<u>49,455</u>
Total operating expenses	<u>\$ 3,591,811</u>	<u>\$ 1,458,674</u>	<u>\$ 116,530</u>	<u>\$ 5,167,015</u>	<u>\$ 935,705</u>	<u>\$ 347,817</u>	<u>\$ 6,450,537</u>
Percent of total operating expenses	55.7%	22.6%	1.8%	80.1%	14.5%	5.4%	100.0%

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

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities

The Western Reserve Historical Society (the Society) is a nonprofit institution that preserves and uses its collections, historic sites and museums to inspire people to discover the American experience by exploring the tangible history of Northeast Ohio.

The Society acquired a controlling interest on August 25, 2016 as sole member of Holsey Gates Residence Preservation Foundation (Holsey Gates), a 501(c)(3) Type I supporting organization whose mission is to support the charitable and educational purposes of the Society. The financial activity of the Holsey Gates Residence Preservation Foundation is presented as a subsidiary in these consolidated financial statements. The consolidated financial statements include the accounts of the Society and the subsidiary, Holsey Gates. All material inter-company accounts and transactions have been eliminated.

Collections and exhibitions focus on the Western Reserve, placing this Northeast Ohio region in its larger historical context. The Society's holdings and exhibits provide an educational resource for library and museum users, including school children, the general public and scholars. In order to communicate effectively with these audiences, exhibits, whenever appropriate, employ modern interactive technologies and techniques. The Society seeks to make its research materials, exhibits and programs accessible to a diverse and inclusive audience.

The Society's headquarters in Cleveland is known as the Cleveland History Center and includes the research library, exhibit galleries, two historic homes, collections storage and administrative offices. The renowned Society costume collection, one of the largest of its kind in the country, and the exhibit galleries of the Crawford Auto Aviation Collection, are located in the Cleveland History Center.

The Society also owns and operates Hale Farm & Village, a 90 acre living history museum in the Cuyahoga Valley south of Cleveland, and three other historic properties.

The Society's revenues are from a combination of earned and contributed revenue. Earned revenue includes admission fees, memberships, proceeds from space rentals, group tour fees, store sales, school group and public program income, and fees for service revenue. Store sales are reported net of any sales taxes. Contributed revenue includes gifts, grants and endowments, and trusts from individuals and organizations located primarily in Northeast Ohio.

New Accounting Pronouncement

On August 18, 2016, the Financial Accounting Standards Board issued Accounting Standards Update ("ASU") 2016-14, Not-for-Profit Entities (Topic 958) – *Presentation of Financial Statements of Not-for-Profit Entities*. The update addresses the complexity and understandability of net asset classification, deficiencies in information about liquidity and availability of resources, and the lack of consistency in the type of information provided about expenses and investment return. Effective July 1, 2018, the Society adopted ASU 2016-14. The Society has adjusted the presentation of these consolidated financial statements accordingly. There was a \$16,374 prior-period adjustment as a result of adoption of this accounting standard relating to the reclassification of underwater endowments.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Basis of Accounting

The Society prepares its consolidated financial statements on the accrual basis of accounting.

Accordingly, the consolidated financial statements reflect all significant receivables, payables, and other liabilities.

Basis of Presentation

The Society reports information regarding its consolidated financial position and activities according to the following two classes of net assets:

Net assets without donor restrictions: These comprise net assets that are not subject to donor-imposed restrictions and may be expended for any purpose in performing the primary objectives of the Society. The Society's board may designate assets without restrictions for specific purposes from time to time.

Net assets with donor restrictions: These comprise net assets subject to stipulations imposed by donors. Some donor restrictions are temporary in nature because those restrictions will be met by actions of the Society or by the passage of time. Other donor restrictions are perpetual in nature because the donor has stipulated the funds or property be maintained in perpetuity.

Contributions

Unconditional contributions are recognized when pledged and recorded as net assets without donor restrictions or net assets with donor restrictions, depending on the existence and/or nature of any donor-imposed restrictions. Conditional promises to give are recognized when the conditions on which they depend are substantially met. Gifts of cash and other assets are reported with donor restricted support if they are received with donor stipulations that limit the use of the donated assets. When a restriction expires, that is, when a stipulated time restriction ends or a purpose restriction is accomplished, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the consolidated statement of activities and changes in net assets as net assets released from donor restrictions.

Contributions of cash or other assets restricted to the acquisition of long-lived assets are recorded as donor-restricted. If there are no donor restrictions on the long-lived asset's use, the donor restrictions are considered met once the long-lived assets are acquired and the net assets with donor restrictions are reclassified to the net assets without donor restrictions class.

Contributed long-lived assets are recorded at fair value when received. The cost basis of long-lived assets includes the fair value of significant amounts of volunteer labor that was contributed to the construction of the assets.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Use of Estimates

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

Cash and Cash Equivalents

The Society considers all highly liquid investments available for current use with an original maturity of three months or less to be cash equivalents. Cash equivalents held within the Society's investment portfolio are reported within investments in the consolidated statement of financial position because of the Society's intention to use these funds for long-term purposes and not for operations.

Inventory

Inventory is stated at the lower of cost or net realizable value on a first-in first-out (FIFO) basis. The Society capitalizes museum store inventory when purchased and expenses it when sold.

Investments

Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the consolidated statement of financial position. Unrealized gains and losses are included in net investment return under non-operating changes in the consolidated statement of activities and changes in net assets.

Property and Equipment

Property and equipment are recorded at cost when purchased.

The Society capitalizes these types of expenditures for costs that exceed \$1,000. Depreciation is computed using the straight-line method over the estimated useful life of the assets as follows:

Building and land improvements	10 - 30 years
Equipment, furniture and fixtures	4 - 5 years

The Society has not capitalized the original cost of the land and museum buildings. Under GAAP, only improvements made to these assets since 1990 have been capitalized.

Routine expenditures for repairs and maintenance are expensed as incurred.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Collections

The Society's collections of historically significant artifacts, art objects and other materials are held for education, research and public exhibition, and are not capitalized by the Society. The cost of collection items purchased is recorded as an expense in the year acquired.

The Board of Directors considers staff recommendations regarding collection items to be deaccessioned and sold, which may occur because the items are duplicates or no longer meet the mission or purposes of the Society. Net proceeds are used to support the Society's collection management initiatives. Such activity is reflected in the consolidated statement of activities and changes in net assets as proceeds from sales of gifts-in-kind, under non-operating changes.

Beneficial Interests in Trusts

The Society is the beneficiary of certain trusts administered by others. The trusts' assets are invested in debt and equity securities, and the Society records its interests in these trusts at the fair value of the trust assets, unless facts and circumstances indicate that the fair value of the beneficial interests differs from the fair value of the underlying trust assets. Unless otherwise specified by the donor, trust distributions are recognized as gifts, grants, and project support without donor restrictions in the consolidated statement of activities and changes in net assets. Subsequent changes in the fair value of the beneficial interests in trust assets are recognized as non-operating activity in the consolidated statement of activities and changes in net assets.

Deferred Revenue

Deferred revenue consists of rental fees and monies received on grants for services yet to be performed.

Income Taxes

The Society is tax-exempt, under Section 501(c)(3) of the Internal Revenue Code (IRC). However, the Society engages in activities subject to Federal income taxes that are considered unrelated to its exempt purpose. There is a net operating loss carry forward of \$653,233 to offset future income tax liabilities. The tax benefit of the net operating loss carryforward is offset by a valuation allowance. The valuation allowance has decreased by approximately \$75,702 during the year ended June 30, 2019. Accordingly, the Society has not recorded a deferred tax benefit for the effect of the net operating loss carry forward. Net operating loss carry forwards begin to expire in 2021.

Concentrations of Risk

The Society has amounts on hand at financial institutions which may, at times, exceed federally insured amounts.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Concentrations of Risk (continued)

The Society invests in a professionally managed investment portfolio that contains common shares of publicly-traded companies, mutual funds, alternative investments, and money market funds. Such investments are exposed to various risks such as interest rate, market and credit. Due to the level of risk associated with such investments and the level of uncertainty related to changes in the value of such investments, it is at least reasonably possible that changes in risks in the near term would materially affect investment balances and the amounts reported in the consolidated financial statements.

Contributed Services

The Society receives a significant amount of donated services from approximately 200 unpaid volunteers who assist in program, fund-raising and special projects. The Society would recognize significant contributions of services received when those services (a) create or enhance nonfinancial assets, or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by the donation. In accordance with GAAP, the Society has not received significant contributed services for the year ended June 30, 2019.

Auxiliary Organizations

Included in the assets of the Society are the accounts of the following auxiliary organizations:

African American Archives Auxiliary
Aviation Hall of Fame
Friends of the Chisholm Halle Costume Wing
Friends of the Crawford Auto-Aviation Museum
Friends of the Library
Genealogical Committee
Museum Advisory Council
Citizens of Hale Farm & Village
WRHS Young Professionals

Donations to these organizations are made for the benefit of the Society. The organizations remit to the Society funds they have received to invest on their behalf. The Society tracks the funds and earnings for each organization and will disburse the funds as requested by the organization to further the purposes of the Society.

Functional Expenses

The consolidated financial statements report certain categories of expenses that are attributable to more than one program or supporting function. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated are salaries and related costs and office expenses which are allocated based on estimates of time and effort, occupancy and depreciation which are allocated on a square footage basis, and liability insurance which is allocated according to relative asset valuation.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Advertising

Advertising costs are expensed when incurred.

Subsequent Events

The Society evaluated subsequent events through November 11, 2019, the date these consolidated financial statements were available to be issued. There were no material subsequent events that required recognition or additional disclosure in these consolidated financial statements.

2. AVAILABILITY AND LIQUIDITY OF FINANCIAL ASSETS

The following reflects the Society's financial assets as of the consolidated statement of financial position date, reduced by amounts not available for general use because of internal designations or donor-imposed restrictions within one year of the consolidated statement of financial position date. Amounts not available include amounts set aside for long-term investing in the quasi-endowment that could be drawn upon if the governing board approves that action. However, amounts already appropriated from either the donor-restricted endowment or quasi-endowment for general expenditure within one year of the consolidated statement of financial position date have not been subtracted as unavailable.

Financial assets at year end:

Cash and cash equivalents	\$ 1,068,809
Accounts receivable	98,575
Pledges receivable	1,210,796
Assets held for long-term purposes	142,908
Investments	16,916,441
Beneficial interest in trusts	<u>6,394,677</u>

Total financial assets	25,832,206
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Less amounts not available to be used within one year:

Funds with donor restrictions	(682,263)
Funds with board designations, included liquidity reserve	(361,794)
Reserve to fund gift annuity payments	(24,695)
Unappropriated by auxiliaries	(232,329)
Pledges receivable due in greater than one year	(257,968)
Assets held for long-term purposes	(142,908)
Investments held at public foundations	(48,388)
Endowments, less amounts appropriated within one year	(15,714,187)
Beneficial interests in trusts, less amounts receivable within one year	<u>(6,053,914)</u>

Financial assets available to meet general expenditures within one year	<u>\$ 2,313,760</u>
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THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

2. AVAILABILITY AND LIQUIDITY OF FINANCIAL ASSETS (continued)

The Society is substantially supported by restricted contributions. Because a donor's restriction requires resources to be used in a particular manner or in a future period, the Society must maintain sufficient resources to meet those responsibilities to its donors. Thus, financial assets may not be available for general expenditure within one year. As part of the Society's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, the Society invests cash in excess of daily requirements in short-term investments. Occasionally, the board designates a portion of any operating surplus as a liquidity reserve. In the event of an unanticipated liquidity need, the Society also could draw upon its available line of credit.

3. PLEDGES RECEIVABLE

Outstanding pledges were discounted to their present value assuming their respective terms, using a discount rate of 5%. The discounted pledges are scheduled to be collected as follows:

Gross receivable in less than one year	\$ 999,528
Gross receivable in one to five years	280,293
Less allowance for uncollectible pledges	(46,700)
Less present value discount	<u>(22,325)</u>
Pledges receivable, net	<u>\$ 1,210,796</u>

As of June 30, 2019, 74% of gross outstanding pledges are from two donors and 11% of operating revenues were contributed from one of these donors.

4. FAIR VALUE MEASUREMENTS

GAAP requires disclosure of a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into the following three broad categories:

- Level 1 - Quoted unadjusted prices for identical instruments in active markets to which the Society has access at the date of measurement.
- Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs and significant value drivers are observable in active markets. Level 2 inputs are those in markets for which there are few transactions, the prices are not current, little public information exists, or in instances where prices vary substantially over time or among brokered market makers.
- Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. FAIR VALUE MEASUREMENTS (continued)

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

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used as of June 30, 2019.

Long-term investments – The fair values of the underlying assets are used to determine the fair value, based on the reported net asset value.

Beneficial interests in trusts – The fair values of the underlying assets are used to determine the fair value, based on the Society's proportionate beneficial interest in the investment pool.

The following table presents the Society's assets and liabilities measured at fair value on a recurring basis at June 30, 2019:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Financial assets:				
Investments:				
Equity	\$ 9,843,572	\$ -	\$ 12,824	\$ 9,856,396
Fixed income	4,882,152	-	2,960	4,885,112
Alternatives	1,124,745	41,332	7,029	1,173,106
Cash equivalents	<u>214,526</u>	<u>-</u>	<u>25,575</u>	<u>240,101</u>
Subtotal	16,064,995	41,332	48,388	16,154,715
Alternative investments measured at net asset value per share				<u>761,726</u>
Total investments				16,916,441
Beneficial interests in trusts	-	-	6,394,677	<u>6,394,677</u>
Total financial assets				<u>\$ 23,311,118</u>
Financial liabilities:				
Gift annuity obligations	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 40,314</u>	<u>\$ 40,314</u>

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

4. FAIR VALUE MEASUREMENTS (continued)

The following table includes a roll-forward of the amounts in the consolidated statement of financial position for the year ended June 30, 2019 for beneficial interests in trusts classified within Level 3 of the fair value hierarchy:

Balance at July 1, 2018	\$ 6,525,629
Settlement of charitable remainder annuity trust	(33,055)
Change in fair value	<u>(97,897)</u>
Balance at June 30, 2019	<u>\$ 6,394,677</u>

Assets classified within the Level 3 fair value hierarchy were also valued using a market-based approach, however, because the nature of the interests being valued have no observable market values, the Society relied upon comparable net asset values of the underlying securities for estimating the fair values of the beneficial interests in trusts. The Society valued the gift annuity obligation by estimating the future cash payout requirements based on actuarial assumptions on the annuitants' lives, and the discount the obligation using a discount rate of 5.0%.

Certain alternative investments are measured using the net asset per share practical expedient that is permitted under GAAP. The significant investment strategy of the investee of these alternative investments is to provide capital appreciation consistent with the return characteristics of alternative investment portfolios in larger endowments, and to provide capital appreciation with less volatility than that of the equity markets. These alternative investments may be redeemed at quarterly intervals upon written notice at the most recently closed net assets value per share that is reported by the investee.

5. PROPERTY AND EQUIPMENT

At June 30, 2019, property and equipment consisted of the following:

Land	\$ 1,702,727
Building and land improvements	26,639,168
Equipment, furniture and fixtures	950,300
Construction in progress	<u>392,926</u>
	29,685,121
Less: accumulated depreciation	<u>(15,900,747)</u>
	<u>\$ 13,784,374</u>

Construction in progress consists of interior site improvements to the main gatehouse at Hale Farm & Village. The budget for the project is \$695,000 and is scheduled to be placed into service during the fiscal year ending June 30, 2020.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

6. NET ASSETS WITHOUT DONOR RESTRICTIONS

The Society has board designated net assets without donor restrictions for the following purposes as of June 30, 2019:

Quasi-endowment	\$	888,414
Various projects		173,191
Reserve to pay gift annuity obligations		24,695
Liquidity reserve		<u>188,603</u>
	\$	<u>1,274,903</u>

7. NET ASSETS WITH DONOR RESTRICTIONS

Net assets with donor restrictions are available for the following purposes or periods as of June 30, 2019:

Projects with donor purpose restrictions	\$	682,263
Grants with donor time restrictions		633,439
Unappropriated from auxiliaries		229,615
Held by external trustees in perpetuity with payments made to the Society from investment earnings		6,394,677
Donor-restricted endowments:		
Original donor-restricted endowments and amounts to be retained as principal		8,312,274
Portion subject to appropriation under UPMIFA		3,482,441
Term endowments subject to purpose and period restrictions		<u>3,833,808</u>
	\$	<u>23,568,517</u>

8. NET ASSETS RELEASED FROM DONOR RESTRICTIONS

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by the occurrence of the passage of time or other events specified by donors as follows for the year ended June 30, 2019:

Satisfaction of donor purpose restrictions	\$	949,915
Passage of time restrictions		840,352
Appropriations from auxiliaries		400
Termination of charitable remainder trust		33,056
Appropriations from endowments		<u>743,256</u>
	\$	<u>2,566,979</u>

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

9. ENDOWMENTS

The Society's endowment consists of 30 individual funds established for a variety of purposes, including both donor-restricted endowment funds and funds designated by the Board of Directors to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law

The Society is subject to the State of Ohio's enacted version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) and, thus, classifies amounts in its donor-restricted endowment funds as net assets without donor restrictions until the Board of Directors appropriates such amounts for expenditure and any other purpose restrictions have been met. The Society has interpreted UPMIFA as not requiring the maintenance of purchasing power of the original gift amount contributed to the endowment fund, unless a donor stipulates the contrary. As a result of this interpretation, when reviewing its donor-restricted endowment funds, the Society considers a fund to be underwater when the fair value of the fund is less than the sum of (a) the original value of initial and subsequent gift amounts donated to the fund and (b) any accumulations to the fund that are required to be maintained in perpetuity in accordance with the direction of the applicable donor gift instrument. The Society has interpreted UPMIFA to permit spending from underwater funds in accordance with the prudent measures required under the law.

In accordance with UPMIFA, the Society considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

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 Society to retain as a fund of perpetual duration. Deficiencies of this nature exist in four donor-restricted endowment funds, which together have an original value of \$639,031, a current fair value of \$622,670, and a deficiency of \$16,361 as of June 30, 2019. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new contributions, and continued appropriation for certain programs that was deemed prudent by the Society. The Society does not modify its spending policy for underwater funds.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

9. ENDOWMENTS (continued)

Return Objectives and Risk Parameters

The Society has adopted investment and spending policies for endowment assets that attempt to provide funds for various operating and maintenance expenses while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Society must hold in perpetuity or for a donor-specified period as well as board-designated funds. Under this policy, as approved by the Board of Directors, the endowment assets are invested in a manner that is intended to produce results that over time will average the level of the approved endowment spending rate plus inflation. Actual returns in any given year may vary from this targeted growth.

Strategies Employed for Achieving Objectives

In order to maintain long-term purchasing power, the Society 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 Society targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

The Society has a policy of appropriating for expenditure each year 5% from the endowment, calculated on the basis of market values that are determined at least quarterly and averaged over a period of three years immediately preceding the year in which the appropriation for expenditure was made

Changes in Endowment Net Assets for the Fiscal Year Ended June 30, 2019

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Endowment net assets, July 1, 2018	\$ 845,529	\$ 15,447,910	\$ 16,293,439
Investment return, net	42,781	775,243	818,024
Contributions	-	165,000	165,000
Appropriation of endowment assets for expenditure	(41,520)	(743,256)	(784,776)
Other changes:			
Transfer to create board-designated endowment fund	25,000	-	25,000
Reclassification due to changes in GAAP	<u>16,374</u>	<u>(16,374)</u>	<u>-</u>
Endowment net assets, June 30, 2019	<u>\$ 888,164</u>	<u>\$ 15,628,523</u>	<u>\$ 16,516,687</u>

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

10. LINE OF CREDIT

The Society maintains a revolving line of credit with a commercial bank. The line of credit has a maximum allowed borrowing of \$2,500,000. Interest is charged based on the outstanding balance at 150 basis points over the Daily LIBOR Rate. The interest rate was 3.89% at June 30, 2019. The line of credit has an expiration date of July 15, 2020, and is secured by endowment assets without donor restrictions and a first mortgage on property owned by the Society.

11. EMPLOYEE BENEFIT PLAN

The Society maintains a defined contribution salary deferred (403(b)) plan (the Plan) covering eligible employees. Under the Plan, the Society may match 100% of employee salary deferrals up to 3%, and matches 50% of employee salary deferrals over 3% up to a maximum of 5%. The match is discretionary on an annual basis based on budgetary considerations by management. Matching contributions during the year ended June 30, 2019 were \$49,689.

12. BENEFICIAL INTEREST IN ASSETS HELD BY OTHERS

The Society is the beneficial recipient of funds held at two public foundations. In accordance with GAAP, the Society cannot record its beneficial interest in the principal amounts because distributions from these funds are subject to the respective foundations' variance power to direct fund distributions to other beneficiaries.

In May 2011, the Frederick C. and Kathleen S. Crawford Fund was established at the Cleveland Foundation. The market value of the Frederick C. and Kathleen S. Crawford Fund was \$17,723,843 as of June 30, 2019. The Cleveland Foundation's grant awards from the Frederick C. and Kathleen S. Crawford Fund were \$697,317 for the calendar year ending December 31, 2019. These awards are recorded as gifts, grants and project support with donor restrictions until the donor-imposed restrictions are met, by actions of the Society and the passage of time, and subsequently reclassified into net assets without donor restrictions in the consolidated statement of activities and changes in net assets as net assets released from restrictions.

The late Ambassador Holsey Gates Handyside established a fund at The Cleveland Foundation that is intended to assist in maintaining the property and operations of the historic Holsey Gates Handyside residence in Bedford, Ohio. The market value of that fund was \$3,865,794 as of June 30, 2019. Terms of the fund permit The Cleveland Foundation to expend principal from the fund.

The market value of other community funds established for the benefit of the Western Reserve Historical Society was \$1,268,488 as of June 30, 2019.

THE WESTERN RESERVE HISTORICAL SOCIETY AND SUBSIDIARY

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

13. CONTRIBUTIONS SUBJECT TO CONDITIONS

At June 30, 2019, donors have made funding commitments that are subject to conditions that the Society must fulfill in order to be eligible to receive the funds. These amounts are not recorded until amounts are received and conditions are fulfilled under the respective agreement. The commitments are as follows:

<u>Purpose of Commitment</u>	<u>Amount Committed</u>
Educational programming	\$ 112,000
Capital projects at Hale Farm & Village	\$ 300,000

14. NEW ACCOUNTING PRONOUNCEMENTS

In May 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09), which requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity also should understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The Society will adopt this ASU with the fiscal year beginning July 1, 2019. The Society has not yet completed its assessment of the impact of the new standard on its consolidated financial statements.

In June 2018, the FASB issued ASU No. 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made* (ASU 2018-08). ASU 2018-08 was issued to clarify and improve the scope and the accounting guidance received and contributions made. The amendments in this ASU are intended to assist entities in (1) evaluation whether transactions should be accounted for as contributions (nonreciprocal transactions) within the scope of Topic 958, *Not-for-Profit Entities*, or as exchange (reciprocal) transactions subject to other guidance; and (2) determining whether a contribution is conditional. The Society will adopt this ASU with the fiscal year beginning July 1, 2019.