

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
FINANCIAL STATEMENTS
FOR THE YEARS ENDED
JUNE 30, 2009 AND 2008

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
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June 30, 2009 and 2008

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INDEPENDENT AUDITOR'S REPORT



To the Board of Trustees
Museum Associates
Los Angeles, California

We have audited the accompanying statements of financial position of Museum Associates (the "Museum") as of June 30, 2009 and 2008, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Museum's management. 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 of America. 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Museum Associates as of June 30, 2009 and 2008, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads 'SingerLewak LLP'.

SingerLewak LLP

Los Angeles, California
October 6, 2009

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
STATEMENTS OF FINANCIAL POSITION
June 30, 2009 and 2008

ASSETS		
	2009	2008
Current assets		
Cash and cash equivalents	\$ 32,071,859	\$ 4,287,334
Accounts receivable and accrued revenue, net	2,566,253	1,067,073
Pledges receivable – current portion, net	33,835,944	32,470,383
Inventories, net	1,092,807	1,068,828
Prepaid expenses and other current assets	124,147	476,990
Total current assets	69,691,010	39,370,608
Noncurrent assets		
Investments	163,888,753	250,402,893
Pledges receivable – long-term portion, net	83,477,731	102,419,018
Receivables under trust agreements, net	117,773	349,288
Property and equipment, net	280,273,771	241,720,956
Revenue bond trust accounts	103,126,030	148,160,593
Revenue bond issuance costs, net	16,847,032	14,279,779
Overfunded pension assets	-	806,438
Total noncurrent assets	647,731,090	758,138,965
Total assets	\$ 717,422,100	\$ 797,509,573

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

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
STATEMENTS OF FINANCIAL POSITION
June 30, 2009 and 2008

LIABILITIES AND NET ASSETS

	2009	2008
Current liabilities		
Notes payable – current portion	\$ 1,199,589	\$ 4,200,000
Accounts payable and accrued liabilities	15,952,260	13,964,793
Underfunded pension liabilities	732,167	-
Deferred revenue	1,069,126	822,714
Split-interest agreement liabilities	173,072	165,227
Total current liabilities	19,126,214	19,152,734
Noncurrent liabilities		
Revenue bonds	383,000,000	376,200,000
Notes payable – long-term portion	-	1,199,589
Split-interest agreement liabilities	896,987	631,579
Interest rate swaps	31,227,039	12,880,411
Total noncurrent liabilities	415,124,026	390,911,579
Total liabilities	434,250,240	410,064,313
Commitments and contingencies (Note 13)		
Net assets		
Unrestricted		
Board-designated, funds functioning as endowment	47,136,627	61,627,172
Donor-restricted endowment fund losses, net	(3,037,941)	-
Other	67,790,858	101,961,948
Temporarily restricted		
Funds functioning as endowment	34,552,828	54,301,059
Other	115,809,847	137,423,019
Permanently restricted – endowment funds	20,919,641	32,132,062
Total net assets	283,171,860	387,445,260
Total liabilities and net assets	\$ 717,422,100	\$ 797,509,573

Total funds functioning as endowment in Net Assets are \$99,571,155 and \$148,060,293 as of June 30, 2009 and 2008, respectively.

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

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
STATEMENTS OF ACTIVITIES
For the Years Ended June 30, 2009 and 2008

	2009				2008			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues and support								
Revenues								
Membership dues	\$ 6,613,079	\$ 1,740,961	\$ -	\$ 8,354,040	\$ 7,709,187	\$ 1,874,731	\$ -	\$ 9,583,918
Admissions	1,909,247	-	-	1,909,247	2,135,790	-	-	2,135,790
Investment income, net	2,185,494	1,574,942	-	3,760,436	5,859,283	2,935,937	-	8,795,220
Net realized and unrealized loss on investments	(45,151,822)	(17,338,005)	-	(62,489,827)	(19,235,351)	(9,463,839)	-	(28,699,190)
Unrealized loss on interest rate swaps	(18,346,628)	-	-	(18,346,628)	(13,059,069)	-	-	(13,059,069)
County operating contract	16,829,000	-	-	16,829,000	13,773,219	-	-	13,773,219
Auxiliary activities	1,533,802	1,181,301	-	2,715,103	1,796,369	1,167,133	-	2,963,502
Other	2,293,141	(116,130)	-	2,177,011	2,396,639	(15,108)	-	2,381,531
Total revenues	(32,134,687)	(12,956,931)	-	(45,091,618)	1,376,067	(3,501,146)	-	(2,125,079)
Support								
Gifts	9,369,115	19,567,326	37,200	28,973,641	6,584,609	122,012,731	1,143,363	129,740,703
Government grants	5,000,000	338,176	-	5,338,176	-	90,494	-	90,494
Fundraising events, net	-	111,065	-	111,065	2,409,133	317,322	-	2,726,455
Total support	14,369,115	20,016,567	37,200	34,422,882	8,993,742	122,420,547	1,143,363	132,557,652
Net assets released from restrictions								
Satisfaction of program restrictions	37,403,341	(37,403,341)	-	-	48,168,395	(48,168,395)	-	-
Expiration of time restrictions	15,178,529	(15,178,529)	-	-	23,367,293	(23,367,293)	-	-
Release from donor restrictions	11,249,621	-	(11,249,621)	-	1,000,000	-	(1,000,000)	-
Total net assets released from restrictions	63,831,491	(52,581,870)	(11,249,621)	-	72,535,688	(71,535,688)	(1,000,000)	-
Total revenues and support	46,065,919	(45,522,234)	(11,212,421)	(10,668,736)	82,905,497	47,383,713	143,363	130,432,573

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

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
STATEMENTS OF ACTIVITIES
For the Years Ended June 30, 2009 and 2008

	2009				2008			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Expenses								
Program-related expenses								
Exhibitions and collections management	\$ 11,546,475	\$ -	\$ -	\$ 11,546,475	\$ 11,428,708	\$ -	\$ -	\$ 11,428,708
Curatorial	7,245,333	-	-	7,245,333	6,800,932	-	-	6,800,932
Education and public programs	4,115,843	-	-	4,115,843	4,480,591	-	-	4,480,591
Marketing and communication	5,443,218	-	-	5,443,218	5,955,947	-	-	5,955,947
Operations and public services	12,059,986	-	-	12,059,986	12,742,857	-	-	12,742,857
Property and deferred maintenance	1,623,610	-	-	1,623,610	1,059,521	-	-	1,059,521
Provision for doubtful pledges	100,000	-	-	100,000	6,176,913	-	-	6,176,913
Depreciation expense	4,749,916	-	-	4,749,916	1,340,994	-	-	1,340,994
Revenue bond interest expense and fees	7,435,505	-	-	7,435,505	4,353,502	-	-	4,353,502
Revenue bond cost of issuance amortization	598,533	-	-	598,533	418,125	-	-	418,125
Auxiliary activities	3,091,012	-	-	3,091,012	3,209,643	-	-	3,209,643
General and administrative	7,871,132	-	-	7,871,132	7,173,279	-	-	7,173,279
Development	2,770,570	-	-	2,770,570	3,065,119	-	-	3,065,119
Total expenses	68,651,133	-	-	68,651,133	68,206,131	-	-	68,206,131
Change in net assets before change related to collection items	(22,585,214)	(45,522,234)	(11,212,421)	(79,319,869)	14,699,366	47,383,713	143,363	62,226,442
Collection items purchased	(26,883,469)	-	-	(26,883,469)	(41,339,511)	-	-	(41,339,511)
Collection items sold	-	4,160,831	-	4,160,831	-	3,891,343	-	3,891,343
Change in net assets after change related to collection items and before changes related to pension plan	(49,468,683)	(41,361,403)	(11,212,421)	(102,042,507)	(26,640,145)	51,275,056	143,363	24,778,274
Increase in deferred actuarial loss and amortization of prior service cost	(2,230,893)	-	-	(2,230,893)	(1,204,580)	-	-	(1,204,580)
Change in net assets after changes related to pension plan	(51,699,576)	(41,361,403)	(11,212,421)	(104,273,400)	(27,844,725)	51,275,056	143,363	23,573,694
Net assets, beginning of year, as restated	163,589,120	191,724,078	32,132,062	387,445,260	191,433,845	140,449,022	31,988,699	363,871,566
Net assets, end of year	\$ 111,889,544	\$ 150,362,675	\$ 20,919,641	\$ 283,171,860	\$ 163,589,120	\$ 191,724,078	\$ 32,132,062	\$ 387,445,260

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

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
STATEMENTS OF CASH FLOWS
For the Years Ended June 30, 2009 and 2008

	2009	2008
Cash flows from operating activities		
Change in net assets	\$ (104,273,400)	\$ 23,573,694
Adjustments to reconcile change in net assets to cash provided by operating activities		
Net realized loss (gain) on investments	51,567,132	(11,777,546)
Net unrealized loss on investments	10,922,695	40,470,665
Unrealized loss on interest rate swaps	18,346,628	13,059,069
Provision for uncollectible pledges	100,000	4,860,000
Depreciation expense	4,749,916	1,340,994
Revenue bond cost of issuance amortization	598,533	418,125
Collection items purchased	26,883,469	41,339,511
Collection items sold	(4,160,831)	(3,891,343)
Change in operating assets and liabilities		
Accounts receivable and accrued revenue, net	(1,499,180)	8,936,190
Pledges receivable, net	17,475,726	(65,753,084)
Inventories, net	(23,979)	(30,442)
Prepaid expense and other current assets	352,843	(333,057)
Receivables under trust agreements, net	231,515	1,478,879
Overfunded pension assets	806,438	425,252
Accounts payable and accrued liabilities	1,987,467	2,548,964
Underfunded pension liabilities	732,167	-
Deferred revenue	246,412	146,121
	<u>25,043,551</u>	<u>56,811,992</u>
Net cash provided by operating activities		
Cash flows from investing activities		
Net purchases of investments	24,024,311	(10,431,173)
Purchase of property and equipment	(43,302,729)	(97,746,033)
Collection items purchased	(26,883,469)	(41,339,511)
Proceeds from collection items sold	4,160,831	3,891,343
	<u>(42,001,056)</u>	<u>(145,625,374)</u>
Net cash used in investing activities		
Cash flows from financing activities		
Decrease (increase) in revenue bond trust accounts	45,034,563	(100,957,635)
Proceeds from revenue bonds	6,800,000	200,000,000
Revenue bond cost of issuance	(3,165,786)	(8,327,093)
Repayment of notes payable	(4,200,000)	(5,537,500)
Proceeds from notes payable	-	5,000,000
Increase in split-interest agreements liability	273,253	37,546
	<u>44,742,030</u>	<u>90,215,318</u>
Net cash provided by financing activities		
Net increase in cash and cash equivalents	27,784,525	1,401,936
Cash and cash equivalents at beginning of year	<u>4,287,334</u>	<u>2,885,398</u>
Cash and cash equivalents at end of year	<u>\$ 32,071,859</u>	<u>\$ 4,287,334</u>

Supplemental disclosure of noncash investing activities

At June 30, 2009 and 2008, the Museum had \$5,444,833 and \$5,346,498, respectively, included in accounts payable and accrued liabilities for the purchase of property and equipment. During the year ended June 30, 2009 and 2008, the Museum paid \$7,435,505 and \$4,353,502, respectively, in interest expense.

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

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
NOTES TO FINANCIAL STATEMENTS
June 30, 2009 and 2008

NOTE 1 – GENERAL

Museum Associates (the “Museum”) is a California nonprofit corporation whose mission is to serve the public through the collection, conservation, exhibition and interpretation of significant works of art from a broad range of cultures and historical periods, and through the translation of these collections into meaningful educational, aesthetic, intellectual and cultural experiences for the widest array of audiences. To that end, the Museum finances the construction of new facilities, mounts exhibitions and conducts other educational programs to enhance public knowledge of the arts through the operation of the Los Angeles County Museum of Art (“LACMA”).

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

The accompanying financial statements include a statement of financial position that presents the amounts for each of the three classes of net assets: unrestricted, temporarily restricted and permanently restricted. These net assets are classified based on the existence or absence of donor-imposed restrictions and a statement of activities that reflects the changes in those categories of net assets.

Temporarily restricted net assets include those assets whose use by the Museum has been limited by donors to later periods of time or for specified purposes. Permanently restricted net assets include those net assets that must (to the extent required by donor restrictions) be maintained in perpetuity; the investment return from such assets may be used for purposes as specified by the donor or, if the donor has not specified a purpose, for purposes as approved by the Board of Trustees.

Certain amounts included in the prior year have been reclassified to conform with the current-year presentation.

Revenues and Support

Annual membership dues are recognized as revenue when such income is received. Monies received for conditional grants are recorded as deferred revenue until the monies are spent for the specified program or purpose. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
NOTES TO FINANCIAL STATEMENTS
June 30, 2009 and 2008

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenues and Support (Continued)

Contributions, including endowment gifts and pledges, as well as any other unconditional promises to give, are recognized as revenue in the period pledged. Amounts expected to be collected within one year are recorded at their net realizable value. Amounts expected to be collected in future years are recorded at the present value of estimated future cash flows discounted at the risk-free interest rate at the date of the contribution. The Museum does not generally experience collectibility issues regarding its contributions; however, for conservative purposes, the Museum has established a general reserve based on an estimated percentage of the pledge balance.

The fundraising efforts of the Museum are supported by the efforts of various groups of volunteers organized in separate councils. These councils organize and facilitate fundraising activities throughout the year, with the proceeds being used to purchase works of art and fund other Museum programs. The net proceeds generated from these activities are shown as fundraising events in the statements of activities.

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Museum considers all short-term, highly liquid investments with an original maturity of three months or less, when purchased, to be cash equivalents.

Inventories

Inventories consist of Museum Shop goods and are stated at the lower of cost or market. At June 30, 2009 and 2008, inventories included on the statements of financial position of \$1,092,807 and \$1,068,828, respectively, were net of respective obsolescence reserves of \$200,000 and \$400,000.

Investments

The Museum's investments are reflected on the statements of financial position at fair value. Changes in unrealized gains and losses resulting from changes in fair value are reflected in the statements of activities. The Museum's investments consist of cash, fixed income, long-only equities, absolute return, private equity and real estate.

The Museum's equity, absolute return and fixed income securities are generally publicly traded on national securities exchanges and have readily available quoted market values. Such investments are recorded at market value.

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
NOTES TO FINANCIAL STATEMENTS
June 30, 2009 and 2008

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments (Continued)

The Museum's private equity, real estate and some portions of its absolute return investments are carried at estimated fair value. Management establishes fair value of these nonmarketable investments through (a) observable trading activity reported at net asset value, or (b) a documented valuation process including review of audited reports for the investment funds, verification of the fair value of marketable securities in the funds, regular review of fund manager valuation approaches, and monitoring of fund activities. Because of the inherent uncertainty of valuation of nonmarketable investments, the estimated fair values may differ significantly from the values that would have been used had a ready market for the investments existed, and the differences could be material.

Investments received through gifts are recorded at estimated fair value at the date of donation.

Dividend and interest income are accrued when earned. Dividend and interest income earned from investments in all net asset classifications is allocated based on the individual investment asset as a percentage of total investment assets. Income from permanently restricted investments is recorded as unrestricted, except where the instructions of the donor specify otherwise.

Receivables under Trust Agreements and Split-Interest Agreement Liabilities

The Museum has been named as the beneficiary of several trust agreements for which a third party has been named as the trustee. Assets contributed by donors under these trust agreements are recognized at the present value of the estimated future distributions to be received. Interest rates used in determining the present values were the Museum's risk-free rate of return at the date of the gift. Amortization of the discount and changes in actuarial assumptions are included in "Other" in the statements of activities. The present value of the total future amounts to be received was \$117,773 and \$349,288 at June 30, 2009 and 2008, respectively.

Assets contributed by donors under gift annuity agreements and controlled by the Museum are recognized at fair value with a corresponding liability to beneficiaries of the annuity agreements. Such liability is calculated as the present value of the estimated future cash flows to be distributed to the income beneficiaries over their expected lives. The Museum has determined such liability using investment returns consistent with the composition of investment portfolios, single or joint life expectancies from the Internal Revenue Service Publication 1457, and the discount rates applicable in the years in which the agreements were entered into. The present value of these split-interest liabilities was \$1,070,059 and \$796,806 at June 30, 2009 and 2008, respectively.

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
NOTES TO FINANCIAL STATEMENTS
June 30, 2009 and 2008

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property and Equipment

With the exception of the facilities described in the following paragraph, costs of renovating and constructing facilities located on land owned by the County of Los Angeles (the “County”) are expensed, as title to these facilities is either vested in the County or transferred to the County at the close of the construction period, which is relatively short. Facilities that are not located on land owned by the County are capitalized at cost and depreciated using the straight-line method over an estimated life of forty (40) years.

Equipment and other property that is purchased are recorded at cost; items that are donated are recorded at fair value at the date of donation, plus related acquisition costs. Equipment and other property are depreciated using the straight-line method over the estimated useful life of five (5) years.

Capitalized Interest

When qualifying assets are financed with the proceeds of restricted tax-exempt borrowings, the amount of interest cost is capitalized less any interest earned on temporary investment of the proceeds of the borrowings, from the date of the borrowings until the assets constructed with those borrowings are ready for their intended use.

Art Collection

In conformity with the practice followed by many museums, art objects purchased by or donated to the Museum are not capitalized in the statement of financial position. The Museum’s art collection is made up of art objects that are held for exhibition and various other program activities. Each of the items is cataloged, preserved and cared for, and activities verifying their existence and assessing their condition are performed continuously. Purchased collection items are recorded as decreases in unrestricted net assets in the year in which the items are acquired, or in temporarily restricted net assets if the net assets used to purchase the items are restricted by donors; contributed collection items are excluded from the financial statements.

Proceeds from deaccessions or insurance recoveries are reflected as increases in the appropriate net asset classes. Deaccession proceeds are required by Museum policy to be applied to the acquisition of works of art for the permanent collection. The Museum purchased collection items in the amount of \$26,883,469 and \$41,339,511 during the years ended June 30, 2009 and 2008, respectively. The Museum received donated art objects valued at approximately \$15,856,000 and \$4,415,000 during the years ended June 30, 2009 and 2008, respectively.

The Museum retains title to art objects that it acquires; art objects acquired jointly with County and Museum funds become the property of the County and the Museum on a pro rata basis.

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
NOTES TO FINANCIAL STATEMENTS
June 30, 2009 and 2008

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financing Costs

Financing costs are capitalized at cost and amortized using the straight-line method over the terms of the related financing.

Contributed Services

A substantial number of unpaid volunteers, including council members, have made significant contributions of their time to develop the Museum's programs. The value of this contributed time is not reflected in these financial statements, as it is not susceptible to objective measurement or valuation.

Income Taxes

The Museum is a California not-for-profit corporation and is therefore exempt from taxation under Section 501(c)(3) of the Internal Revenue Code ("IRC") and is exempt from federal income taxes pursuant to Section 501(a) of the Internal Revenue Code, and is also exempt from state franchise taxes.

In June 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. ("FIN") 48, "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109" (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 requires that an organization recognize in the financial statements the impact of the tax position if that position will more likely than not be sustained on audit, based on the technical merits of the position. FIN 48 also provides guidance related to de-recognition, classification, interest and penalties, accounting in interim periods, and disclosure. During the years ended June 30, 2009 and 2008, respectively, the Museum performed an evaluation of uncertain tax positions and did not note any matters that would require recognition in the financial statements or which may have an affect on its tax-exempt status.

Estimated Fair Value of Financial Instruments

Financial instruments included in the Museum's statement of financial position include cash and cash equivalents, accounts receivable and accrued revenue, pledges receivable, investments, receivables under trust agreements, revenue bond trust accounts, accounts payable and accrued liabilities, split-interest agreement liabilities, and interest rate swaps. For cash and cash equivalents, accounts receivable and accrued revenue, accounts payable and accrued liabilities, the carrying amounts represent a reasonable estimate of fair values due to their short-term maturity. Pledges receivable have been discounted using applicable risk-free rates to approximate fair value. Receivables under trust agreements and split-interest agreement liabilities are reflected at their estimated fair values using the methodology described above. Investments, revenue bond trust accounts, and derivative financial instruments (i.e., interest rate swaps) are reflected at estimated fair value as described below.

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
NOTES TO FINANCIAL STATEMENTS
June 30, 2009 and 2008

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Estimated Fair Value of Financial Instruments (Continued)

On July 1, 2008, the Museum adopted FASB Statement of Financial Accounting Standards No. 157, "Fair Value Measurements" (SFAS 157), including FASB Staff Position (FSP) No. FAS 157-3, "Determining Fair Value of a Financial Asset When the Market for That Asset Is Not Active," except as it applies to those nonfinancial assets and liabilities for which the effective date has been delayed by one year. SFAS 157 defines fair value, establishes a framework for measuring fair value, and requires enhanced disclosures about fair value measurements. Fair value is the amount 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 (i.e., the exit price).

SFAS 157 requires enhanced disclosures about financial instruments that are measured and reported at fair value. SFAS 157 establishes a fair value hierarchy which prioritizes and ranks the level of market price observability used in measuring fair value. Market price observability is impacted by a number of factors, including the type of instrument, the characteristics specific to the instrument and the state of the marketplace (including the existence and transparency of transactions between market participants). Instruments with readily available actively quoted prices or for which fair value can be measured from actively quoted prices in an orderly market will generally have a higher degree of market price observability and a lesser degree of judgment used in measuring fair value.

Instruments measured and reported at fair value are classified and disclosed in one of the following categories based on inputs:

Level 1 – Quoted prices are available in active markets for identical instruments as of the reporting date. The type of instruments which would generally be included in Level 1 include listed equity securities and the Museum's revenue bond trust account, which is comprised entirely of cash equivalents and taxable bonds with quoted market prices in active markets.

Level 2 – Pricing inputs are observable for the instruments, either directly or indirectly, as of the reporting date, but are other than quoted prices in active markets as in Level 1. Fair value is determined through observable trading activity reported at net asset value or through the use of models or other valuation methodologies. The types of instruments which would generally be included in this category include a portion of the Museum's absolute return investments and its unlisted derivative financial instruments (i.e., interest rate swap).

Level 3 – Pricing inputs are unobservable for the instrument and include situations where there is little, if any, market activity for the instrument. The inputs into the determination of fair value require significant judgment or estimation by the Museum. The types of instruments which would generally be included in this category include debt and equity securities issued by private entities and real estate.

MUSEUM ASSOCIATES
(A CALIFORNIA NOT-FOR-PROFIT CORPORATION)
NOTES TO FINANCIAL STATEMENTS
June 30, 2009 and 2008

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Estimated Fair Value of Financial Instruments (Continued)

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the determination of which category within the fair value hierarchy is appropriate for any given instrument is based on the lowest level of input that is significant to the fair value measurement. The Museum's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the instrument.

The adoption of SFAS 157 did not have a material effect on the Museum's financial statements. See Notes 4 and 6 for further discussion relating to SFAS 157 and the Museum's financial assets.

Concentration of Credit Risk

Credit risk is the failure of another party to perform in accordance with the contract terms. Financial instruments which potentially subject the Museum to concentrations of credit risk consist primarily of cash and cash equivalents, pledges and receivables, investments, and interest rate swaps.

The Museum places its cash and cash equivalents with investment-grade institutions. These account balances usually exceed federally insured limits. However, the Museum has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash and cash equivalents.

With respect to pledges and receivables, the Museum routinely assesses the financial strength of its creditors and believes that the related credit risk exposure is limited. At June 30, 2009, 76% of pledges are due from members of the Board of Trustees.

Investment securities, in general, are exposed to various risks, such as interest rate, credit and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the value of investment securities will occur in the near term and that such change could materially affect the amounts reported in the statements of financial position. The Museum attempts to limit its credit risk associated with investments through diversification and by utilizing the expertise and processes of an outside investment consultant.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recently Issued Accounting Pronouncements

In May 2009, the FASB issued SFAS 165, “Subsequent Events.” SFAS 165 provides general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. The Museum adopted SFAS 165 during the year ended June 30, 2009 and it did not have a material impact on the financial statements. The subsequent events have been evaluated through October 6, 2009, which is the date the financial statements were issued or ready to be issued.

In June 2009, the FASB approved the *FASB Accounting Standards Codification* (“Codification”), which launched on July 1, 2009 and will be effective for financial statements for interim or annual reporting periods ending after September 15, 2009. The Codification is not expected to change GAAP, but will combine all authoritative standards into a comprehensive, topically organized online database. After the Codification launch on July 1, 2009 only one level of authoritative GAAP exists, other than guidance issued by the SEC. All other accounting literature excluded from the Codification will be considered non-authoritative. The Museum is currently evaluating the potential effect that the adoption of the Codification will have on its 2010 financial statements.

NOTE 3 – PLEDGES RECEIVABLE

At June 30, 2009 and 2008, the Museum had the following pledges receivable:

	<u>2009</u>	<u>2008</u>
Due within one year	\$ 34,035,944	\$ 32,570,383
Allowance for doubtful pledges	<u>(200,000)</u>	<u>(100,000)</u>
Pledges receivable – current portion, net	33,835,944	32,470,383
Due between one and five years	67,033,491	81,640,964
Due after five years	40,727,540	49,112,539
Present value discount	(19,283,300)	(23,334,485)
Allowance for doubtful pledges	<u>(5,000,000)</u>	<u>(5,000,000)</u>
Pledges receivable – noncurrent portion, net	<u>83,477,731</u>	<u>102,419,018</u>
Total pledges receivable, net	<u>\$ 117,313,675</u>	<u>\$ 134,889,401</u>

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NOTE 4 – INVESTMENTS

The Museum’s investments consist of operating reserves, funds functioning as endowment, and funds which have been restricted by the donor as endowment. The Museum’s investments are managed as a single diversified portfolio governed by the Museum’s investment policy, which sets asset allocation ranges for marketable and nonmarketable investments, as well as equity and fixed-income investments. Management establishes the fair value of Level 1 investments based on quoted market prices. Management establishes Level 2 investments through observation of trading activity reported at net asset value. Management establishes Level 3 investments through a documented valuation process including review of audited reports for the investment funds, verification of the fair value of marketable securities in the funds, regular review of fund manager valuation approaches, and monitoring of fund activities.

Investments at June 30, 2009 and 2008 are stated at fair value and consist of the following:

	2009	2008
Fixed income	\$ 40,889,250	\$ 36,688,829
Absolute return/alternative investments	93,769,997	61,991,919
Long-only equity	20,059,293	-
Private equity/real estate	9,170,213	-
Domestic equities	-	74,056,684
International equities	-	65,689,500
REITs	-	11,975,961
	<u>\$ 163,888,753</u>	<u>\$ 250,402,893</u>

As of June 30, 2009, the Museum’s investments were classified by level within the valuation hierarchy as follows:

	Level 1	Level 2	Level 3	Total
Fixed income	\$27,707,201	\$ 13,182,049	\$ -	\$ 40,889,250
Absolute return/ alternative investments	8,530,540	27,767,118	57,472,339	93,769,997
Long-only equity	20,059,293	-	-	20,059,293
Private equity/real estate	-	-	9,170,213	9,170,213
	<u>\$56,297,034</u>	<u>\$ 40,949,167</u>	<u>\$ 66,642,552</u>	<u>\$ 163,888,753</u>

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NOTE 4 – INVESTMENTS (Continued)

For the year ended June 30, 2009, the changes in fair value of the Museum’s Level 3 investments are as follows.

Balance, beginning of year	\$ 41,750,405
Purchases (sales), net	29,722,181
Realized gain (loss), net	(264,926)
Unrealized gain (loss), net	<u>(4,565,108)</u>
Balance, end of year	<u>\$ 66,642,552</u>

NOTE 5 – PROPERTY AND EQUIPMENT

Property and equipment at June 30, 2009 and 2008 consisted of the following:

	<u>2009</u>	<u>2008</u>
Land	\$ 36,143,953	\$ 36,143,953
Buildings and improvements	186,715,975	186,715,975
Construction in progress	64,973,586	21,716,490
Equipment and other property	<u>8,208,297</u>	<u>8,162,662</u>
	296,041,811	252,739,080
Less accumulated depreciation	<u>15,768,040</u>	<u>11,018,124</u>
Property and equipment, net	<u>\$ 280,273,771</u>	<u>\$ 241,720,956</u>

Depreciation expenses amounted to \$4,749,916 and \$1,340,994, respectively, for the years ended June 30, 2009 and 2008.

Interest expense and related fees of approximately \$8,956,000 and \$6,779,000, which is net of (\$2,362,000) and (\$5,782,000) in investment income, realized losses and unrealized gains, were capitalized in construction in progress during the year ended June 30, 2009 and 2008, respectively.

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NOTE 6 – REVENUE BONDS AND INTEREST RATE SWAPS

Revenue Bonds

On May 26, 2004, pursuant to an indenture (the “Indenture”) by and between the California Statewide Communities Development Authority (the “Issuer”) and BNY Western Trust Company, as trustee (the “Trustee”), \$118,575,000 of tax-exempt Auction Rate Securities (“2004A&B Bonds”) were issued in two series: Series 2004A was issued for \$50,000,000 and Series 2004B was issued for \$68,575,000. The 2004A&B Bonds were issued in \$25,000 denominations with a variable interest rate that is reset every seven days.

The Issuer lent the proceeds of the 2004A&B Bonds to the Museum pursuant to a Loan Agreement (the “Loan Agreement”) by and between the Issuer and the Museum. Such proceeds received by the Museum were used to finance (i) the construction of new capital improvements on LACMA’s campus, (ii) capitalized interest on the 2004A&B Bonds, and (iii) costs of issuance of the 2004A&B Bonds.

On October 30, 2004, pursuant to an indenture (the “Indenture”) by and between the California Statewide Communities Development Authority (the “Issuer”) and US Bank, as trustee (the “Trustee”), \$57,625,000 of tax-exempt Variable Rate Demand Obligations (“2004C Bonds”) were issued. The 2004C Bonds were issued in \$100,000 denominations with a variable interest rate that is reset every week.

The Issuer lent the proceeds of the Series 2004C Bonds to the Museum pursuant to a Loan Agreement (the “Loan Agreement”) by and between the Issuer and the Museum. Such proceeds received by the Museum were used to finance (i) the design, construction, installation, furnishings and equipping of a new subterranean parking garage on LACMA’s campus, (ii) capitalized interest on the 2004C Bonds, and (iii) costs of issuance of the 2004C Bonds.

On November 9, 2007, pursuant to an Indenture (the “Indenture”) by and between the California Statewide Communities Development Authority (the “Issuer”) and US Bank as trustee (the “Trustee”), \$200,000,000 of tax-exempt Auction Rate Securities (“2007A,B,C&D Bonds”) were issued in four series (Series 2007A, Series 2007B, Series 2007C and Series 2007D) and each for \$50,000,000. The 2007A,B,C&D Bonds were issued in \$25,000 denominations with variable interest rates which reset every seven days.

The Issuer lent the proceeds of the 2007A,B,C&D Bonds to the Museum pursuant to a Loan Agreement (the “Loan Agreement”) by and between the Issuer and the Museum. Such proceeds received by the Museum will be used to finance (i) the design, construction, installation, furnishings and equipping of a new exhibition pavilion, (ii) renovation and improvements to LACMA West, (iii) increase capacity to LACMA’s central heating and cooling plant, (iv) capitalized interest on the 2007A,B,C&D Bonds, and (v) costs of issuance of the 2007A,B,C&D Bonds.

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NOTE 6 – REVENUE BONDS AND INTEREST RATE SWAPS (Continued)

Revenue Bonds (Continued)

The 2004A&B Bonds, 2004C Bonds, and 2007A,B,C&D Bonds were limited to obligations of the Issuer payable solely from and secured by revenues pledged under the Indenture, consisting primarily of loan payments made by the Museum, the Loan Agreement and certain other funds as provided in the Indenture. Payment of principal and interest on the 2004A&B Bonds, 2004C Bonds, and 2007A,B,C&D Bonds when due were insured by the municipal bond insurance policy issued by Financial Guaranty Insurance Company (the “Bond Insurer”). The loan payments were general obligations of the Museum. No specific property was pledged under the Loan Agreement and the payment obligations of the Museum were without recourse to the Museum’s art collection.

On September 10, 2008, pursuant to an Indenture (the “Indenture”) by and between the California Statewide Communities Development Authority (the “Issuer”) and US Bank, as trustee (the “Trustee”), the Museum refinanced the 2004 Bonds (Series A, B and C) and 2007 Bonds (Series A, B, C and D) with \$383,000,000 of tax-exempt Variable Rate Demand Obligations (“2008 Bonds”). The 2008 Bonds were issued in \$100,000 denominations with a variable interest rate that is reset, depending on the series, either weekly or daily.

The 2008 Bonds were issued in five series: Series 2008A was issued for \$100,000,000, Series 2008B was issued for \$100,000,000, Series 2008C was issued for \$95,000,000, Series 2008D was issued for \$60,000,000 and Series 2008E was issued for \$28,000,000.

The 2008 bonds are supported by a letter of credit from a consortium of banks fronted by Wells Fargo. The letter of credit has a three-year term which is set to expire in September 2011, but which may be renewed before that date. Interest is charged at a rate of 1.0% on the letter of credit. As of June 30, 2009, there were no amounts borrowed or outstanding on the letter of credit.

The Issuer lent the proceeds of the Series 2008 Bonds to the Museum pursuant to a Loan Agreement (the “Loan Agreement”) by and between the Issuer and the Museum. Such proceeds received by the Museum were used to (i) redeem all of the Museum’s 2004 and 2007 bonds, totaling \$376,200,000, (ii) finance capitalized interest on the 2008 Bonds, and (iii) finance costs of issuance of the 2008 Bonds.

Under the terms of the Loan Agreement, the Museum is subject to a certain financial covenant, the Adjusted Unrestricted Net Assets to Indebtedness ratio (UNA ratio), which is tested each June 30 and December 31. If the ratio falls below .75, it is an event of default. If the ratio falls below .95 or .85, the Museum is subject to certain requirements by the letter of credit banks and the swap counterparty. As of June 30, 2009, the UNA ratio was .93, which means the letter of credit banks and swap counterparty will require the Museum to deposit the equivalent of one year’s interest into an account with the bond trustee. This amount is estimated to be \$12,500,000 at June 30, 2009, and the Museum will use unspent bond proceeds to satisfy this requirement.

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NOTE 6 – REVENUE BONDS AND INTEREST RATE SWAPS (Continued)

Revenue Bonds (Continued)

As of June 30, 2009 and 2008, unspent bond proceeds held in trust with the trustee consisted of cash and United States Treasury securities, and are classified as Level 1 inputs under the valuation hierarchy. At June 30, 2009 and 2008, the balances on the unspent bond proceeds of the 2008 Bonds and 2004/2007 Bonds, were as follows:

	2009	2008
2008 Bonds	\$ 103,126,030	\$ -
2007 Bonds	-	148,160,593
2004 Bonds	-	-
Total revenue bond trust accounts	\$ 103,126,030	\$ 148,160,593

As of June 30, 2009 and 2008, outstanding amounts due on the 2008 Bonds and 2004/2007 Bonds were as follows:

	2009	2008
2008 Bonds	\$ 383,000,000	\$ -
2007 Bonds	-	200,000,000
2004 Bonds	-	176,200,000
Total revenue bonds	\$ 383,000,000	\$ 376,200,000

As of June 30, 2009, the Series 2008 Bond mandatory bond redemption requirements have been summarized as follows:

Redemption Date	
<u>December 1,</u>	
2030	\$ 35,580,000
2031	35,965,000
2032	36,450,000
2033	75,155,000
2034	76,350,000
2035	39,810,000
2036	41,180,000
2037	42,510,000
Total	\$383,000,000

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NOTE 6 – REVENUE BONDS AND INTEREST RATE SWAPS (Continued)

Interest Rate Swaps

In addition to the Loan Agreement on the 2004A&B Bonds, the Museum entered into a 30-year interest rate swap agreement with Citibank, N.A., New York (“Citibank”) with a notional amount of \$68,575,000. Under the swap agreement, the Museum agreed to pay Citibank a fixed amount of interest, 3.611% per month, and received 56.9% of one-month London Inter-Bank Offered Rate (“LIBOR”) plus 0.21%.

In addition to the Loan Agreement on the 2004C Bonds, the Museum entered into a 30-year interest rate swap agreement with Citibank with a notional amount of \$37,740,000. Under the swap agreement, the Museum agreed to pay Citibank a fixed amount of interest, 3.207% per month, and received 55.1% of one-month LIBOR plus 0.31%.

In addition to the Loan Agreement on the 2007A,B,C&D Bonds, the Museum entered into three 30-year interest rate swap agreements with Citibank with a notional amount of \$50,000,000 each for the Series 2007A, 2007B and 2007C Bonds. Under the swap agreements, the Museum agreed to pay Citibank a synthetic fixed amount of interest, 3.351% per month, and received 60.2% of one-month LIBOR plus 0.15%.

In September 2008, the Museum recast the five existing swap agreements on the 2004 and 2007 Bonds with Citibank and consolidated them into one swap agreement with the same aggregate notional amount of \$256,315,000, and a termination date of December 1, 2037. Under the recast swap agreement, the Museum agrees to pay Citibank a synthetic fixed amount of interest, 3.552% per month, and will receive 59.5% of one-month LIBOR plus 0.30%. The Museum can terminate the swap agreements at any time, but Citibank may terminate the agreement only if certain adverse conditions occur.

As a result of the adoption of SFAS 157, the Museum modified the assumptions used in measuring the fair value of its derivative positions. Specifically, effective July 1, 2008, the Museum now includes the impact of its own credit risk on derivative liabilities measured at fair value under SFAS 157. Counterparty credit risk adjustments are applied to derivatives, such as over-the-counter derivatives, where the base valuation uses market parameters based on LIBOR interest rate curves. Not all counterparties have the same credit risk as that implied by the relevant LIBOR curve, so it is necessary to consider the market value of the credit risk of the counterparty in order to estimate the fair value of such an item. Bilateral or “own” credit risk adjustments are applied to the Museum’s own credit risk when valuing derivatives measured at fair value. Credit adjustments consider the estimated future cash flows between the Museum and its counterparty under the terms of the instrument and affect the credit risk on the valuation of those cash flows, rather than a point-in-time assessment of the current recognized net asset or liability.

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NOTE 6 – REVENUE BONDS AND INTEREST RATE SWAPS (Continued)

Interest Rate Swaps (Continued)

The fair value of the Museum’s interest rate swap liability was estimated in relation to its credit rating by the ratings agencies. Changes in fair value resulting from changes in instrument-specific credit risk were estimated based on credit default swap spreads and an interpolated bond yield spread analysis, and are classified under Level 2 of the valuation hierarchy.

As of June 30, 2009 and 2008, the aggregate interest rate swap value on the 2008 Bonds (credit risk adjusted per SFAS 157) and 2004/2007 Bonds at fair value were as follows:

	2009	2008
2008 Bonds	\$ (31,227,039)	\$ -
2007 Bonds	-	(5,688,204)
2004 Bonds	-	(7,192,207)
Total interest rate swap	\$ (31,227,039)	\$ (12,880,411)

The aggregate unrealized loss reflecting the change in swap value for the 2008 Bonds and 2004/2007 Bonds for the years ended June 30, 2009 and 2008 was \$18,346,628 and \$13,059,069, respectively.

Revenue Bond Issuance Costs

Aggregate issuance costs incurred and capitalized in connection with the 2004 and 2007 Bonds was \$15,399,310 for the year ended June 30, 2008. These costs were being amortized over the bond terms on a straight-line basis. At June 30, 2008 the net capitalized costs were \$14,279,779. For the year ended June 30, 2009, the remaining unamortized capitalized costs on the 2004 and 2007 Bonds were aggregated with the issuance costs incurred and capitalized on the 2008 Bonds amounting to \$3,165,786 and amortized over the 2008 Bond terms on a straight-line basis in accordance with the provisions of EITF 96-19, “Debtor’s accounting for a modification or exchange of debt instruments.” At June 30, 2009, the aggregate net capitalized costs on the 2004, 2007 and 2008 Bonds were \$16,847,032 and are included under “Revenue bond issuance costs, net” on the statements of financial position. The Museum recognized \$598,533 in amortization costs on the capitalized bond issuance costs for the year ended June 30, 2009 and such costs are included under “Revenue bond costs of issuance amortization” on the statements of activities.

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NOTE 7 – NOTES PAYABLE

All notes payable outstanding at June 30, 2009 and 2008 related to the purchase of artwork and consisted of the following:

<u>Note</u>	<u>Due</u>	<u>Interest Rate</u>	<u>2009</u>	<u>2008</u>
Note Payable #1	01/01/10	5.0%	\$ 1,199,589	\$ 2,399,589
Note Payable #2	03/23/09	-%	-	1,000,000
Note Payable #3	01/01/08	-%	<u>-</u>	<u>2,000,000</u>
Total notes payable			1,199,589	5,399,589
Less current portion			<u>1,199,589</u>	<u>4,200,000</u>
Long-term portion			<u>\$ -</u>	<u>\$ 1,199,589</u>

Interest expense incurred on notes payable for the years ended June 30, 2009 and 2008 were \$89,980 and \$151,077, respectively.

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NOTE 8 – NET ASSETS

Unrestricted, temporarily restricted and permanently restricted net assets at June 30, 2009 and 2008 were available for the following purposes:

	2009			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment and funds functioning as endowment				
Operating support	\$ 45,498,407	\$ -	\$ 712,337	\$ 46,210,744
Restricted operating support	-	29,272,624	13,497,735	42,770,359
Art acquisition	1,638,220	5,280,204	6,709,569	13,627,993
Donor-restricted endowment fund losses	(3,037,941)	-	-	(3,037,941)
 Total endowment and funds functioning as endowment	<u>44,098,686</u>	<u>34,552,828</u>	<u>20,919,641</u>	<u>99,571,155</u>
 Other funds				
Programs	76,728,577	114,235,371	-	190,963,948
Art acquisition	5,052,565	1,574,476	-	6,627,041
Property and equipment	(13,990,284)	-	-	(13,990,284)
 Total other funds	<u>67,790,858</u>	<u>115,809,847</u>	<u>-</u>	<u>183,600,705</u>
 Total	<u>\$111,889,544</u>	<u>\$150,362,675</u>	<u>\$ 20,919,641</u>	<u>\$283,171,860</u>

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NOTE 8 – NET ASSETS (Continued)

	2008			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Endowment and funds functioning as endowment				
Operating support	\$ 58,955,990	\$ 712,337	\$ 1,961,959	\$ 61,630,286
Restricted operating support	-	46,420,590	23,472,068	69,892,658
Art acquisition	<u>2,671,182</u>	<u>7,168,132</u>	<u>6,698,035</u>	<u>16,537,349</u>
Total endowment and funds functioning as endowment	<u>61,627,172</u>	<u>54,301,059</u>	<u>32,132,062</u>	<u>148,060,293</u>
Other funds				
Programs	90,189,577	120,167,491	-	210,357,068
Art acquisition	288,470	17,255,528	-	17,543,998
Property and equipment	<u>11,483,901</u>	<u>-</u>	<u>-</u>	<u>11,483,901</u>
Total other funds	<u>101,961,948</u>	<u>137,423,019</u>	<u>-</u>	<u>239,384,967</u>
Total	<u>\$163,589,120</u>	<u>\$191,724,078</u>	<u>\$ 32,132,062</u>	<u>\$387,445,260</u>

NOTE 9 – NET ASSETS RECLASSIFICATION

During the year ended June 30, 2009, the Museum contacted several donors and requested permission to release the permanent restriction attached to their respective donations and allow the Museum to reclassify these net assets as unrestricted. As a result, as of June 30, 2009 the Museum reclassified \$11,249,621 in permanently restricted net assets to unrestricted net assets.

NOTE 10 – ENDOWMENT

The Museum's endowment funds consist of funds functioning as endowment through (a) designation by the Board, (b) temporarily restricted funds managed as endowment funds and (c) donor-restricted endowment funds. The earnings of the Museum's endowment funds support education and art programs, and the mission of the Museum. Net assets associated with endowment funds, including funds designated by the Board to function as endowment, are classified and reported based on the existence or absence of donor-imposed restrictions.

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NOTE 10 – ENDOWMENT (Continued)

Through December 31, 2008, the California Uniform Management of Institutional Funds Act (UMIFA) governed the management and use of donor-restricted endowment funds held by charitable institutions in the state of California. Under UMIFA, the Museum classified as permanently restricted net assets the original value of gifts donated to the permanent endowment and accumulations to the permanent endowment made in accordance with the direction, if any, of the applicable donor gift instrument. Accumulated earnings of donor-restricted endowment funds are classified as unrestricted or temporarily restricted net assets, funds available for operations in accordance with the donor specifications.

Effective January 1, 2009, the state of California adopted the Uniform Prudent Management of Institutional Funds Act (UPMIFA), which replaces UMIFA. In August of 2008, the FASB issued FSP No. 117-1, “Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds.” The disclosure provisions of FSP No. 117-1 were applied by the Museum in the year ended June 30, 2009, as shown below.

At June 30, 2009, the Museum’s endowment net asset composition by type of fund was as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Board-designated endowment funds	\$ 47,136,627	\$ -	\$ -	\$ 47,136,627
Temporarily restricted funds managed as endowment funds	-	22,836,396	-	22,836,396
Donor-restricted endowment funds	<u>(3,037,941)</u>	<u>11,716,432</u>	<u>20,919,641</u>	<u>29,598,132</u>
Total endowment funds	<u>\$ 44,098,686</u>	<u>\$ 34,552,828</u>	<u>\$ 20,919,641</u>	<u>\$ 99,571,155</u>

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the Museum to retain as a fund of perpetual duration. In accordance with the provisions of FSP No. 117-1, deficiencies of this nature that are reported in unrestricted net assets were \$3,037,941 as of June 30, 2009. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the Board of Trustees.

MUSEUM ASSOCIATES
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NOTE 10 – ENDOWMENT (Continued)

For the year ended June 30, 2009, the Museum’s endowment net assets changed as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>		<u>Permanently Restricted</u>	<u>Total</u>
		<u>Donor- restricted</u>	<u>Managed as Endowment</u>		
Balance, beginning of year	\$ 61,627,172	\$ 20,605,041	\$ 33,696,018	\$ 32,132,062	\$ 148,060,293
Investment return					
Investment income, net	1,388,944	569,503	485,779	-	2,444,226
Net realized and unrealized depreciation	<u>(27,801,621)</u>	<u>(11,783,716)</u>	<u>(11,385,227)</u>	<u>-</u>	<u>(50,970,564)</u>
Total investment return	(26,412,677)	(11,214,213)	(10,889,448)	-	(48,526,338)
Contributions	-	-	-	37,200	37,200
Other changes					
Transfers of Board-designated endowment funds	2,578,844	(712,337)	(616,886)	(1,249,621)	-
Donor-released from restrictions	9,343,288	-	656,712	(10,000,000)	-
Reclassification of underwater endowment funds	<u>(3,037,941)</u>	<u>3,037,941</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total endowment funds	<u>\$ 44,098,686</u>	<u>\$ 11,716,432</u>	<u>\$ 22,836,396</u>	<u>\$ 20,919,641</u>	<u>\$ 99,571,155</u>

In conformity with generally accepted accounting principles, investment income on the Museum’s endowment is recorded as unrestricted revenue and unrestricted net assets, unless otherwise directed by the applicable donor gift instrument.

The Museum’s endowment spending policy is based on the trailing market value of its endowment. Specifically, it is 5% of the average market value of the endowment at each of the 12 prior quarters as of March 31 in the most recent fiscal year. The spending policy is reviewed by the Finance Committee of the Board of Trustees annually.

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NOTE 10 – ENDOWMENT (Continued)

As delegated authority by the full Board, the Finance Committee of the Board has adopted an investment policy that governs the management and oversight of the endowment funds and other investments (endowment and reserves). The policy sets forth the objectives for the endowment and reserves of the Museum, the strategies to achieve the objectives, procedures for monitoring and control, and the delineation of responsibilities for the Finance Committee, consultant, investment managers, staff and custodian in relation to the portfolio. The policy is intended to allow for sufficient flexibility in the management oversight process to capture investment opportunities as they may occur, while at the same time setting forth reasonable risk control parameters that a prudent person would take in the execution of the investment program. Investment assets are managed on a total return basis, with emphasis on both preservation of capital and acceptance of investment risk necessary to achieve favorable performance on a risk-adjusted basis. In addition to parameters of return and risk, the policy establishes minimum liquidity guidelines for the portfolio. Other objectives are to maintain or enhance the real purchasing power of the endowment and reserves after covering its spending rate; to provide sufficient cash to cover debt interest and retirement of debt over the life of the Museum's outstanding debt; to outperform a policy benchmark return, after fees, at a lower level of risk over seven-to-ten-year rolling periods; and to diversify investments to reduce the impact of losses in single investments, industries or asset classes.

NOTE 11 – CHANGE IN ACCOUNTING POLICY

The Museum has made a review of its policy over accounting for irrevocable and enforceable pledges from donors that are payable upon death, and has determined that it is more appropriate to recognize these pledges as a contribution on the pledge date instead of recording such pledges upon receipt of the proceeds upon the donor's death. The net contributions recognized in temporarily restricted income at June 30, 2007 was \$4,069,142.

The Museum has restated its beginning net assets as of June 30, 2008 as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Net assets at June 30, 2007, as previously reported	\$191,433,845	\$136,379,880	\$31,988,699	\$359,802,424
Adjustments noted above	-	4,069,142	-	4,069,142
Net assets at June 30, 2007, as restated	<u>\$191,433,845</u>	<u>\$140,449,022</u>	<u>\$31,988,699</u>	<u>\$363,871,566</u>

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NOTE 12 – EMPLOYEE BENEFIT PLANS

The Museum sponsors four (4) employee benefit plans as described below:

Defined Benefit Plan

The Museum sponsors a defined benefit pension plan. Retirement benefits are provided through a noncontributory defined-benefit retirement plan (the “Plan”) for generally all employees who have completed one year of service, and have not attained age sixty-five (65). The Museum’s funding policy is to contribute amounts to the Plan sufficient to meet the minimum funding requirements of the Employee Retirement Income Security Act, plus additional amounts as determined to be appropriate. Contributions to the Plan were \$1,450,000 during the year ended June 30, 2009.

The following sets forth the components of net periodic benefit costs and the obligations and funded status of the defined benefit plan. Valuations of assets and liabilities are determined using a measurement date of June 30.

Net periodic benefit costs for the years ended June 30:

	<u>2009</u>	<u>2008</u>
Service cost	\$ 925,632	\$ 795,642
Interest cost	499,178	437,732
Expected return on plan assets	(753,387)	(705,748)
Amortization of transition (assets) or obligations	-	2,886
Amortization of prior service cost	34,779	34,779
Amortization of actuarial (gains) losses	-	(21,102)
Amortization of net (gains) losses	<u>51,510</u>	<u>(65,377)</u>
Net periodic benefit cost	<u>\$ 757,712</u>	<u>\$ 478,812</u>

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NOTE 12 – EMPLOYEE BENEFIT PLANS (Continued)

Defined Benefit Plan (Continued)

Obligation and funded status at June 30:

	2009	2008
Change in benefit obligation		
Benefit obligation at beginning of year	\$ 7,945,681	\$ 7,002,572
Service cost	925,632	795,642
Interest cost	499,178	437,732
Benefits paid	(451,724)	(250,973)
Settlements, curtailments or other events	51,510	6,446
Actuarial (gain) or loss	(309,321)	(45,738)
Benefit obligation, end of year	8,660,956	7,945,681
Change in plan assets		
Fair value of plan assets at beginning of year	8,752,119	8,234,262
Actual return on plan assets	(1,821,606)	(581,130)
Employer contributions	1,450,000	1,350,000
Settlement or curtailment	(317,621)	(131,462)
Benefits paid	(134,103)	(119,551)
Fair value of plan assets, end of year	7,928,789	8,752,119
Funded status	\$ (732,167)	\$ 806,438

Due to the adoption of SFAS 158 at July 1, 2006, the Museum made an adjustment to the beginning net assets to recognize the unfunded status of the pension plan as an asset for pension benefits. During the year ended June 30, 2009 and 2008, the Museum also recorded the actuarial loss and amortization of prior service costs adjustments to net assets.

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NOTE 12 – EMPLOYEE BENEFIT PLANS (Continued)

Defined Benefit Plan (Continued)

The following represents pension costs directly charged to net assets at June 30:

	2009	2008
Accumulated net adjustment to net assets, beginning of year	\$ (480,989)	\$ 723,591
Current year change		
Actuarial loss during the year	(2,265,672)	(1,241,140)
Amortization of prior service cost	34,779	36,560
Total current year change	(2,230,893)	(1,204,580)
Accumulated net adjustment to net assets, end of year	<u>\$(2,711,882)</u>	<u>\$ (480,989)</u>

The accumulated benefit obligation for the plan was \$8,660,956 and \$7,945,681 at June 30, 2009 and 2008, respectively.

Weighted-average assumptions used to determine benefit obligations were as follows at June 30:

	2009	2008
Discount rate	6.3%	6.3%
Expected return on plan assets	8.0%	8.0%
Rate of compensation increase	5.0%	5.0%

The discount rate is estimated based on the yield on a portfolio of high-quality debt instruments. Expected long-term rate of return on plan assets is the projected rate for plan assets, and the rate of compensation increase is estimated based on the Museum's historical rate. The Museum's management develops all actuarial assumptions with the third-party pension actuary.

The Museum's year-end plan weighted-average asset allocations by category were as follows:

	Target	2009	2008
Equity securities	75%	57.0%	66.8%
Debt securities	25%	43.0%	32.9%
Cash	-%	-%	0.3%

Plan assets are invested in a diversified portfolio whose value is subject to fluctuations of the securities market.

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NOTE 12 – EMPLOYEE BENEFIT PLANS (Continued)

Defined Benefit Plan (Continued)

Changes in this value attributable to differences between actual and assumed returns on plan assets are deferred as unrecognized gains or losses and included in the determination of net pension expense over time.

The Museum expects to contribute \$1,200,000 to the defined benefit plan for the fiscal year ending June 30, 2009.

Benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows:

<u>For the Year</u> <u>Ending June 30,</u>	
2010	\$ 266,238
2011	268,702
2012	272,596
2013	329,536
2014	361,850
2015 to 2020	<u>2,904,579</u>
Total	<u>\$ 4,403,501</u>

Defined Contribution Plan

The Museum also offers a defined contribution plan, whereby employees elect to make voluntary contributions (up to limits set by law) to the plan through a payroll deduction. The Museum then matches 100% of the employee contributions, up to four percent (4%) of salary. Matching contributions during the years ended June 30, 2009 and 2008, amounted to approximately \$457,000 and \$434,000, respectively.

Deferred Compensation Plan

The Museum offers a deferred compensation plan for its highly compensated employees. Employees compensated in excess of \$90,000 annually are eligible to elect to make voluntary contributions (up to the limits set by law) to the plan through payroll deductions in excess of the annual thresholds allowed under the Museum's defined contribution plan.

Executive Deferred Compensation Plans

In April 2005, the Museum implemented an executive deferred compensation program for certain key employees. The plan had a five-year vesting period, after which the employees were able to withdraw the funds. The total cost of the program was to be expensed over the five-year vesting period and required five annual payments of \$56,000. The plan's vesting period was accelerated to three (3) years and the entire \$280,000 was paid into the plan as of June 30, 2008.

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NOTE 12 – EMPLOYEE BENEFIT PLANS (Continued)

Executive Deferred Compensation Plans (Continued)

In February 2006, the Museum implemented an executive deferred compensation program for a key employee. The plan has a five-year vesting period, after which the employee is able to withdraw the funds. The total cost of the program is \$1,000,000 and is being expensed over the five-year vesting period in the amount of \$200,000 annually.

As of July 1, 2008, the Museum implemented a second executive deferred compensation program for another key employee. The plan vests over a three-fiscal-year period, after which the employee will be entitled to the compensation. The total cost of the program is \$450,000 and is being expensed over the three-year vesting period in the amount of \$150,000 annually.

NOTE 13 – COMMITMENTS AND CONTINGENCIES

Litigation

In the normal course of business, the Museum may become a party to litigation. Management believes there are no asserted or unasserted claims or contingencies that would have a significant impact on the financial statements of the Museum as of June 30, 2009.

Operating Leases

The Museum has certain equipment under noncancellable operating leases with terms up to sixty-nine (69) months and expiring through 2015. Total rental expense on operating leases was approximately \$390,000 and \$649,000 for the years ended June 30, 2009 and 2008, respectively. Future minimum lease payments are as follows:

For the Year <u>Ending June 30,</u>	
2010	\$ 388,000
2011	108,000
2012	16,000
2013	16,000
2014	16,000
Thereafter	<u>12,000</u>
Total	<u>\$ 556,000</u>