

SANTA BARBARA MUSEUM OF NATURAL HISTORY

FINANCIAL STATEMENTS

December 31, 2009

(with Independent Auditors' Report Thereon)

**SANTA BARBARA MUSEUM OF NATURAL HISTORY
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REED S. SPANGLER
SUSAN M. FRAZIER
JANE E. RUSSELL
GAIL H. ANIKOUCHINE
WILLIAM L. JACKSON

INDEPENDENT AUDITORS' REPORT

JAMES W. FISCHER
MELISSA R. PETERSEN
HOWARD B. ATKINSON
MARILYN D. PARKE
JEFF RESTIVO

To the Board of Directors of
Santa Barbara Museum of Natural History

ROBERT R. BABCOCK
Consultant
RICHARD L. HUNT
Consultant
HARVEY K. LYNN
Consultant

We have audited the accompanying statement of financial position of the Santa Barbara Museum of Natural History (a California nonprofit organization) as of December 31, 2009 the related statements of activities, net assets and cash flows for the year ended December 31, 2009. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Santa Barbara Museum of Natural History as of December 31, 2008, were audited by other auditors whose report dated March 4, 2009, expressed an unqualified opinion on those statements.

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 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 audit provides 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 Santa Barbara Museum of Natural History as of December 31, 2009, and the changes in its net assets, cash flows and functional expenses for the year ended December 31, 2009, in conformity with accounting principles generally accepted in the United States of America.

MacFarlane, Faletti & Co. LLP

Santa Barbara, California
March 16, 2010

E-MAIL cpa@mfc.com
WEBSITE www.mfc.com

Santa Barbara Museum of Natural History
Statement of Financial Position as of December 31, 2009
with Comparative 2008 Totals

	As of December 31,	
	2009	2008
ASSETS		
Current Assets		
Cash & Cash Equivalents	\$1,595,305	\$439,043
Investments (NOTE 2)	\$37,791,102	\$32,581,820
Grants & Pledges Receivable (NOTE 3)	\$201,304	\$196,857
Other Receivables	\$232,373	\$207,355
Inventory	\$59,118	\$67,079
Prepaid Expenses & Other Assets	\$134,311	\$104,152
Total Current Assets	\$40,013,513	\$33,596,306
Non-Current Assets		
Grants & Pledges Receivable - Long-term (NOTE 3)	\$120,000	\$73,000
Interest in Charitable Trusts (NOTE 6)	\$5,193,681	\$5,197,666
Property Held for Investment (NOTE 4)	\$630,000	\$630,000
Property & Equipment, net (NOTE 5)	\$12,371,436	\$12,741,976
Total Non-Current Assets	\$18,315,117	\$18,642,642
Total Assets	\$58,328,630	\$52,238,948
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accounts Payable & Accrued Liabilities	\$291,528	\$298,660
Deferred Revenue (NOTE 14)	\$253,900	\$232,700
Total Current Liabilities	\$545,428	\$531,360
Net Assets (NOTES 7, 8 & 9)		
Unrestricted-Undesignated	\$15,392,313	\$15,631,716
Unrestricted-Board Designated	\$23,284,472	\$18,141,756
Temporarily Restricted	\$11,506,473	\$10,334,170
Permanently Restricted	\$7,599,945	\$7,599,945
Total Net Assets	\$57,783,202	\$51,707,588
Total Liabilities and Net Assets	\$58,328,630	\$52,238,948

The accompanying notes are an integral part of this financial statement

Santa Barbara Museum of Natural History
Statement of Activities for the Year Ended December 31, 2009
with Comparative 2008 Totals

	Unrestricted			Temporarily Restricted	Permanently Restricted	All Funds	
	Operating	Other Unrestricted	Board Designated			2009 Total	2008 Total
Income							
Support & Revenue							
Admissions	\$675,218	\$0	\$0	\$0	\$0	\$675,218	\$558,388
Membership	\$430,580	\$0	\$0	\$0	\$0	\$430,580	\$415,551
Contributions and Grants	\$259,908	\$0	\$171,453	\$1,873,844	\$0	\$2,305,205	\$2,414,577
Investment Income / Draw	\$1,857,786	\$0	\$4,226,678	\$1,145,284	\$0	\$7,229,748	(\$15,182,807)
Education Fees	\$109,356	\$1,000	\$0	\$0	\$0	\$110,356	\$102,108
Contracts	\$0	\$0	\$0	\$39,325	\$0	\$39,325	\$19,500
Other Income	\$40,450	\$80,722	(\$86,452)	\$69,393	\$0	\$104,113	\$95,078
Change in Value of Charitable Trusts	\$0	\$0	\$0	\$908,739	\$0	\$908,739	(\$1,337,983)
Total Income	\$3,373,298	\$81,722	\$4,311,679	\$4,036,585	\$0	\$11,803,284	(\$12,915,588)
Revenue Centers							
Store Sales	\$418,294	\$0	\$62,781	\$0	\$0	\$481,075	\$503,200
Less Store Expenses	(\$279,500)	(\$36,629)	\$0	\$0	\$0	(\$316,129)	(\$340,923)
Special Events	\$291,116	(\$11,129)	\$63,529	\$0	\$0	\$343,516	\$474,179
Less Special Event Expenses	(\$228,514)	\$0	(\$51,516)	\$0	\$0	(\$280,030)	(\$324,496)
Rental Income	\$271,529	\$0	\$0	\$0	\$0	\$271,529	\$259,573
Less Rental Expenses	(\$26,023)	\$0	\$0	\$0	\$0	(\$26,023)	(\$28,679)
Total Revenues Centers	\$446,902	(\$47,758)	\$74,794	\$0	\$0	\$473,938	\$542,854
Total Income	\$3,820,200	\$33,964	\$4,386,473	\$4,036,585	\$0	\$12,277,222	(\$12,372,734)
Net Assets							
Released from Restriction	\$475,531	\$1,195,707	\$1,193,044	(\$2,864,282)	\$0	\$0	\$0
	\$475,531	\$1,195,707	\$1,193,044	(\$2,864,282)	\$0	\$0	\$0
Expenses							
Program Expenses							
Exhibits & Visitor Services	\$663,622	\$1,070,648	\$22,786	\$0	\$0	\$1,757,056	\$1,783,078
Education	\$779,375	\$222,456	\$0	\$0	\$0	\$1,001,831	\$1,029,368
Collections & Research	\$628,795	\$1,405,664	\$87,888	\$0	\$0	\$2,122,347	\$2,334,010
Total Program Expenses	\$2,071,792	\$2,698,768	\$110,674	\$0	\$0	\$4,881,234	\$5,146,456
Supporting Services							
Management & General	\$1,475,006	(\$975,212)	\$326,127	\$0	\$0	\$825,921	\$824,697
Membership	\$87,228	\$49,026	\$0	\$0	\$0	\$136,254	\$172,439
Development	\$622,048	(\$263,850)	\$0	\$0	\$0	\$358,198	\$379,060
Total Supporting Services	\$2,184,282	(\$1,190,036)	\$326,127	\$0	\$0	\$1,320,373	\$1,376,196
Total Expenses	\$4,256,074	\$1,508,732	\$436,801	\$0	\$0	\$6,201,607	\$6,522,652
Net Excess (Deficit)	\$39,657	(\$279,061)	\$5,142,716	\$1,172,303	\$0	\$6,075,615	(\$18,895,386)

Accompanying notes are an integral part of this statement

Santa Barbara Museum of Natural History
Statement of Cash Flows for the Year Ended December 31, 2009
with Comparative 2008 Totals

	2009	2008
Cash Flows from Operating Activities		
Change in Net Assets	\$ 6,075,615	\$ (18,895,385)
Adjustments to reconcile change in net assets to cash provided by operating activities		
Depreciation	679,616	600,275
Realized and unrealized (gain)/loss on investments	(6,481,003)	16,551,828
Change in value of charitable trusts	3,985	1,337,983
Changes in:		
Pledges receivable	(51,447)	(223,786)
Other receivables	(25,018)	130,019
Inventory	7,961	7,116
Prepaid expenses and other assets	(30,159)	45,910
Accounts payable and accrued expenses	(7,132)	(53,409)
Deferred revenue	21,200	(13,395)
Net Cash Provided/(Used) by Operating Activities	193,618	(512,844)
Cash Flows from Investing Activities		
Purchase of fixed assets	(309,076)	(1,348,052)
Purchase of investments	(20,649,282)	(19,384,295)
Proceeds from sale of investments	21,921,002	21,329,419
Net Cash Provided by Investing Activities	962,644	597,072
Net Increase in Cash	1,156,262	84,228
Cash and Cash Equivalents a Beginning of Year	439,043	354,815
Cash and Cash Equivalents a End of Year	\$ 1,595,305	\$ 439,043

Supplemental Cash Flow Information:

See Footnote 13.

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organizational Data – The Santa Barbara Museum of Natural History (the Museum) was founded in 1916. The Museum’s mission is to inspire a thirst for discovery and a passion for the natural world. The Museum accomplishes this mission through the three following guiding principles:

Inspiring an Awe for Nature and a Thirst for Discovery

The Santa Barbara Museum of Natural History aims to spark curiosity and ignite a passion for nature. We strive to expand our understanding of the natural world, share the process of discovery, and communicate the interconnectedness of all species.

The spirit of discovery drives our research, exhibits, and educational programs. We encourage involvement by making science fun and accessible, inspiring our audiences to explore the vast mysteries of nature.

Promoting Sustainability

The Museum promotes the preservation of the Earth's natural systems as an urgent priority and fosters a sense of collective responsibility, necessary for maintaining biodiversity and for the well-being of our own species.

We embrace sustainability as a critical element in all we do. We recognize that society's long term success requires an understanding and respect for nature's limits, and we strive to lead by example, illuminating the connections between research, policy and personal responsibility.

Connecting Our Communities

The Museum is a community resource and a welcoming, accessible center for community engagement. We use the full range of the human experience to reach and connect people of all ages and backgrounds, transcending geographic, economic, and cultural boundaries.

We pursue a broad web of relationships and partnerships to facilitate communication and mutual understanding, leveraging our resources and technology to bring the Museum into the lives of the widest possible range of professional and community groups.

The Museum fulfills its mission through collections, research, exhibits and educational programs.

The Museum operates in two locations; at its Mission Canyon Campus at 2559 Puesta del Sol, Santa Barbara, California and at its Ty Warner Sea Center located at 211 Stearns Wharf, Santa Barbara California.

Aggregate attendance at the Mission Canyon Campus and the Ty Warner Sea Center was 159,000 people in 2009.

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

Fund Accounting – The accounts of the Museum are maintained in accordance with the principles of fund accounting. This accounting and reporting method classifies resources by their nature and purpose, based on the presence or absence of donor-imposed restrictions, into three classes of net assets, unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Unrestricted net assets consist of funds free of any donor-imposed restrictions and are sub-classified into undesignated funds and Board designated funds.

Unrestricted net assets consist of the following:

- Operating Funds that are unrestricted resources used to support the Museum's operations.
- Other Unrestricted Funds that are primarily quasi-endowment funds consisting of realized and unrealized capital gains from the permanently restricted endowment funds as well as funds that the Board of Trustees has decided to maintain intact and to invest to generate operating income.
- Board Designated Funds that are resources designated for specific purposes by the Board of Trustees.

Temporarily restricted net assets consist of contributions and other inflows of funds temporarily subject to donor-imposed restrictions. The restrictions are temporary in that they are expected to expire with the passage of time or be satisfied and removed by actions of the Museum that fulfill donor stipulations.

Permanently restricted net assets consist of contributions and other inflows of funds subject to donor-imposed restrictions that neither expire by the passage of time nor can be fulfilled or otherwise removed by actions of the Museum. These funds are invested to provide income to support either specific activities or general operations, in accordance with donor stipulations.

Inventory – Inventory consists of goods held for sale in the Museum store and is carried at the lower of cost (first-in, first-out method) or market value. At December 31, 2009 management has established a reserve against inventory valuation of \$9,000.

Investments – Investments are carried at their fair market value. (See Note 2)

Building, Equipment and Improvements – Building, equipment and improvements are recorded at cost, or if donated, at estimated fair value at date of donation. Assets having an estimated useful life in excess of one year and original cost or donated value of \$5,000 or more are capitalized in the year of acquisition. Depreciation expense is computed using the straight-line method over the useful lives of the assets. Depreciable lives of the assets range from 3 to 40 years. Donor restrictions on contributions for the purchase of buildings, equipment or improvements are considered satisfied when the expenditure is incurred and a transfer from temporarily restricted to unrestricted net assets is made at that time.

Museum League – The Museum conducts a number of fund raising activities through an auxiliary unit, the Museum League, which supports essential Museum projects. The income

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

from these activities is included in special events on the Statement of Activities in the board designated column.

Collections – In conformity with the practice followed by museums, collection objects purchased and donated are not included in the accompanying statement of financial position.

The Museum is continually developing the collections, which currently include more than three million specimens, artifacts, other cultural objects, books and manuscripts. These holdings are used by Museum scientists and a worldwide network of researchers from a variety of disciplines. Their usage forms the basis of published findings, as well as programs in education and Museum exhibitions. The collection is kept under curatorial care including conservation practices, and is subject to the Museum's policy that requires proceeds from the sale of collection items to be used only for acquisition of additional collections. The Museum does not recognize any contribution income from donated collection items, as its collections are not capitalized.

Contributed Services – A significant number of volunteers donated many hours of their time in 2009 to the Museum as docents, research associates, interns, board members and in auxiliary organizations. This volunteer time is critical to the success of the Museum. However, as this volunteer service does not meet the recognition requirements under generally accepted accounting principles, no amount has been recorded in these financial statements for these services.

Membership Revenue – Membership revenue is comprised of both a contribution component and an earned income component. The portion of membership dues that represents an economic benefit received by the member is recognized as income as it is earned. The portion of membership dues that represents a contribution is recognized as income when received.

Functional Allocation of Expenses – The costs of providing the various programs and other activities are charged to each department based on direct expenditures incurred. Any expenditure not directly chargeable is allocated to each department based on the estimated benefit to that department.

Income Taxes – The Santa Barbara Museum of Natural History is exempt from federal and state income taxes under Section 501(c)(3) of the Internal Revenue Code and Section 23701d of the California Revenue and Taxation Code. The Museum is not considered a private foundation. At December 31, 2009, the Museum is not aware of any uncertain tax positions.

Cash and Cash Equivalents - The Museum classifies its unrestricted short-term, highly liquid investments having original maturities of three months or less as cash equivalents, except for cash held for investment by portfolio managers.

Comparative Information – The financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles.

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

Estimates – Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenue and expenses.

Significant estimates used in preparing these financial statements include:

- Depreciable lives and estimated residual value of buildings, equipment and improvements
- Original cost of assets acquired before 1979
- Allocation of certain expenses by function
- Net present value of future income receivable and future annuities payable and assets held by charitable trusts
- Reserve for uncollectible pledges and grants receivable

It is at least reasonably possible that the significant estimates used will change within the next year.

NOTE 2: INVESTMENTS

Investments in marketable securities consist of the following:

	<u>Cost</u>	<u>Market</u>	<u>Unrealized Gain (Loss)</u>
Marketable investments:			
Money market funds	\$ 1,022,991	\$ 1,022,991	\$ -
Mutual funds:			
Equity	31,698,204	27,565,120	(4,133,084)
Fixed	7,629,474	7,720,239	90,765
Non-marketable investments	<u>2,652,100</u>	<u>1,482,752</u>	<u>(1,169,348)</u>
Total	<u>\$43,002,769</u>	<u>\$ 37,791,102</u>	<u>\$ (5,211,667)</u>

Investment income is comprised of the following:

Interest and dividends	\$ 827,301
Change in unrealized loss	10,197,006
Realized loss	<u>(3,716,003)</u>
	7,308,304
Less investment fees	<u>(78,555)</u>
Total return	<u>\$ 7,229,749</u>

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

All investments in marketable securities are stated at their market value and are managed and held by Common Fund, a nonprofit investment manager. Nonmarketable investments consist of a private equity fund, a hedge fund and a real estate fund. Market values for the marketable and nonmarketable investments were derived from the investment custodian.

None of the investments are held for trading purposes.

The Board of Trustees has adopted a “total return” methodology for providing operating support to the Museum’s Operating Fund. (See Note 16)

NOTE 3: GRANTS AND PLEDGES RECEIVABLE

Pledges and grants receivable represent unconditional promises to give by individuals, foundations and government agencies. Pledges and grants receivable come due as follows:

2010	\$ 201,304
2011	62,000
2012	57,000
2013	<u>1,000</u>
	<u>\$ 321,304</u>

Management believes these amounts will be fully collected and therefore no provision for uncollectible grants or pledges receivable has been made.

NOTE 4: PROPERTY HELD FOR INVESTMENT

The Museum owns donated real property in Goleta, California, which it leases to a convalescent hospital. The lease term is seventy-five years and expires in the year 2042. The current monthly rent is \$5,644 and is adjusted by the cost of living every five years. The rent received in 2009 was \$67,728.

The Museum also owns several residential units and one small office building, which are leased on a month-to-month basis.

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

NOTE 5: PROPERTY AND EQUIPMENT

The cost of land, buildings, improvements and equipment, net of accumulated depreciation and amortization at December 31, 2009 are as follows:

Land and improvements	\$ 309,388
Buildings and improvements	15,268,133
Furniture and equipment	1,726,840
Construction in progress	<u>22,786</u>
Total cost	17,327,147
Less accumulated depreciation	<u>(4,955,711)</u>
Property and equipment, net	<u>\$ 12,371,436</u>

Depreciation expense for the year ending December 31, 2009 was \$679,616.

The Museum's Ty Warner Sea Center is located on Stearns Wharf in Santa Barbara, California. The Museum leases the wharf space from the City of Santa Barbara. That lease agreement terminates on June 30, 2010 with two six years options to extend commencing July 1, 2010 and July 1, 2016 and one five year option commencing on July 1, 2022. The Museum is in the process of exercising its first option to extend the lease term to June 30, 2016.

Per the terms of this lease, the Museum pays the City of Santa Barbara 10% of the gross receipts of the Sea Center store. Payments to the City of Santa Barbara in 2009 totaled \$10,800.

NOTE 6: INTEREST IN CHARITABLE TRUSTS

The Museum has been named an irrevocable beneficiary of a number of charitable trusts.

Charitable trust agreements in which the Museum has been named as a remainder beneficiary or income beneficiary are recorded on the books of the Museum. Since the Museum is not the trustee for any of the trusts, all trusts are recorded in the year they are established as a contribution and an asset equivalent to the present value of the trust assets and estimated future income, net of the present value of estimated future payouts to the income beneficiaries. In subsequent years, any change in the present value of estimated future benefits is recorded in the Statement of Activities as a change in the value of charitable remainder trusts.

Charitable trust agreements are classified as temporarily restricted net assets unless the donor has permanently restricted the Museum's use of its interest in the asset. The assets are

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

recorded at approximate fair market value based upon the most recent tax return filed by the trust that is available to the Museum or current values provided by the trustee to the Museum. The present value of the estimated future value to be received by the Museum is calculated using the IRS annuity tables and a discount rate of 4%, based on the Museum's historic risk free rate of return.

NOTE 7: BOARD DESIGNATED FUNDS

Unrestricted Board designated funds consist of the following at December 31, 2009:

Strategic reserve	\$ 1,039,522
Specific projects	196,632
Quasi-endowment	<u>22,048,318</u>
	<u>\$ 23,284,472</u>

Quasi-endowment funds are those funds the Trustees have designated primarily for investment and include net unrealized and realized gains on the permanently restricted endowment fund. The Museum plans to leave these gains reinvested in perpetuity unless allocated for other purposes by resolution of the Board.

NOTE 8: TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets available at December 31, 2009 are restricted to the following:

For programs	\$ 6,192,792
For future periods	<u>5,313,681</u>
	<u>\$ 11,506,473</u>

NOTE 9: PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets available at December 31, 2009 are restricted for investment in perpetuity, the income from which is expendable to support:

Invertebrate Zoology – Malacology	\$ 1,000,000
Museums studies internships	100,000
Operations	<u>6,499,945</u>
	<u>\$ 7,599,945</u>

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

NOTE 10: PENSION PLAN

The Museum maintains a tax deferred annuity plan for all employees except adjunct and part-time employees. Employees are eligible for participation in the plan after one year of employment and are fully vested after participation begins. Participants are required to contribute three percent of their salaries to the plan, and the Museum contributed seven percent until June 1, 2009, after which the Museum contributed three percent. The Museum's contributions to the plan were \$104,227 in 2009. The pension is provided through the organization T.I.A.A.-C.R.E.F. which manages pension funds of private colleges, universities, museums and other such institutions nationally.

NOTE 11: CONTINGENT LIABILITIES

The Museum received grants from various governmental agencies. These grants are subject to audit by the corresponding cognizant oversight agency as to allowable costs paid with federal funds and as to the share of costs contributed by the Museum. The Museum could be liable up to the full amount of federal funds expended (approximately \$150,000) should costs charged to the project be disallowed.

NOTE 12: CONCENTRATION OF RISKS

In 2009, all of the Museum's investments were held by Common Fund. The Museum derives a significant portion of its earnings from its investments. These investments are subject to the inherent risks of inflation, default, market fluctuation, and liquidity.

At December 31, 2009, the Museum had over \$1 million on deposit in interest bearing accounts with one bank. Only deposits up to \$250,000 are federally insured.

The Museum obtains support primarily from the Santa Barbara region.

NOTE 13: STATEMENT OF CASH FLOWS – SUPPLEMENTAL DISCLOSURES

The following transactions did not affect the Museum's cash balances:

- The Museum is the remainderman of several charitable remainder trusts. The estimated future benefits to be received by the Museum when the trust assets are distributed are recorded as an asset in the financial statements and are adjusted annually to reflect changes in the fair value of the assets and the life expectancies of the recipients.
- The \$908,739 net increase in the value of the remaining trusts' assets is recorded in the financial statements, but has no effect on the amount of cash received or used during the year.

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

NOTE 14: DEFERRED MEMBERSHIP REVENUE

The Museum offers one year and two year memberships for sale. The portion of membership dues that represents an economic benefit received by the member is recognized as income as it is earned. The portion of membership dues that represents a contribution is recognized as income when received.

NOTE 15: LINE OF CREDIT

The Museum has a line of credit for \$150,000 for business needs. The line of credit was not drawn on in 2009 and has no balance outstanding as of December 31, 2009.

NOTE 16: ENDOWMENT

The Museum's endowment has been established for a variety of program purposes. Its endowment consists of donor-restricted and Board designated endowment funds. As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law - The Board of Trustees of the Museum has interpreted the State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, The Museum classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Museum in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, the Museum 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 Museum and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The long-term expected total return from income and the appreciation of investments
- (6) Other resources of the Museum

SANTA BARBARA MUSEUM OF NATURAL HISTORY
NOTES TO FINANCIAL STATEMENTS

(7) The investment policies of the Museum.

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 SPMIFA requires the Museum to retain as a fund of perpetual duration. No such deficiencies existed during the year ended December 31, 2009.

Return Objectives and Risk Parameters - The Museum has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Museum must hold in perpetuity.

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

Spending Policy and How the Investment Objectives Relate to Spending Policy - In recognition of the foundational role the endowment and quasi-endowment play in the support of the core operations of the Museum, the purpose of the spending policy is to adopt a process that will virtually assure the continued growth of support for the operations of the Museum. To that end, the Museum has adopted its "Snake in the Tunnel" withdrawal formula. Each year, the Museum may draw funds from the endowment and quasi-endowment to support the operations of the Museum. In 1998, 4.5% of a trailing 12-quarter average of the market value of the endowment corpus as of June 30 was designated for expenditure in the following calendar year. In each subsequent year, the payout increases by 4.5% a year within the limits that the payout will neither exceed 5% nor fall below 4% of a trailing 12 quarter rolling average of the endowment corpus. For the year ended December 31, 2009 the draw was 4.6% of the twelve quarter average market value as of June 30, 2008.

Endowment net asset composition by type of fund as of December 31, 2009:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Board designated endowment funds	\$ 22,048,318	--	--	\$ 22,048,318
Donor restricted endowment funds	--	\$ 5,878,118	\$ 7,599,945	<u>13,478,063</u>
Total	<u>\$ 22,048,318</u>	<u>\$ 5,878,118</u>	<u>\$ 7,599,945</u>	<u>\$ 35,526,381</u>

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Changes in endowment net assets for the year ending December 31, 2009 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 17,978,495	\$ 4,896,970	\$ 7,599,945	\$ 30,475,410
Investment earnings or losses	5,993,981	938,082	--	6,932,063
Contributions	150,682	250,200	--	400,882
Matured charitable remainder trust	912,724	--	--	912,724
Appropriation of assets for expenditure based on "draw" formula	(1,767,320)	(61,240)	--	(1,828,560)
Appropriation of assets for Strategic Reserve	(1,039,522)	--	--	(1,039,522)
Donor-restricted expenditures out of fund	--	(145,894)	--	(145,894)
Board approved transfers for other funds	(180,722)	--	--	(180,722)
 Total	 <u>\$ 22,048,318</u>	 <u>\$ 5,878,118</u>	 <u>\$ 7,599,945</u>	 <u>\$ 35,526,381</u>

NOTE 17: ASSETS VALUED AT FAIR VALUE

The Museum has adopted ASC Topic 820, Fair Value Measurements and Disclosures (ASC 820). ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements.

ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC 820 establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets or liabilities.

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Level 2: Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; discounted cash flows; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

In determining fair value, the Museum utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible as well as considers counterparty credit risk in its assessment of fair value. At December 31, 2009, the Museum held certain assets and instruments that are required to be measured at fair value on a recurring basis.

Financial assets carried at fair value as of December 31, 2009, are classified in the table below in one of the three categories described above:

	<u>Quoted Prices in Active Markets for Identical Assets</u>	<u>Significant Other Observable Inputs</u>	<u>Significant Unobservable Inputs</u>
Marketable securities held for trading purposes	\$ 8,402,853	\$ --	\$ --
Alternative investments	--	24,649,659	4,738,590
Charitable trusts	--	--	5,193,681
Total	\$ 8,402,853	\$ 24,649,659	\$ 9,932,271

NOTE 18: SUBSEQUENT EVENTS

Management has evaluated subsequent events through March 9, which is the date the financial statements were available to be issued pending final approval of the Board of Trustees. Management has determined no subsequent events requiring disclosure or significantly impacting disclosure have occurred.