



**MUSIC ACADEMY OF THE WEST**

**FINANCIAL STATEMENTS**

**December 31, 2016**



## **INDEPENDENT AUDITORS' REPORT**

To Board of Directors  
Music Academy of the West  
Santa Barbara, California

We have audited the accompanying financial statements of Music Academy of the West (a California nonprofit organization), which comprise the statement of financial position as of December 31, 2016, and the related statements of activities, net assets, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

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

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

### **Auditors' Responsibility**

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

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

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

### **Report on Summarized Comparative Information**

We have previously audited the Music Academy of the West's financial statements, and our report dated May 31, 2016, expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2015 is consistent, in all material respects, with the audited financial statements from which it has been derived.

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Music Academy of the West as of December 31, 2016, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

*Stoltey & Associates*

May 30, 2017  
Orcutt, California

**Music Academy of the West**

STATEMENT OF FINANCIAL POSITION  
Statement of Financial Position  
December 31, 2016  
(With Comparative Totals for December 31, 2015)

ASSETS

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2016</u>	<u>2015</u>
<b>CURRENT ASSETS</b>					
Cash and equivalents	\$ 6,352,834	\$ -	\$ -	\$ 6,352,834	\$ 9,485,209
Pledges receivable (Note 4)	-	4,840,675	-	4,840,675	2,313,534
Prepaid expenses and other current assets	231,425	-	-	231,425	153,225
<b>Total Current Assets</b>	<b>6,584,259</b>	<b>4,840,675</b>	<b>-</b>	<b>11,424,934</b>	<b>11,951,968</b>
 Property and equipment, net (Note 6)	 36,509,883	 -	 -	 36,509,883	 31,024,429
<b>OTHER ASSETS</b>					
Investments (Note 5)	28,405,022	4,373,373	300,000	33,078,395	32,973,433
Pledges receivable (Note 4)	-	2,441,022	-	2,441,022	4,110,234
Bequests receivable (Note 4)	-	6,066,725	-	6,066,725	6,054,648
Other investment (Note 7)	427,598	-	-	427,598	427,598
Contributions in trust (Note 8)	-	3,986,891	-	3,986,891	3,998,192
<b>Total Other Assets</b>	<b>28,832,620</b>	<b>16,868,011</b>	<b>300,000</b>	<b>46,000,631</b>	<b>47,564,105</b>
 <b>TOTAL ASSETS</b>	<b>\$ 71,926,762</b>	<b>\$ 21,708,686</b>	<b>\$ 300,000</b>	<b>\$ 93,935,448</b>	<b>\$90,540,502</b>

**MUSIC ACADEMY OF THE WEST**

Statement of Financial Position

December 31, 2016

(With Comparative Totals for December 31, 2015)

LIABILITIES AND NET ASSETS

	Unrestricted	Temporarily Restricted	Permanently Restricted	2016	2015
<b>CURRENT LIABILITIES</b>					
Accounts payable	\$ 336,902	\$ -	\$ -	\$ 336,902	\$ 464,717
Accrued expenses	191,413	-	-	191,413	186,772
Deposits	170	-	-	170	170
Deferred revenue	104,870	-	-	104,870	104,986
Current portion of long-term debt (Note 9)	<u>470,761</u>	<u>-</u>	<u>-</u>	<u>470,761</u>	<u>452,551</u>
 Total Current Liabilities	 <u>1,104,116</u>	 <u>-</u>	 <u>-</u>	 <u>1,104,116</u>	 <u>1,209,196</u>
 <b>LONG-TERM LIABILITIES</b>					
Notes payable, net of current portion (Note 9)	<u>12,646,947</u>	<u>-</u>	<u>-</u>	<u>12,646,947</u>	<u>13,105,209</u>
 Total Long-Term Liabilities	 <u>12,646,947</u>	 <u>-</u>	 <u>-</u>	 <u>12,646,947</u>	 <u>13,105,209</u>
 Total Liabilities	 <u>13,751,063</u>	 <u>-</u>	 <u>-</u>	 <u>13,751,063</u>	 <u>14,314,405</u>
 <b>NET ASSETS (Note 10)</b>					
Unrestricted	27,077,440	-	-	27,077,440	24,147,757
Unrestricted - board designated	31,098,259	-	-	31,098,259	30,714,763
Temporarily restricted	-	21,708,686	-	21,708,686	20,396,606
Permanently restricted	<u>-</u>	<u>-</u>	<u>300,000</u>	<u>300,000</u>	<u>966,971</u>
Total Net Assets	<u>58,175,699</u>	<u>21,708,686</u>	<u>300,000</u>	<u>80,184,385</u>	<u>76,226,097</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u><b>\$ 71,926,762</b></u>	<u><b>\$ 21,708,686</b></u>	<u><b>\$ 300,000</b></u>	<u><b>\$ 93,935,448</b></u>	<u><b>\$ 90,540,502</b></u>

# MUSIC ACADEMY OF THE WEST

## Statement of Activities

For the Year Ended December 31, 2016

(With Comparative Totals for December 31, 2015)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2016</u>	<u>2015</u>
<b>PUBLIC SUPPORT</b>					
Contributions (note 1)	\$ 4,130,639	\$ 5,472,759	\$ -	\$ 9,603,398	\$ 15,475,127
Concert program advertising	30,738	-	-	30,738	38,180
Other support	4,190	-	-	4,190	12,042
<b>TOTAL PUBLIC SUPPORT</b>	<u>4,165,567</u>	<u>5,472,759</u>	<u>-</u>	<u>9,638,326</u>	<u>15,525,349</u>
<b>REVENUE CENTERS</b>					
Rack and Treasure House sales	252,398	-	-	252,398	210,641
Rack and Treasure House expenses	<u>(127,721)</u>	<u>-</u>	<u>-</u>	<u>(127,721)</u>	<u>(119,884)</u>
<b>TOTAL REVENUE CENTERS</b>	<u>124,677</u>	<u>-</u>	<u>-</u>	<u>124,677</u>	<u>90,757</u>
<b>SPECIAL EVENTS</b>					
Gross revenue	906,627	2,500	-	909,127	946,259
Direct costs	<u>(261,240)</u>	<u>-</u>	<u>-</u>	<u>(261,240)</u>	<u>(330,733)</u>
<b>SPECIAL EVENTS, NET</b>	<u>645,387</u>	<u>2,500</u>	<u>-</u>	<u>647,887</u>	<u>615,526</u>
<b>REVENUE</b>					
Concerts, recitals and master classes	754,367	-	-	754,367	724,517
Fees	217,150	-	-	217,150	240,808
Rentals and miscellaneous	125,267	-	-	125,267	143,226
Gain (loss) on sale of assets	(37,231)	-	-	(37,231)	(143,226)
Other revenue	-	-	-	-	4,220
Investment income	1,446,710	-	-	1,446,710	(80,768)
<b>Total Revenue</b>	<u>2,506,263</u>	<u>-</u>	<u>-</u>	<u>2,506,263</u>	<u>888,777</u>
<b>TOTAL PUBLIC SUPPORT AND REVENUE</b>	<u>7,441,894</u>	<u>5,475,259</u>	<u>-</u>	<u>12,917,153</u>	<u>17,120,409</u>
Assets Released From Restriction	<u>4,830,150</u>	<u>(4,830,150)</u>	<u>-</u>	<u>-</u>	<u>-</u>
<b>FUNCTIONAL EXPENSES</b>					
Program Expenses:					
Summer School and Festival (note 1)	7,266,171	-	-	7,266,171	7,510,830
Supporting Services					
Management and general	695,738	-	-	695,738	707,964
Fundraising	996,956	-	-	996,956	1,019,503
<b>Total Functional Expenses</b>	<u>8,958,865</u>	<u>-</u>	<u>-</u>	<u>8,958,865</u>	<u>9,238,297</u>
<b>CHANGES IN NET ASSETS</b>	<u>\$ 3,313,179</u>	<u>\$ 645,109</u>	<u>\$ -</u>	<u>\$ 3,958,288</u>	<u>\$ 7,882,112</u>

**MUSIC ACADEMY OF THE WEST**  
**STATEMENT OF CHANGES IN NET ASSETS**  
For the Year Ended December 31, 2016  
(With Comparative Totals for 2015)

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>2016</u>	<u>2015</u>
Beginning Balance	\$ 54,862,520	\$ 20,396,606	\$ 966,971	\$ 76,226,097	\$ 68,343,985
Reclassifications		666,971	(666,971)	-	-
Changes in Net Assets	<u>3,313,179</u>	<u>645,109</u>	<u>-</u>	<u>3,958,288</u>	<u>7,882,112</u>
Ending Balance	<u>\$ 58,175,699</u>	<u>\$ 21,708,686</u>	<u>\$ 300,000</u>	<u>\$ 80,184,385</u>	<u>\$ 76,226,097</u>

## MUSIC ACADEMY OF THE WEST

### STATEMENT OF FUNCTIONAL EXPENSES

For the Year Ended December 31, 2016

(with comparative Totals for 2015)

	<b>Program Expenses</b>	<b>Management and General</b>	<b>Fundraising</b>	<b>2016 Total</b>	<b>2015 Total</b>
Salaries	\$ 1,769,103	\$ 156,756	\$ 313,512	\$ 2,239,371	\$ 1,987,592
Pension plan contributions	60,419	5,354	10,707	76,480	58,702
Other employee benefits	175,592	15,559	31,117	222,268	250,653
Payroll taxes	123,894	10,978	21,956	156,828	146,298
Fees:					
Accounting and legal	-	28,655	-	28,655	32,994
Investment	-	12,284	-	12,284	12,493
Other	309,918	18,230	36,461	364,609	370,258
Advertising and promotion	227,984	20,201	40,402	288,587	319,306
Office expenses	76,512	6,777	13,553	96,842	87,540
Information technology	113,150	10,026	20,052	143,228	148,039
Occupancy	1,319,547	77,620	155,241	1,552,408	1,640,313
Travel	228,838	20,277	40,554	289,669	303,613
Interest	392,448	34,774	69,547	496,769	514,512
Depreciation and amortization	783,319	156,664	39,166	979,149	921,312
Insurance	69,459	6,155	12,309	87,923	70,694
Festival productions	1,615,988	115,428	192,379	1,923,795	2,373,978
Total Expenses	\$ 7,266,171	\$ 695,738	\$ 996,956	\$ 8,958,865	\$ 9,238,297

The accompanying notes are an integral part of these financial statements



**MUSIC ACADEMY OF THE WEST**

STATEMENT OF CASH FLOWS  
For the Year Ended December 31, 2016  
(with comparative Totals for 2015)

	<u>2016</u>	<u>2015</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in net assets	\$ 3,958,288	\$ 7,882,112
Adjustments to reconcile change in net assets to net cash provided in operating activities:		
Depreciation and amortization	979,149	921,312
Amortization of loan issuance costs	12,445	12,445
Loss (gain) on value of securities	(522,258)	992,585
Loss (gain) on sale of securities	(1,946)	(46,635)
Loss (gain) on sale of fixed assets	37,231	143,226
Loss (gain) on value of charitable trusts	11,301	293,867
(Increase) decrease in operating assets:		
Pledges and interest receivable	(870,006)	(3,737,234)
Prepaid expenses	(78,200)	(1,321)
Increase (decrease) in operating liabilities:		
Accounts payable	(127,815)	329,680
Accrued expenses	4,641	16,864
Deposits	-	(3,661)
Deferred revenue	(116)	11,956
<b>NET CASH FLOWS FROM OPERATING ACTIVITIES</b>	<u>3,402,714</u>	<u>6,815,196</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of long-term investments	(403,224)	(11,198)
Proceeds from maturity and sale of long-term investments	822,466	1,209,002
Payments for property and equipment	(6,501,834)	(1,544,559)
<b>NET CASH FROM INVESTING ACTIVITIES</b>	<u>(6,082,592)</u>	<u>(346,755)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Principal payments on notes payables	(452,497)	(437,666)
<b>NET CASH FLOWS FROM FINANCING ACTIVITIES</b>	<u>(452,497)</u>	<u>(437,666)</u>
<b>NET INCREASE IN CASH</b>	(3,132,375)	6,030,775
<b>CASH - Beginning of year</b>	<u>9,485,209</u>	<u>3,454,434</u>
End of year	<u>\$ 6,352,834</u>	<u>\$ 9,485,209</u>
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>		
Cash paid during the year for interest	<u>\$ 484,324</u>	<u>\$ 502,067</u>

## MUSIC ACADEMY OF THE WEST

### NOTES TO FINANCIAL STATEMENTS

#### Note 1 - ORGANIZATION

Founded in 1947, the Music Academy of the West (Academy) is an 8-week summer school and festival located in Santa Barbara, California. The academy provides training for exceptionally talented musicians from around the world and presents distinguished faculty and visiting artists in public master classes and performances. The festival offers more than 200 events for the community annually. More than 20 are free and open to the public.

The academy annually provides up to 140 musicians (fellows) full scholarship for the summer school and festival, including tuition, room, and board. Fellows are selected from nearly 2,000 worldwide applicants to study with eminent faculty and visiting guest artists. Fellows participate in one of five programs: instrumental (strings, woodwinds, brass, and percussion), solo piano, collaborative piano, vocal piano, and voice. The voice program, led by legendary mezzo-soprano Marilyn Horne, has been featured in a fully staged opera production presented in the community every year since 1997.

From 2014-2018, the Music Academy of the West is partnering with the New York Philharmonic to provide educational opportunities for academy fellows and concerts for the community. New York Philharmonic musicians will teach and perform during the summer festival, the New York Philharmonic performed during the 2015 festival and will return for the 2017 festival, and Academy fellows will perform in New York City with the New York Philharmonic in concert. The Academy has committed to fund this partnership which will result in increased festival production expenses that will vary year over year based on programming.

During the year ended December 31, 2015 the Academy entered into a capital campaign to fund Phase 3 of the campus renovation. As a result of the campaign the Academy received a significant increase in contributions for the renovation of the Main House and the construction of the New Teaching Studio.

Music Academy of the West alumni are members of major symphony orchestras, chamber ensembles, opera companies, and university and conservatory faculties worldwide. More than 65 alumni participate in careers with the Metropolitan Opera, LA Opera, and San Francisco Opera. The New York Philharmonic, Los Angeles Philharmonic, Chicago Symphony Orchestra, and San Francisco Symphony have a total of more than 50 Academy alumni on their current rosters. Legendary and esteemed artists including Burt Bacharach, Marilyn Horne, Thomas Hampson, Donald McInnes, Paul Schenly, and David Shifrin attended the Academy and have received its highest honor, the Distinguished Alumni Award.

#### Note 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

##### A. Basis of Accounting

The Academy follows the accrual method of accounting. It is the Academy's policy to recognize revenue when it is earned and to record expenses when incurred. Unconditional pledges and irrevocable bequests are recorded and recognized as revenue upon receipt of the promise or notification of the irrevocable bequest.

##### B. Investments

As required by generally accepted accounting principles, investments in marketable

## MUSIC ACADEMY OF THE WEST

### NOTES TO FINANCIAL STATEMENTS

securities with readily determinable fair values and all investments in marketable debt securities are valued at their fair values as of the date of the statement of financial position. Unrealized gains and losses in marketable securities are included in the change in net assets.

#### C. Pledges and Irrevocable Bequests Receivable

Unconditional pledges and irrevocable bequests receivable are recorded and recognized as revenue upon receipt of the pledge or notification of the irrevocable bequest. All pledges and irrevocable bequests receivable due in more than one year have been recorded at present value using a discount rate of 2.5%.

#### D. Property and Equipment

Land, building and equipment are recorded at cost or, if donated, at fair market value at the time of the donation. Such donations are reported as unrestricted support unless the donor has restricted the donated asset to a specified purpose. Absent donor stipulations regarding how long donated assets must be maintained, the Academy reports expirations of donor restrictions when the donated or acquired assets are placed in service as instructed by the donor. The Academy reclassifies temporarily restricted net assets to unrestricted net assets at that time. The Academy has implemented a capitalization threshold of \$2,500.

Depreciation is computed using the straight-line method over the useful lives of the related assets. Buildings and artwork are depreciated over 50 years. Musical equipment and library texts are depreciated over twenty-five years, and the remaining assets are depreciated over five years.

#### E. Fair Value of Financial Instruments

The estimated fair values of the Academy's short-term financial instruments, including cash, cash equivalents, and accounts payables arising in the ordinary course of business, approximate their individual carrying amounts due to the relatively short period of time between their origination and expected realization. The fair value of the marketable securities is based on quoted market rates. The fair value of investments determined by estimated net asset value is determined by the estimated value of the underlying assets held by the investment fund.

#### F. Donated Services

During the year ended December 31, 2016, numerous volunteers donated their time and services. The donated services were not recognized in the financial statements because they do not meet the criteria for recognition under generally accepted accounting principles.

#### G. Use of Contributions

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset classes. However, if a restriction is fulfilled in the same time period in which the contribution is received, the

# MUSIC ACADEMY OF THE WEST

## NOTES TO FINANCIAL STATEMENTS

Academy reports the support as unrestricted.

### H. Functional Expenses

The Academy allocates its expenses on a functional basis among its various programs and support services. Expenses that can be identified with a specific program and support service are allocated directly according to their natural expenditure classification. The Academy's policy is for the management and general functional expense category to be used for expenses that can't be directly allocated to other functional expense categories.

### I. Cash and Cash Equivalents

For the purpose of statement of the cash flows, the Academy considers all short-term investments with an original maturity of three months or less to be cash equivalents.

### J. 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 certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

### K. Income Taxes

The Academy is exempt from income taxes under Internal Revenue Code section 501(c)(3), however income tax is imposed on income from a business enterprise of a non-profit organization that is not related to its tax-exempt status. There is no tax for the year ended December 31, 2016. As a California nonprofit school, the Academy is exempt from state income taxes. Contributions to the Academy are deductible by the donors as provided by the Internal Revenue Code. The Academy is not considered a private foundation.

### L. Comparative Amounts

The amounts shown for 2015 in the accompanying financial statements are included to provide a basis for comparison with 2016 and are not intended to present all information necessary for a fair presentation of the 2015 financial statements in conformity with generally accepted accounting principles.

Certain amounts in the 2015 financial statements have been reclassified to conform to 2016 financial statement presentation.

### M. Advertising Costs

The Organization uses advertising to promote its programs among the audiences it serves. Advertising costs are expensed as incurred. Advertising expense for the year ended December 31, 2016 was \$107,793.

MUSIC ACADEMY OF THE WEST

NOTES TO FINANCIAL STATEMENTS

Note 3 - CONCENTRATION OF RISK

Credit Risk

Financial instruments that potentially subject the Academy to concentrations of credit risk consist principally of cash equivalents, marketable securities, short-term deposits, pledges receivable and bequests receivable. The Academy places its cash equivalents and short-term deposits with two high-quality financial institutions. The Academy's donor base consists of a large number of diverse donors.

The FDIC insures deposits according to the ownership category in which funds are insured and how the accounts are titled. The standard deposit insurance coverage limit is \$250,000 per depositor, per FDIC-insured bank, per ownership category. Deposits held in different ownership categories are separately insured, up to at least \$250,000, even if held at the same bank. At December 31, 2016 the Academy held approximately \$5,200,000 of uninsured cash deposits.

Geographic Risk

The Academy historically has derived a large percentage of its donations from individuals, foundations and companies in Southern California, principally in Southern Santa Barbara County.

Note 4 - PLEDGES AND BEQUESTS RECEIVABLE

*Pledges Receivable - Unconditional*

The collection schedule of non-current pledges receivable is as follows:

Year ending December 31:	
2017	\$ 4,840,675
2018	1,256,501
2019	800,000
2020	377,953
2021	15,000
Thereafter	<u>190,000</u>
Total pledges receivable	7,480,129
Less allowance for uncollectible Pledges receivable	(2,140)
Less present value discount	<u>(196,292)</u>
Total Pledges Receivable	<u>\$ 7,281,697</u>

**MUSIC ACADEMY OF THE WEST**  
NOTES TO FINANCIAL STATEMENTS

*Bequests Receivable – Unconditional and Irrevocable*

The collection schedule of non-current bequests receivable is as follows:

Year ending December 31:	
2017	\$ -
2018	500,000
2019	3,100,000
2020	1,100,000
2021	-
Thereafter	<u>2,150,000</u>
Total bequests receivable	6,850,000
Less present value discount	<u>(783,275)</u>
Total Bequests Receivable	<u>\$ 6,066,725</u>

*Pledges Receivable – Conditional and Revocable*

The Academy has been named as a beneficiary of the Estate of Sima Mannick. In accordance with the last will and testament of Mrs. Mannick, the Academy will receive annually an amount equivalent to the Academy’s cost of two students’ attendance. The funds to pay the tuition will be paid from the income of an endowment trust set up at the University of Southern California. The value of the pledge can be revoked and as such has not been recorded in the accompanying financial statements.

On September 1, 1990, the Ridley - Tree Foundation set up a scholarship fund of \$50,000 in the name of the Academy. The Ridley - Tree Foundation has subsequently added an additional \$275,000 to the original contribution amount. The earnings of the fund are paid to the Academy semiannually. Due to the revocable nature of the arrangement the principal amount held by Paine Webber has not been recorded as an asset of the Academy, nor has the principal been recorded as a contribution to the Academy.

Note 5 - INVESTMENTS

*Investments Reported at Fair Value*

Investments considered to be marketable securities are presented in the financial statements at estimated fair market value derived from estimated net asset value per share.

**MUSIC ACADEMY OF THE WEST**  
NOTES TO FINANCIAL STATEMENTS

At December 31, 2016 marketable securities consisted of the following:

	<u>Cost</u>	<u>Market Value</u>	<u>Excess of Market over Cost</u>
Mutual funds – balanced	\$ 20,889,685	\$ 17,637,229	\$ (3,252,456)
Funds - other	<u>13,804,738</u>	<u>15,441,166</u>	<u>1,636,428</u>
Total	<u>\$ 34,694,423</u>	<u>\$ 33,078,395</u>	<u>\$ (1,616,028)</u>

*Investment Income*

Investment income is summarized as follows:

Interest and dividend income	\$ 922,506
Realized gain on securities	1,946
Unrealized loss on securities	<u>522,258</u>
Total	<u>\$ 1,446,710</u>

Note 6 - PROPERTY AND EQUIPMENT

A summary of land, building and equipment as of December 31, 2016, is as follows:

Land and improvements	\$ 421,077
Buildings	38,125,038
Furniture, fixtures and equipment	1,304,190
Construction in process	1,373,720
Library text and music	18,612
Instruments	2,530,334
Vehicles	<u>43,153</u>
	43,816,124
Less accumulated depreciation	<u>(7,306,241)</u>
Net Property and Equipment	<u>\$ 36,509,883</u>

Depreciation expense for the year ended December 31, 2016 totaled \$979,149. Construction in process consists of costs associated with the renovation of the “Hind Hall” located on the Academy’s campus. Construction in process is not subject to depreciation until placed into service.

Note 7 - OTHER INVESTMENT

The Academy is the beneficiary of a second trust deed, of \$427,598, secured by real property located in Santa Barbara, California. As stated in the second trust deed, there is no interest charged on the principal and the Academy will share in the appreciation of the real property upon sale in the future.

## MUSIC ACADEMY OF THE WEST

### NOTES TO FINANCIAL STATEMENTS

#### Note 8 - CONTRIBUTIONS IN TRUST

During the year ended September 30, 1991, a pooled income trust fund was established. The present value of the trust as of the date of the contribution was \$4,444. At December 31, 2016, the fair market value of the Academy's share of trust assets was \$55,380. These assets are recorded as temporarily restricted assets.

During the year ended December 31, 2005, the Academy was named as a 20% beneficiary of the Maximus Fund to be held by the Santa Barbara Foundation. The Academy is to receive an annual payment equal to 5% of the fund's fair market value as determined on January 1 of each year. The estimated fair market value of the gift has been determined to equal the underlying assets at the time of the gift. The Academy has recorded the gift as an increase to temporarily restricted net assets. The Academy's share of the net assets of the fund at December 31, 2016 was \$2,503,410.

During the year ended December 31, 2012, the Academy was named as a 20% beneficiary of the Thomas E & Elenor H. Hugunin Endowment Fund to be held by the Santa Barbara Foundation. The Academy is to receive an annual payment equal to 5% of the fund's fair market value as determined on January 1 of each year. The estimated fair market value of the gift has been determined to equal the underlying assets at the time of the gift. The Academy has recorded the gift as an increase to temporarily restricted net assets. The Academy's share of the net assets of the fund at December 31, 2016 was \$1,428,101.

For the year ended December 31, 2016, the Academy reported a decrease in value in the value of contributions in trust of \$11,301 as part of contributions.

#### Note 9 - NOTE PAYABLE

In September 2012, the Academy entered into a note payable agreement with First Republic Bank. Under the agreement the Academy borrowed \$15,200,000. The note payable bears interest at 3.65% per annum, is to be repaid with monthly principal and interest payments of \$79,221 and matures in September 2036. In connection with the note payable, the Academy incurred \$298,661 of issuance costs which are being amortized over the life of the note. At December 31, 2016 the Academy reported unamortized loan issuance costs of \$245,255. The proceeds of the note were used to retire \$14,884,925 of certificates of participation. The note payable is secured by a lien on all of the Academy's assets other than its real property and permanently restricted assets. The note requires the Academy to maintain liquidity of \$14,000,000.



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Minimum maturities of the note payable are as follows:

2017		\$ 470,761
2018		488,234
2019		506,355
2020		523,935
2021		544,597
Thereafter		<u>10,829,081</u>
Total minimum maturities		13,362,963
Less unamortized debt issuance costs		<u>(245,255)</u>
Note payable, net		<u>\$ 13,117,708</u>

In prior years the Academy reported debt issuance costs as a deferred charge in the statement of financial position and amortization of such costs in the statement of activities as interest expense. To comply new generally accepted accounting principle presentation requirements, in 2016 the Academy began reporting such costs as direct deduction from the face amount of the related debt (as shown in the table above). The Academy reclassified the unamortized debt issuance costs at December 31, 2015 to be comparable to the 2016 presentation. The reclassification of the 2015 amount resulted in a reduction of 2015 assets of \$257,700.

The Academy continues to report amortization of the debt issuance costs (\$12,500 in 2016) as interest expense.

Note 10 - DESIGNATIONS AND RESTRICTIONS OF NET ASSETS

*Board Designated Funds*

Board designated funds include amounts placed into the Academy's endowment fund for the following purposes:

Loan repayment		\$ 4,832,858
Future operations		<u>26,265,401</u>
		<u>\$ 31,098,259</u>

*Temporarily Restricted Funds*

Temporarily restricted net assets represent donor restrictions for which the restriction has not been met at December 31, 2016. Temporary restricted net assets as of December 31, 2016 consist of the following:

Campus renovation plan		\$ 6,918,259
Artistic Initiative fund		1,425,150
Building maintenance		1,820,342
Various program activities		416,500
Time restricted		<u>11,128,435</u>
		<u>\$ 21,708,686</u>

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*Permanently Restricted Funds*

Permanently restricted net assets consist of bequests receivable and contributions to be held indefinitely of which the income is restricted for the purpose of scholarships.

Note 11 – ASSETS VALUED AT FAIR VALUE

Fair value for mutual funds other is measured using the net asset value per share held at December 31, 2016.

Fair value for the contribution receivable from the beneficial interest in perpetual trusts is measured using the fair value of the assets held in the trust as reported by the trustee as of December 31, 2016. The Academy considers the measurement of its beneficial interest in the trusts to be a Level 3 measurement within the fair value hierarchy because even though that measurement is based on the unadjusted fair values of the trust assets reported by the trustee, the Academy will never receive those assets or have the ability to direct the trustee to redeem them.

The Academy recognizes transfers in between levels in the fair value hierarchy at the end of the reporting period. There were no transfers between the levels in the fair value hierarchy during the year ended December 31, 2016.

Fair Value Measurements at December 31, 2016 are summarized as follows:

	Quoted Prices In Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<i>Recurring fair value measurements:</i>			
Mutual funds:			
Balanced income	\$ 17,637,229	\$ -	\$ -
Other funds	<u>-</u>	<u>15,441,166</u>	<u>-</u>
Total investments	17,637,229	15,441,166	-
Beneficial Interest in perpetual trust	<u>-</u>	<u>-</u>	<u>3,986,891</u>
Total	<u>\$ 17,637,229</u>	<u>\$ 15,441,166</u>	<u>\$ 3,986,891</u>

## MUSIC ACADEMY OF THE WEST

### NOTES TO FINANCIAL STATEMENTS

The table below presents information about fair value measurements that use significant unobservable inputs (level 3):

#### Beneficial interest in perpetual trust

Balance at December 31, 2015	\$ 3,998,192
Additional beneficial interest received	-
Total Gains(Losses) Included In Changes in Net Assets	<u>(11,301)</u>
Balance at December 31, 2016	<u>\$ 3,986,891</u>

#### Note 12 - ENDOWMENT

The Academy's endowment has been established for general operating purposes, building maintenance and loan repayment. Its endowment consists exclusively of board designated endowment funds. As required by generally accepted accounting principles (GAAP), net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

#### **Interpretation of Relevant Law**

The Board of Directors of the Academy 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 Academy 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 organization in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, the organization 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 Academy and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The expected total return from income and the appreciation of investments
- (6) Other resources of the Academy
- (7) The investment policies of the Academy.

**MUSIC ACADEMY OF THE WEST**

NOTES TO FINANCIAL STATEMENTS

Endowment net asset composition by type of fund as of December 31, 2016:

<b>Unrestricted (Designated)</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
<u>\$ 31,098,259</u>	<u>\$ 2,042,624</u>	<u>\$ 300,000</u>	<u>\$33,440,883</u>

Changes in endowment net assets for the fiscal year ended December 31, 2016 are as follows:

	<b>Unrestricted (Designated)</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Endowment net assets, beginning of year	\$ 30,714,763	\$ 1,958,670	\$ 300,000	\$ 32,973,433
Contributions	316,250	15,000	-	331,250
Investment Income	1,299,624	96,324	-	1,395,948
Expenditures:				
Loan Repayment	(10,661)	-	-	(10,661)
Programs	(1,228,803)	(8,000)	-	(1,236,803)
Investment Expenses	(11,501)	(783)	-	(12,284)
Reclassifications	<u>18,587</u>	<u>(18,587)</u>	<u>-</u>	<u>-</u>
Endowment net assets, ending of year	<u>\$ 31,098,259</u>	<u>\$ 2,042,624</u>	<u>\$ 300,000</u>	<u>\$ 33,440,883</u>

**Funds with Deficiencies**

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or SPMIFA requires the Academy to retain as a fund of perpetual duration. No such deficiencies existed at December 31, 2016.

**Return Objectives and Risk Parameters**

The Academy 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 Academy must hold in perpetuity.

**Strategies Employed for Achieving Objectives**

To satisfy its long-term rate-of-return objectives, The Academy 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 Academy targets a diversified asset allocation that places a greater emphasis on alternative investments and equity mutual funds investments to achieve its long-term return objectives within prudent risk constraints.

MUSIC ACADEMY OF THE WEST

NOTES TO FINANCIAL STATEMENTS

**Spending Policy**

The Academy has adopted a spending policy which allows expenditures equal to 4.75% of the five year endowment average balance.

Note 13 - RETIREMENT PLAN

In 2001, the Academy adopted The Music Academy of the West Tax-Deferred Annuity Plan under section 403(b) of the Internal Revenue Code. Eligible employees are at minimum twenty-one years of age, have completed one year of service, and work full time. The Academy matches employee contributions 100% for the first 5% of deferred salary. Retirement plan contributions and operating expenses for the year ended December 31, 2016 was \$76,839.

Note 14 - COMMITMENTS

*Operating Leases*

The Academy leases a private residence located in Santa Barbara, Californian in which the Academy's President and CEO is required to reside under his employment contract. The lease expires June 30, 2017 and requires monthly payments of \$3,500. The Academy considers the lease to be an operating lease.

*Contracts*

On March 26, 2016, the Academy entered into a contract with the New York Philharmonic (Philharmonic) for years 2016 to 2017 where the Philharmonic has agreed to perform up to two concerts as the Academy's guest orchestra in 2016 and 2017. In addition, the Philharmonic will offer a guest conductor for the Academy's festival and provide the opportunity for 10 Academy fellows to train with the Philharmonic in New York City.

For the year ending December 31, 2017, the contract obligates the Academy to pay the Philharmonic a residency and expense fee according the following schedule:

2017	\$725,000
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The Academy has begun the development phase for the renovation of multiple teaching studios to be named "Hind Hall." Hind Hall began construction in August of 2016 and is scheduled to be completed in July 2017. For the project the Academy has entered in various architectural, consulting and construction contracts totaling \$5,825,000.

*Line of Credit*

The Academy has available a bank line of credit for any amount up to \$1,500,000 at December 31, 2016. The line of credit is secured by a lien on all of the Academy's assets other than its real property and permanently restricted assets. Draws on the line of credit bear interest at 3.25%. The Academy did not draw on the line during the year ended December 31, 2016. The line of credit expires June 30, 2017. The Academy plans to renew the line of credit upon expiration.

**MUSIC ACADEMY OF THE WEST**

**NOTES TO FINANCIAL STATEMENTS**

**Note 15 - SUBSEQUENT EVENTS**

Management has evaluated events through May 30, 2017, which is the date the financial statements were available to be issued. Management has determined that no subsequent event requiring disclosure or significantly impacting disclosure has occurred.