

THE MARINERS' MUSEUM

FINANCIAL REPORT

September 30, 2019 and 2018

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INDEPENDENT AUDITOR'S REPORT

Board of Trustees
The Mariners' Museum
Newport News, Virginia

We have audited the accompanying financial statements of The Mariners' Museum, which comprise the statements of financial position as of September 30, 2019 and 2018, and the related statements of activities and cash flows for the years then ended and the statement of functional expenses for the year ended September 30, 2019, 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.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Mariners' Museum as of September 30, 2019 and 2018, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Change in accounting principle

As discussed in Note 2 to the financial statements, The Mariners' Museum adopted FASB ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities* in 2019. Our opinion is not modified with respect to this matter.

Brown, Edwards & Company, S. L. P.

CERTIFIED PUBLIC ACCOUNTANTS

Newport News, Virginia
February 24, 2020

THE MARINERS' MUSEUM

STATEMENTS OF FINANCIAL POSITION

September 30, 2019 and 2018

	2019	2018
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents, operating accounts	\$ 2,300	\$ 129,079
Accounts receivable - other	39,269	52,396
Grants receivable	7,469	7,469
Current portion of pledges receivable (Note 4)	147,694	122,488
Inventories (Note 2)	139,104	152,465
Other current assets	89,570	99,485
	425,406	563,382
PROPERTY AND EQUIPMENT, net (Note 6)	25,382,231	26,094,100
OTHER ASSETS		
Pledges receivable, less current portion (Note 4)	821,974	1,118,889
Investments		
Cash and cash equivalents, investment accounts (Note 5)	986,906	1,290,641
Investments (Note 5)	13,737,877	16,144,795
Beneficial interest in trusts (Note 7)	90,938,703	92,793,341
	106,485,460	111,347,666
	\$ 132,293,097	\$ 138,005,148
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 142,448	\$ 186,011
Checks written in excess of cash	27,145	-
Accrued expenses	426,964	423,992
Current portion of bond payable (Note 11)	960,000	960,000
	1,556,557	1,570,003
LONG-TERM LIABILITIES		
Charitable gift annuities (Note 9)	41,584	36,441
Deferred revenue (Note 10)	3,279,580	3,381,041
Bond payable, less current portion (Note 11)	6,720,000	7,680,000
	11,597,721	12,667,485

The Notes to Financial Statements are an integral part of these statements.

THE MARINERS' MUSEUM

STATEMENTS OF FINANCIAL POSITION
September 30, 2019 and 2018

(Continued)

	<u>2019</u>	<u>2018</u>
NET ASSETS		
Without donor restrictions:		
Undesignated	\$ 16,064,401	\$ 16,750,004
Board designated (Note 15)	10,870,448	13,362,730
	<u>26,934,849</u>	<u>30,112,734</u>
Total net assets without donor restrictions		
With donor restrictions:		
Restricted by purpose (Note 14)	1,615,433	2,007,337
Restricted by perpetuity (Note 14)	92,145,094	93,217,592
	<u>93,760,527</u>	<u>95,224,929</u>
Total net asset with donor restrictions		
Total net assets	<u>120,695,376</u>	<u>125,337,663</u>
	<u>\$ 132,293,097</u>	<u>\$ 138,005,148</u>

The Notes to Financial Statements are an integral part of these statements.

THE MARINERS' MUSEUM

STATEMENT OF ACTIVITIES

Year Ended September 30, 2019

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
OPERATING REVENUES			
Income from funds held in trust by others	\$ 4,354,973	\$ -	\$ 4,354,973
Realized and unrealized gains on investments, net	91,852	(1,854,641)	(1,762,789)
Contributions	705,889	661,112	1,367,001
Dividend and interest income, net	364,376	64,023	428,399
Contracts	250,000		250,000
Admission fees	199,622	-	199,622
Museum shop	171,488	-	171,488
Lease	171,234	-	171,234
Facility rental	147,404	-	147,404
Miscellaneous	146,014	(4,489)	141,525
Education program fees	39,282	-	39,282
Photography	30,416	-	30,416
Deaccession	1,881	-	1,881
Net assets released from restrictions	<u>330,407</u>	<u>(330,407)</u>	<u>-</u>
 Total revenue, gains and support	 <u>7,004,838</u>	 <u>(1,464,402)</u>	 <u>5,540,436</u>
PROGRAM EXPENSES			
Exhibitions	2,065,119	-	2,065,119
Programs	2,428,788	-	2,428,788
Research	1,984,968	-	1,984,968
Conservation	<u>2,263,539</u>	<u>-</u>	<u>2,263,539</u>
 Total program expenses	 <u>8,742,414</u>	 <u>-</u>	 <u>8,742,414</u>
SUPPORTING EXPENSES			
Fundraising expenses	663,593	-	663,593
Management and general	<u>776,716</u>	<u>-</u>	<u>776,716</u>
 Total supporting expenses	 <u>1,440,309</u>	 <u>-</u>	 <u>1,440,309</u>
 Total expenses	 <u>10,182,723</u>	 <u>-</u>	 <u>10,182,723</u>
 Change in net assets	 (3,177,885)	 (1,464,402)	 (4,642,287)
Net assets, beginning of year	<u>30,112,734</u>	<u>95,224,929</u>	<u>125,337,663</u>
 Net assets, end of year	 <u>\$ 26,934,849</u>	 <u>\$ 93,760,527</u>	 <u>\$ 120,695,376</u>

The Notes to Financial Statements are an integral part of these statements.

THE MARINERS' MUSEUM

STATEMENT OF ACTIVITIES

Year Ended September 30, 2018

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
OPERATING REVENUES			
Income from funds held in trust by others	\$ 4,310,776	\$ -	\$ 4,310,776
Lease	3,314,070	-	3,314,070
Realized and unrealized gains on investments, net	599,643	1,605,219	2,204,862
Contributions	1,569,563	442,095	2,011,658
Dividend and interest income, net	457,773	68,733	526,506
Admission fees	310,466	-	310,466
Contracts	250,000	-	250,000
Museum shop	181,228	-	181,228
Facility rental	149,157	-	149,157
Miscellaneous	101,883	8,821	110,704
Grants	61,467	46,744	108,211
Education program fees	78,577	-	78,577
Photography	23,762	-	23,762
Deaccession	7,077	-	7,077
Net assets released from restrictions	<u>276,033</u>	<u>(276,033)</u>	<u>-</u>
 Total revenue, gains and support	 <u>11,691,475</u>	 <u>1,895,579</u>	 <u>13,587,054</u>
 PROGRAM EXPENSES			
Exhibitions	2,416,793	-	2,416,793
Programs	1,980,574	-	1,980,574
Research	2,233,813	-	2,233,813
Conservation	<u>2,276,189</u>	<u>-</u>	<u>2,276,189</u>
 Total program expenses	 <u>8,907,369</u>	 <u>-</u>	 <u>8,907,369</u>
 SUPPORTING EXPENSES			
Fundraising expenses	682,665	-	682,665
Management and general	<u>809,001</u>	<u>-</u>	<u>809,001</u>
 Total supporting expenses	 <u>1,491,666</u>	 <u>-</u>	 <u>1,491,666</u>
 Total expenses	 <u>10,399,035</u>	 <u>-</u>	 <u>10,399,035</u>
 Change in net assets	 1,292,440	 1,895,579	 3,188,019
Net assets, beginning of year	<u>28,820,294</u>	<u>93,329,350</u>	<u>122,149,644</u>
 Net assets, end of year	 <u>\$ 30,112,734</u>	 <u>\$ 95,224,929</u>	 <u>\$ 125,337,663</u>

The Notes to Financial Statements are an integral part of these statements.

THE MARINERS' MUSEUM
STATEMENT OF FUNCTIONAL EXPENSES
Year Ended September 30, 2019

	<u>Program Services</u>				<u>Supporting Services</u>				
	<u>Exhibitions</u>	<u>Programs</u>	<u>Research</u>	<u>Conservation</u>	<u>Total Program Services</u>	<u>General and Administrative</u>	<u>Fundraising</u>	<u>Total Supporting Services</u>	<u>Total</u>
EXPENSES									
Salaries and wages	\$ 891,744	\$ 1,080,564	\$ 806,846	\$ 1,059,818	\$ 3,838,972	\$ 211,345	\$ 468,636	\$ 679,981	\$ 4,518,953
Depreciation	346,939	346,939	346,939	346,939	1,387,756	346,940	-	346,940	1,734,696
Employee benefits	202,704	243,359	184,318	238,922	869,303	50,733	101,525	152,258	1,021,561
Occupancy	169,512	155,874	156,933	161,972	644,291	77,419	7,038	84,457	728,748
Repair and maintenance	115,079	114,355	129,007	146,756	505,197	41,732	3,794	45,526	550,723
Interest	64,096	64,096	64,096	64,096	256,384	-	-	-	256,384
Advertising	57,392	69,061	52,162	56,870	235,485	106	4,716	4,822	240,307
Outside services	43,527	99,226	40,591	35,379	218,723	10,429	948	11,377	230,100
Supplies	18,878	108,225	38,845	23,700	189,648	5,323	24,007	29,330	218,978
Other	50,361	27,248	85,771	32,208	195,588	1,495	8,585	10,080	205,668
Insurance	41,563	41,563	41,563	41,563	166,252	20,782	1,889	22,671	188,923
Event costs	17,699	13,436	12,069	32,148	75,352	1,216	9,804	11,020	86,372
Staff training/travel	3,970	44,958	3,928	5,647	58,503	3,326	12,949	16,275	74,778
Dues and licenses	26,150	7,785	7,448	6,929	48,312	3,733	6,679	10,412	58,724
Bank service charges	12,690	9,793	11,139	9,428	43,050	1,811	3,903	5,714	48,764
Postage and shipping	2,815	2,306	3,313	1,164	9,598	326	9,120	9,446	19,044
	<u>\$2,065,119</u>	<u>\$2,428,788</u>	<u>\$1,984,968</u>	<u>\$ 2,263,539</u>	<u>\$ 8,742,414</u>	<u>\$ 776,716</u>	<u>\$ 663,593</u>	<u>\$ 1,440,309</u>	<u>\$10,182,723</u>

The Notes to Financial Statements are an integral part of this statement.

THE MARINERS' MUSEUM

STATEMENTS OF CASH FLOWS
Years Ended September 30, 2019 and 2018

	2019	2018
OPERATING ACTIVITIES		
Change in net assets	\$ (4,642,287)	\$ 3,188,019
Adjustments to reconcile change in net assets to net cash used by operating activities:		
Depreciation	1,734,696	1,721,906
Unrealized gains on investments:		
Funds held in trust by others	1,854,641	(1,605,219)
Investments	(91,852)	(599,643)
Contributions for endowment	(206,484)	(100)
Contributions for property and equipment	(203,475)	(287,288)
Change in valuation of charitable gift annuities	24,619	9,384
Loss on disposal of asset	23,606	57,079
Change in assets and liabilities:		
Accounts receivable - other	13,127	(29,213)
Pledges receivable	271,709	(615,147)
Inventories	13,361	(41,819)
Other current assets	9,915	47,188
Accounts payable	(43,563)	51,278
Accrued expenses	2,972	(8,329)
Deferred revenue	(101,461)	(3,227,492)
Net cash used by operating activities	(1,340,476)	(1,339,396)
INVESTING ACTIVITIES		
Property and equipment acquisitions	(1,046,432)	(1,256,856)
Sales and maturities of investments	10,321,023	5,503,666
Purchases of investments	(7,822,258)	(2,341,021)
Net cash provided by investing activities	1,452,333	1,905,789
FINANCING ACTIVITIES		
Payments on long-term debt	(960,000)	(960,000)
Payments on charitable gift annuities	(19,475)	(19,475)
Proceeds from contributions for endowment	206,484	100
Proceeds from contributions for property and equipment	203,475	287,288
Net cash used by financing activities	(569,516)	(692,087)
Net decrease in cash and cash equivalents	(457,659)	(125,694)
CASH AND CASH EQUIVALENTS		
Beginning of year	1,419,720	1,545,414
End of year	\$ 962,061	\$ 1,419,720

The Notes to Financial Statements are an integral part of these statements.

THE MARINERS' MUSEUM

STATEMENTS OF CASH FLOWS
Years Ended September 30, 2019 and 2018

(Continued)

	<u>2019</u>	<u>2018</u>
CASH AND CASH EQUIVALENTS, end of year		
Held in operating accounts	\$ 2,300	\$ 129,079
Checks written in excess of cash	(27,145)	-
Held in investment accounts	986,906	1,290,641
	<u>962,061</u>	<u>1,419,720</u>
Cash and cash equivalents, end of year	<u>\$ 962,061</u>	<u>\$ 1,419,720</u>
SUPPLEMENTAL DISCLOSURES		
Cash paid for interest	<u>\$ 256,384</u>	<u>\$ 289,122</u>

The Notes to Financial Statements are an integral part of these statements.

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS September 30, 2019 and 2018

1. Organization and Nature of Activities

The Mariners' Museum (Museum) is a Virginia nonprofit educational and cultural institution which was incorporated in May 1930, and is located in Newport News, Virginia.

The stated mission of the Museum is “to connect people to the world’s waters, because through the world’s waters – through our shared maritime heritage – we are connected to one another.” The Museum executes on its mission through four core functions: exhibits, programs, research, and conservation. The Museum designs its activities within the four core functions to serve audiences – both in-person and virtually – from all over the world. The Museum’s Batten Conservation Complex is home to the world’s largest marine archaeological metals conservation project. The collection on which the Museum’s exhibits, programs, and research support is based includes the largest maritime library and archival collection in the Western Hemisphere and several other collection types that are generally recognized as being internationally significant. The 550-acre Mariners’ Park, 167-acre Lake Maury, and 5-mile Noland Trail comprise the campus in which the Museum sits and hosts a variety of environmental conservation activities, educational programs, and recreation and wellness activities.

2. Summary of Significant Accounting Policies

Accounting method

The financial statements of the Museum have been prepared on the accrual basis in accordance with accounting principles generally accepted in the United States of America; revenue and gains are recognized when earned, and expenses and losses are recognized when incurred. The significant accounting policies are described below to enhance the usefulness of the financial statements to the reader.

Basis of presentation

The financial statements report amounts separately by classes of net assets.

Net assets without donor restrictions are those currently available at the discretion of the Museum’s Board of Trustees for use in operations and those resources invested in property and equipment.

Net assets with donor restrictions are those which are subject to donor-imposed restrictions. Some are temporary in nature and are stipulated by donors for specific operating purposes or for the acquisition of property and equipment. Other donor-imposed restrictions are perpetual in nature, where there is a stipulation that they be invested to provide a permanent source of revenue. Such revenue is expendable in accordance with the conditions of each specific donation. When a donor restriction is satisfied, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statements of activities as net assets released from restrictions.

All contributions are considered available for unrestricted use unless specifically restricted by the donor or subject to other legal restrictions.

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS September 30, 2019 and 2018

2. Summary of Significant Accounting Policies (Continued)

Cash and cash equivalents

The Museum considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Inventories

Inventories consist of gift shop items and are stated at the lower of cost (determined using the first-in, first-out method) or net realizable value. Inventory related to the Museum Shop was \$139,104 and \$152,465 at September 30, 2019 and 2018, respectively.

Investments

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the statement of financial position. Fair value is 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. See Note 12 for discussion of fair value measurements. Investment distribution or loss (including gains and losses on investments, interest and dividends) is included in the statements of activities as increases or decreases in net assets without donor restrictions unless the income or loss is restricted by donor or law. The Museum's investments are primarily in equity and fixed income securities and investment income is reported in the accompanying statements of activities, net of investment management fees. The Museum paid management fees, primarily to JP Morgan Chase Bank, of \$287,260 and \$278,148 in 2019 and 2018, respectively.

Beneficial interest in trusts represent resources neither in the possession nor under the control of the Museum, but held and administered by outside fiscal agents, with the Museum deriving income from such funds. While the Museum does not control the trust, the chairperson of the Museum's Finance and Investment Committee serves as one of the trustees of the trust. The trusts are stated at fair value. The assets held in trust are classified as net assets with donor restrictions. The distribution received from the trusts is classified as increases in net assets without donor restrictions in the accompanying statements of activities. Unrealized gains or losses of the assets held by the trusts are reflected as a change in net assets with donor restrictions on the accompanying statements of activities.

Property and equipment

Property and equipment are stated at cost on acquisition date or fair value on gift date. Property and equipment, except land and lakes, dams and improvements, are depreciated by the straight-line method over their estimated useful lives as follows:

Building and improvements	5 - 40 years
Furniture and equipment	2 - 20 years
Land improvements	10 - 20 years
The Noland Trail	20 years

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS September 30, 2019 and 2018

2. Summary of Significant Accounting Policies (Continued)

Property and equipment (Continued)

Maintenance and ordinary repairs are expensed; improvements are capitalized. Gains and losses arising from disposal or retirement of property and equipment are recognized currently in the accompanying statements of activities and the cost and related accumulated depreciation, if applicable, are removed from the accounts. For donated capital assets, the Museum does not impose a restriction on the length of time the assets must be held. The Museum's policy is to capitalize all items with a useful life greater than three years.

Collection

The Museum maintains significant collection assets, including models, small crafts, prints, paintings, books, photographs, and navigation instruments. In accordance with industry practice, the value of the collection has been excluded from the statements of financial position. Only current year purchases and proceeds from sale are reflected in the statements of activities. It is the policy of the Museum that proceeds from the sale of any collection items are to be used to support the direct care of existing collections in addition to the acquisition of new items for the collection. The Museum presently defines direct care as the conservation or maintenance of items currently owned by the Museum either by Museum staff or by external conservators.

Pledges receivable

Pledges receivable are recognized as revenue in the period the promise is made by the donor. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved when deemed significant. An allowance for uncollectible pledges receivable is provided based upon management's judgment, including such factors as prior collection history and type of pledge.

In-kind contributions and donated services

The Museum received in-kind contributions of \$54,974 and \$36,570 in 2019 and 2018, respectively, which were not collection items. Additionally, the Museum received volunteer hours of 22,549 and 21,831 in 2019 and 2018, respectively. No amounts have been recognized in the statements of activities for donated services because the criteria for recognition under applicable accounting standards have not been satisfied.

Restricted contributions

Contributions received by the Museum with donor-imposed restrictions, which are not met within the same reporting period, are reported as net assets with donor restrictions. The revenue is then shown as released from restrictions on the accompanying statements of activities when the restriction has been satisfied. Donor-restricted contributions whose restrictions are met in the same period are reported as unrestricted support.

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS September 30, 2019 and 2018

2. Summary of Significant Accounting Policies (Continued)

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 and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and assumptions.

Method used for allocation of expenses among program and supporting services

The Museum allocates its expenses on a functional basis among its various programs and supporting services. Expenses that can be identified with a specific program or supporting service are charged directly. Other expenses that are common to several functions are allocated based on square footage of the Museum.

Advertising costs

Advertising costs are expensed as incurred and were \$240,307 and \$255,905 for 2019 and 2018, respectively. Advertising costs are included in various program and fundraising expense groupings on the statements of activities.

Income taxes

The Museum is a nonstock corporation which has been determined by the Internal Revenue Service to be exempt from taxes on income derived from activities related to its exempt purpose under Section 501(c)(3) of the Internal Revenue Code. The Museum is subject to income taxes on profits, if any, generated from the sale of items in its gift shop which are unrelated to its exempt purpose. The Internal Revenue Service has also determined that the Museum is not a private foundation under Section 509(a)(1).

Credit risk

Financial instruments that potentially expose the Museum to concentrations of credit risk consist primarily of cash and cash equivalents and investments. Cash and cash equivalents and investments are maintained at high quality financial institutions. At September 30, 2019 and 2018, the Museum had approximately \$736,000 and \$1,040,000, respectively, of cash and cash equivalents on deposit with financial institutions in excess of the Federal Deposit Insurance Corporation (FDIC) limit, most of which was held in the investment accounts.

Adoption of accounting pronouncement

In August 2016, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities: Topic 958*. The amendments in this ASU affect not-for-profit entities and the users of their general purpose financial statements. In addition to changes in terminology used to describe categories of net assets throughout the financial statements, a new statement of functional expenses, and new disclosures were added regarding liquidity and availability of resources. The Museum adopted this ASU retrospectively during 2019. Total net assets was not impacted as a result. As allowed by the ASU, the statement of functional expenses and the disclosure regarding liquidity and availability are only for 2019, the year of implementation.

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS
September 30, 2019 and 2018

2. Summary of Significant Accounting Policies (Continued)

A recap of the net asset reclassifications driven by the adoption of ASU 2016-14 as of September 30, 2018, is as follows:

	ASU 2016-14 Classifications		
	Without Donor Restrictions	With Donor Restrictions	Total Net Assets
As previously presented			
Unrestricted	\$ 30,112,734	\$ -	\$ 30,112,734
Temporarily restricted	-	2,007,337	2,007,337
Permanently restricted	-	93,217,592	93,217,592
Total funds	\$ 30,112,734	\$ 95,224,929	\$125,337,663

Reclassifications

Certain reclassifications have been made to the 2018 financial statements to conform to the 2019 financial statement presentation. Total net assets and change in net assets are unchanged due to these reclassifications.

Subsequent events

In preparing these financial statements, the Museum has evaluated events and transactions for potential recognition or disclosure through February 24, 2020, the date the financial statements were available to be issued.

3. Liquidity and Availability

As part of its liquidity management, the Museum utilizes the earnings from its investment funds to make bond payments and fund plant and equipment costs (both capital expenditures and operating expenditures) designated by the Board. Operations are also funded by the annual draw from a portion of the beneficial interest in trusts.

Financial assets available for general expenditure without donor or other restrictions limiting their use, within one year of the balance sheet date, comprise the following:

Cash and cash equivalents, not restricted by donor with purpose restrictions	\$ 495,082
Accounts receivable - other	39,269
Investments, not restricted in perpetuity or for purpose - board designated	2,609,092
	\$ 3,143,443

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS

September 30, 2019 and 2018

4. Pledges Receivable

The Museum records pledges receivable as income in the year the promise is received. Pledges receivable include the following:

	<u>2019</u>	<u>2018</u>
The Monitor Center campaign	\$ 466,455	\$ 550,000
General operating and library support	<u>503,213</u>	<u>691,377</u>
	<u>\$ 969,668</u>	<u>\$ 1,241,377</u>

The anticipated cash flows from pledges receivable is as follows:

	<u>2019</u>	<u>2018</u>
Receivable in less than one year	\$ 147,694	\$ 122,488
Receivable in one to five years	<u>971,974</u>	<u>1,268,889</u>
Total pledges receivable	1,119,668	1,391,377
Allowance for uncollectible pledges	<u>(150,000)</u>	<u>(150,000)</u>
	969,668	1,241,377
Current portion	<u>(147,694)</u>	<u>(122,488)</u>
	<u>\$ 821,974</u>	<u>\$ 1,118,889</u>

5. Investments

Investments are presented at fair value and consist of the following:

	<u>2019</u>	<u>2018</u>
Fixed income - US bond funds	\$ 9,266,142	\$ 6,367,645
Equity securities - US large cap	2,565,984	6,113,706
Equity securities - Non US	1,197,798	2,253,555
Equity securities - US mid cap/small cap	<u>707,953</u>	<u>1,409,889</u>
	<u>\$ 13,737,877</u>	<u>\$ 16,144,795</u>

The investments are under the management of JP Morgan Chase Bank. At September 30, 2019 and 2018, \$986,906 and \$1,290,641 of cash and cash equivalents is held in the JP Morgan Chase Bank investment accounts.

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THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS
September 30, 2019 and 2018

5. Investments (Continued)

At September 30, 2019, fair values and unrealized gains are summarized as follows:

	<u>Cost</u>	<u>Fair Value</u>	<u>Unrealized Gain</u>
JP Morgan Chase Bank	<u>\$ 12,735,273</u>	<u>\$ 13,737,877</u>	<u>\$ 1,002,604</u>

At September 30, 2018, fair values and unrealized gains are summarized as follows:

	<u>Cost</u>	<u>Fair Value</u>	<u>Unrealized Gain</u>
JP Morgan Chase Bank	<u>\$ 14,580,806</u>	<u>\$ 16,144,795</u>	<u>\$ 1,563,989</u>

6. Property and Equipment

Property and equipment consist of the following:

	<u>2019</u>	<u>2018</u>
Building and improvements	\$ 53,190,318	\$ 52,535,110
Land improvements	4,656,952	4,656,952
Furniture and equipment	7,099,736	6,923,709
The Noland Trail	2,219,802	2,219,802
Lakes, dams and improvements	<u>626,901</u>	<u>626,901</u>
	67,793,709	66,962,474
Accumulated depreciation	<u>(42,639,345)</u>	<u>(40,904,649)</u>
	25,154,364	26,057,825
Construction in progress	<u>227,867</u>	<u>36,275</u>
	<u>\$ 25,382,231</u>	<u>\$ 26,094,100</u>

Depreciation expense for 2019 and 2018 was \$1,734,696 and \$1,721,906, respectively.

7. Beneficial Interest in Trusts

The Museum is the beneficiary of various irrevocable trusts established by the Museum founder, Archer M. Huntington, which are classified as net assets with donor restrictions. The Museum receives distributions on the securities held by the trusts. These distributions are reported in the accompanying statements of activities, net of expenses and are included in income from funds held in trust by others.

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THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS

September 30, 2019 and 2018

7. Beneficial Interest in Trusts (Continued)

At September 30, 2019 and 2018, the value recorded for the beneficial interest in trusts is comprised of the following:

	<u>2019</u>	<u>2018</u>
JP Morgan Chase Bank Trust #03152009	\$ 45,387,334	\$ 46,345,835
JP Morgan Chase Bank Trust #03583005	30,831,682	31,899,511
JP Morgan Chase Bank Trust #98940006	5,495,506	5,400,880
JP Morgan Chase Bank Trust #98843002	3,633,808	3,580,381
JP Morgan Chase Bank Trust #03152306	1,490,881	1,448,929
JP Morgan Chase Bank Trust #03583302	994,568	964,925
SunTrust Bank Trust #13214200	1,920,443	1,960,021
Bank of America (formerly U.S. Trust Co. of New York #239550)	881,213	889,309
Bank of New York #676580	150,105	150,530
Bank of New York #676730	86,920	86,361
Bank of New York #676760	<u>66,243</u>	<u>66,659</u>
	<u>\$ 90,938,703</u>	<u>\$ 92,793,341</u>

The Museum and JP Morgan, as trustees, have adopted a total return policy with respect to distributions from its Huntington Trust at JP Morgan. This total return policy uses as a benchmark the rolling average value of the trusts, using the quarter end values of the preceding twelve quarters, ending with September 30 of the current year. For 2019 and 2018, the Board of Trustees requested and received a distribution of five percent (5%).

The Museum is also a co-beneficiary with three other not-for-profit organizations under the trust agreement with Bank of America (formerly U.S. Trust Co., of New York). Therefore, the amount recorded in the accompanying statement of financial position is 25% of the trust's value, which represents the Museum's share under this split-interest agreement.

8. Retirement Plan

The Museum sponsors a 403(b) Tax Deferred Retirement Plan. The Plan is a defined contribution plan covering substantially all employees. Employees may contribute to the Plan subject to the limitations imposed by the Internal Revenue Service. Effective April 1, 2017, the Museum makes an elective matching contribution tiered up to 4% of eligible compensation. The Museum contributed \$148,245 and \$136,060 to the Plan during 2019 and 2018, respectively.

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THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS

September 30, 2019 and 2018

9. Charitable Gift Annuities

The Museum holds charitable gift annuities, recognized at fair value. Upon the donor's death, the annuity becomes a part of the Museum's endowment fund, and any subsequent distribution earned is available to support Museum operations. The liability to beneficiaries was \$41,584 and \$36,441 at September 30, 2019 and 2018, respectively. The discount rate used to calculate the fair value was 4.2% for 2019 and ranged from 4.2% to 7.6% for 2018.

10. Deferred Revenue

During 2018, a lessee exercised an option to purchase the land of a previous lease agreement. The Museum recognized lease income of \$3,152,150 in 2018. The Museum deferred the principal payments and recognized them during 2018 when ownership of the land was legally transferred.

The Museum's deferred revenue consists primarily of three lease agreements for portions of the Museum's land. In connection with the first agreement, the Museum received an advance rental payment of \$5,000,000, and the lease term extends through 2061. The Museum has deferred the recognition of the amount received, and is amortizing the revenue on a straight-line basis over the lease term at an annual amount of \$69,204. The amount deferred is \$2,923,874 and \$2,993,078 at September 30, 2019 and 2018, respectively.

The second lease agreement commenced on December 1, 2010, and was for an initial term of 20 years. The rent for the initial term was \$65,000, paid upon the commencement of the lease. The lessee had two options to renew the lease for 20 years and an additional 30 years by making payments upon exercise of those options in the amount of \$25,000 and \$20,000, respectively. The lessee has chosen to exercise both options by making the payments with respect to those options. The term of the lease now ends on November 30, 2080. The Museum has deferred recognition of the amount received, and is amortizing the revenue over the lease term at the following rates, \$3,250 annually over the first 20 years, through 2030, \$1,250 annually for the next 20 years, 2030 - 2050, and \$667 annually for the final 30 years, 2050 - 2080. The deferred amount is \$81,292 and \$84,542 at September 30, 2019 and 2018, respectively.

During 2012, the Museum entered into a third lease agreement, similar to the above. The lease commenced on May 1, 2012, and was for an initial term of 18.5 years. The rent for the initial term was \$143,780, paid upon the commencement of the lease. The lessee had two options to renew the lease for 20 years and an additional 30 years by making payments upon exercise of those options in the amount of \$65,492 and \$42,650, respectively. The lessee has chosen to exercise both options by making the payments with respect to those options. The term of the lease now ends on November 30, 2080. The Museum has deferred recognition of the amount received, and is amortizing the revenue over the lease term at the following rates, \$7,772 annually over the first 18.5 years, through 2030, \$3,275 annually for the next 20 years, 2030 - 2050, and \$1,422 annually for the final 30 years, 2050 - 2080. The deferred amount is \$194,280 and \$202,052 at September 30, 2019 and 2018, respectively.

Additionally, the Museum had various deferred amounts of \$80,134 and \$101,369 at September 30, 2019 and 2018, respectively, relating to revenues for facility rental and other fees collected in advance of events at the Museum that have not taken place at year-end.

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS
September 30, 2019 and 2018

11. Bond Payable

On February 1, 2012, the Museum refinanced its bond arrangement. Under the new agreement with the Economic Development Authority of Lancaster County, Virginia, the Museum was issued a \$9,600,000 fixed rate bank qualified tax-exempt bond, which is unsecured. This new bond issue retired the previous debt. The bond had a fixed interest rate of 2.7% at September 30, 2017. In January 2018, the rate of the bond increased to 3.28%. In January 2019, the agreement was modified to reduce the interest rate to 3.18%, effective January 1, 2018. The interest paid with the increased rate was refunded to the Museum. Accrued interest on the unpaid principal balance is due monthly through April 1, 2027. The bond contains a provision that allows the interest rate to be adjusted up to take into consideration the Maximum Federal Corporate Tax Rate affecting the Lender. The Museum has been notified that the rate may be adjusted upwards in order to maintain the same after tax yield for the Lender. The Museum was in compliance or had obtained waivers for all financial covenants at September 30, 2019 and 2018. On April 1, 2018, the Museum began annual principal payments of \$960,000 which extends through April 1, 2027, when the bond is due and payable in full. Interest expense related to these bonds was \$256,384 and \$289,122 for 2019 and 2018, respectively, and is included in program expenses on the statements of activities.

Future minimum principal payments are as follows:

<u>Year Ending</u> <u>September 30,</u>	
2020	\$ 960,000
2021	960,000
2022	960,000
2023	960,000
2024	960,000
Thereafter	<u>2,880,000</u>
	<u>\$ 7,680,000</u>

The Board of Trustees has set aside investments with a value of \$6,272,156 and \$7,171,052 at 2019 and 2018, respectively, for the purpose of repaying the bond's principal as it comes due.

12. Fair Value Measurements

Accounting standards established a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy are described below:

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THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS

September 30, 2019 and 2018

12. Fair Value Measurements (Continued)

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Museum has the ability to access.

Level 2: Inputs to the valuation methodology include:

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical assets or liabilities in inactive markets;
- inputs other than quoted prices that are observable for the asset or liability;
- inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

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

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at September 30, 2019 and 2018.

Equity securities: Valued at the closing price reported on the active market on which the equity securities are traded.

Fixed income securities: Valued by a computerized pricing service or, for less actively traded issues, by utilizing a yield-based matrix system to arrive at an estimated fair value at year end.

Pledges receivable: Pledges receivable are reported at net realizable value if at the time the promise is made payment is expected to be received in one year or less. Pledges receivable that are expected to be collected in more than one year are reported at fair value initially and, in subsequent periods, fair value is calculated as the present value of the expected future pledges to be received using a discount rate.

Charitable gift annuities: Charitable gift annuities are valued at the discounted value of the future payments to the donor using IRS life expectancy tables.

Beneficial interest in trusts: Valued using the fair value of the underlying assets of the trust as an estimate for the present value of the expected future cash flows.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Museum believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

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THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS
September 30, 2019 and 2018

12. Fair Value Measurements (Continued)

The following sets forth by level, within the fair value hierarchy, the Museum's assets and liabilities at fair value at September 30, 2019:

	Assets at Fair Value as of September 30, 2019			
	Level 1	Level 2	Level 3	Total
Trading securities:				
Cash and cash equivalents held in investment accounts	\$ 986,906	\$ -	\$ -	\$ 986,906
Equity securities - US large cap	2,565,984	-	-	2,565,984
Equity securities - US mid/small cap	707,953	-	-	707,953
Equity securities - Non US	1,197,798	-	-	1,197,798
Fixed income securities - US bond	-	9,266,142	-	9,266,142
	5,458,641	9,266,142	-	14,724,783
Pledges receivable	-	-	969,668	969,668
Charitable gift annuities	-	-	(41,584)	(41,584)
Beneficial interest in trusts	-	-	90,938,703	90,938,703
Total assets and liabilities at fair value	<u>\$ 5,458,641</u>	<u>\$ 9,266,142</u>	<u>\$ 91,866,787</u>	<u>\$106,591,570</u>

The following sets forth by level, within the fair value hierarchy, the Museum's assets and liabilities at fair value at September 30, 2018:

	Assets at Fair Value as of September 30, 2018			
	Level 1	Level 2	Level 3	Total
Trading securities:				
Cash and cash equivalents held in investment accounts	\$ 1,290,641	\$ -	\$ -	\$ 1,290,641
Equity securities - US large cap	6,113,706	-	-	6,113,706
Equity securities - US mid/small cap	1,409,889	-	-	1,409,889
Equity securities - Non US	2,253,555	-	-	2,253,555
Fixed income securities - US bond	-	6,367,645	-	6,367,645
	11,067,791	6,367,645	-	17,435,436
Pledges receivable	-	-	1,241,377	1,241,377
Charitable gift annuities	-	-	(36,441)	(36,441)
Beneficial interest in trusts	-	-	92,793,341	92,793,341
Total assets and liabilities at fair value	<u>\$ 11,067,791</u>	<u>\$ 6,367,645</u>	<u>\$ 93,998,277</u>	<u>\$111,433,713</u>

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS

September 30, 2019 and 2018

12. Fair Value Measurements (Continued)

The table below sets forth a summary of changes in the fair value of the Museum's level 3 investment assets:

	<u>Pledges Receivable</u>	<u>Beneficial Interest in Trusts</u>
Balance - September 30, 2017	\$ 626,230	\$ 91,188,122
New pledges	1,547,758	-
Pledge collections	(922,576)	-
Pledges written off	(10,035)	-
Distributions from Trusts	-	(4,175,575)
Adjustment to fair value	-	5,780,794
Balance - September 30, 2018	1,241,377	92,793,341
New pledges	588,422	-
Pledge collections	(857,984)	-
Pledges written off	(2,147)	-
Distributions from Trusts	-	(4,221,821)
Adjustment to fair value	-	2,367,183
Balance - September 30, 2019	\$ 969,668	\$ 90,938,703

13. Donor-Designated Endowments

The Mariners' Museum Endowment (Endowment) was established to support its mission. The Endowment substantially contributes to the growth, financial security and the long-term stability of the Museum.

The Endowment consists of donor-restricted funds that are restricted for a particular purpose. With respect to these donor designated funds, the net assets associated with these endowment funds are classified and reported based on the existence of donor-imposed restrictions. 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 net assets with donor restrictions (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. 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 various funds, (2) the purposes of the donor-restricted endowment funds, (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 Museum, and (7) the Museum's investment policies.

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS
September 30, 2019 and 2018

13. Donor-Designated Endowments (Continued)

Investment Return Objectives, Risk Parameters and Strategies. The Museum has adopted investment and spending policies, approved by the Board of Trustees, for endowment assets that attempt to provide a predictable stream of distributions to programs supported by its endowment funds while also maintaining the purchasing power of those endowment assets over the long-term. Accordingly, the investment process seeks to maximize the total return of the Endowment to ensure conservation of the principal while providing appreciable yield, to the extent financially prudent and practicable. Endowment assets are invested in a well-diversified asset mix that is intended to result in a consistent inflation-protected rate of return. Generally, total return shall mean for this purpose that (1) assets are invested to achieve the highest overall return (interest, dividends, and realized as well as unrealized appreciation), consistent with the safety and preservation of the assets and (2) the Board of Trustees, or its designee, may annually determine the amount of the total return, up to the limit established by the underlying endowment agreement between the Museum and the respective donors, that will be treated as distributions available for current. Investment risk is measured in terms of the total endowment fund; investment assets and allocation between asset classes and strategies are managed to not expose the fund to unacceptable levels of risk.

Spending Policy. The Museum Board of Trustees governs the use of the Endowment. Limits on distributions from the Endowment are established within the underlying endowment agreement between the Museum and the respective donors. The Museum directly allocates the distributions to the mission related programs and services identified within these underlying endowment agreements.

Composition of and changes in donor designated endowment net assets at September 30, 2019 and 2018, are presented below.

Donor-designated endowment net asset composition at September 30, 2019 is as follows:

<u>September 30, 2019</u>	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Donor-designated endowment funds	\$ -	\$ 1,206,391	\$ 1,206,391

Changes in endowment net assets were as follows:

<u>September 30, 2019</u>	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Endowment Fund net assets, beginning of year	\$ -	\$ 424,251	\$ 424,251
Investment return, net	-	(22,230)	(22,230)
Contributions	-	804,370	804,370
Endowment Fund net assets, end of year	\$ -	\$ 1,206,391	\$ 1,206,391

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS
September 30, 2019 and 2018

13. Donor-Designated Endowments (Continued)

Donor-designated endowment net asset composition at September 30, 2018 is as follows:

<u>September 30, 2018</u>	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Donor-designated endowment funds	\$ <u> -</u>	\$ <u> 424,251</u>	\$ <u> 424,251</u>

Changes in endowment net assets were as follows:

<u>September 30, 2018</u>	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Endowment Fund net assets, beginning of year	\$ -	\$ 311,149	\$ 311,149
Investment return, net	-	(3,177)	(3,177)
Contributions	<u> -</u>	<u> 116,279</u>	<u> 116,279</u>
Endowment Fund net assets, end of year	\$ <u> -</u>	\$ <u> 424,251</u>	\$ <u> 424,251</u>

14. Net Assets with Donor Restriction and Release from Restrictions

The amounts included in net assets with donor restrictions consist of the following at September 30:

	<u>2019</u>	<u>2018</u>
Subject to expenditure for specific purpose:		
Program restrictions, including gallery and exhibit funds, artifacts and collection	\$ <u> 1,615,433</u>	\$ <u> 2,007,337</u>
Not subject to appropriation or expenditure:		
Beneficial interest in trusts, a portion of the spending rate which is available to support operations	90,938,703	92,793,341
Endowment funds	<u> 1,206,391</u>	<u> 424,251</u>
	\$ <u> 93,760,527</u>	\$ <u> 95,224,929</u>

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of the passage of time or other events specified by donors. Those amounts released from restriction are as follows:

	<u>2019</u>	<u>2018</u>
Purpose restrictions accomplished:		
Program restrictions, including gallery and exhibit funds, artifacts and collection	\$ <u> 330,407</u>	\$ <u> 276,033</u>

(Continued)

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS
September 30, 2019 and 2018

15. Net Assets without Donor Restrictions - Board Designated

At September 30, 2019 and 2018, \$10,870,448 and \$13,362,730, respectively, of net assets without donor restrictions are Board-designated net assets without donor restrictions, most of which are designated for bond repayment, gallery upgrades, and plant and equipment costs.

16. Leasing Arrangements

The Museum leases a 5,400 square foot building to National Oceanic and Atmospheric Administration (NOAA) under a noncancelable lease that expires in February 2025. The building is included in property and equipment on the statements of financial position at a total cost of \$649,493 offset by accumulated depreciation of \$242,721 and \$226,150 at September 30, 2019 and 2018, respectively. The lease agreement provides for annual rental payments of \$2,500 per year plus reimbursement of operating expenses incurred by the Museum for the upkeep and maintenance of the building as a shared expense. The operating expenses are estimated by the Museum at the beginning of each year and split into twelve equal installments to be paid by NOAA. Within 120 days after the end of each year, the Museum adjusts the rent charged for the actual operating expenses incurred to NOAA and either credits their future rent or requires additional payment, as necessary. The following is a summary of future minimum rental income under the noncancelable operating lease.

Future minimum payments on the above long-term lease are as follows:

<u>Year Ending</u> <u>September 30,</u>	
2020	\$ 2,500
2021	2,500
2022	2,500
2023	2,500
2024	<u>2,500</u>
	<u>\$ 12,500</u>

The Museum also has other lease agreements for portions of the Museum's land. The significant agreements are described in Note 10.

THE MARINERS' MUSEUM

NOTES TO FINANCIAL STATEMENTS
September 30, 2019 and 2018

17. Expenses by Natural Category

As noted in Note 2, the statement of functional expenses is only for 2019, the year of implementation of Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities: Topic 958*. Natural expenses for the year ending September 30, 2018, are presented below:

Natural Expense Category

Salaries and wages	\$ 4,566,339
Depreciation	1,721,906
Employee benefits	1,006,892
Occupancy	721,540
Repair and maintenance	604,162
Interest expense	289,122
Advertising	255,905
Other expenses	239,666
Outside services	220,472
Insurance	190,626
Supplies	161,997
Staff training and travel	153,614
Postage and shipping	146,157
Event costs	68,930
Bank service charges	<u>51,707</u>
	<u>\$ 10,399,035</u>