

ARIZONA-SONORA DESERT MUSEUM, INC.

YEAR ENDED SEPTEMBER 30, 2010

ARIZONA-SONORA DESERT MUSEUM, INC.

YEAR ENDED SEPTEMBER 30, 2010

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Independent Auditors' Report

Board of Trustees
Arizona-Sonora Desert Museum, Inc.
Tucson, Arizona

We have audited the accompanying statement of financial position of Arizona-Sonora Desert Museum, Inc. as of September 30, 2010, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of Arizona-Sonora Desert Museum, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards established by the AICPA Auditing Standards Board. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Museum's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Arizona-Sonora Desert Museum, Inc. as of September 30, 2010, and the changes in its net assets and its cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying information on page 22 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The accompanying information on page 22 has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

BeachFleischman PC

December 16, 2010

ARIZONA-SONORA DESERT MUSEUM, INC.

STATEMENT OF FINANCIAL POSITION

SEPTEMBER 30, 2010

	Unrestricted							Total
	Operating	Property and Equipment	Board Designated Reserve	Board Designated Endowment	Total Unrestricted	Temporarily Restricted	Permanently Restricted	
ASSETS								
Cash and cash equivalents	\$ 220,922		\$ 26,429	\$ 158,574	\$ 405,925	\$ 42,286	\$ 301,291	\$ 749,502
Estates and pledges receivable, net	1,098,037		803		1,098,840	103,881		1,202,721
Other receivables	86,766				86,766			86,766
Due from (to) other net asset groups	(178,562)		194,590	162,471	178,499	104,386	(282,885)	
Investments	2,874		299,086	1,971,921	2,273,881	542,989	3,784,085	6,600,955
Beneficial interest in perpetual trust							134,034	134,034
Inventory	225,642		2,588		228,230			228,230
Other assets	80,982				80,982	555,333		636,315
Property and equipment, net		\$17,008,656	68,904		17,077,560	31,235		17,108,795
Total assets	\$ 1,536,661	\$17,008,656	\$ 592,400	\$ 2,292,966	\$21,430,683	\$ 1,380,110	\$ 3,936,525	\$ 26,747,318
LIABILITIES AND NET ASSETS								
Liabilities:								
Accounts payable	\$ 168,024				\$ 168,024			\$ 168,024
Accrued liabilities	516,566				516,566	\$ 5,893		522,459
Unearned revenue	60,622				60,622			60,622
Deferred revenue, membership dues	193,400				193,400			193,400
Capital leases payable	47,500		\$ 7,636		55,136			55,136
Liability under trust agreement						80,923		80,923
Total liabilities	986,112		7,636		993,748	86,816		1,080,564
Net assets:								
Unrestricted:								
Undesignated	550,549				550,549			550,549
Invested in property and equipment		\$17,008,656			17,008,656			17,008,656
Designated for future capital			584,764		584,764			584,764
Designated for long-term reserves				\$ 2,292,966	2,292,966			2,292,966
Temporarily restricted						1,293,294		1,293,294
Permanently restricted							\$ 3,936,525	3,936,525
Total net assets	550,549	17,008,656	584,764	2,292,966	20,436,935	1,293,294	3,936,525	25,666,754
Total liabilities and net assets	\$ 1,536,661	\$17,008,656	\$ 592,400	\$ 2,292,966	\$21,430,683	\$ 1,380,110	\$ 3,936,525	\$26,747,318

See notes to financial statements.

ARIZONA-SONORA DESERT MUSEUM, INC.

STATEMENT OF ACTIVITIES

YEAR ENDED SEPTEMBER 30, 2010

	Unrestricted				Total Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	Operating	Property and Equipment	Board Designated Reserve	Board Designated Endowment				
Revenues and other support:								
Admissions	\$ 2,437,789				\$ 2,437,789			\$ 2,437,789
Concessions rental	395,677				395,677			395,677
Museum food services rental	209,033				209,033			209,033
Facilities rental	40,121				40,121			40,121
Membership	1,134,500				1,134,500			1,134,500
Contributions	1,273,167		\$ 60,892		1,334,059	\$ 548,728	\$ 4,903	1,887,690
Grant revenue	123,349				123,349			123,349
Special events, net	157,635				157,635			157,635
Education	156,480				156,480	68,497		224,977
Publications	26,922				26,922			26,922
Investment income:								
Interest and dividends	3,032		8,967	\$ 54,320	66,319	14,254	88,349	168,922
Net investment gain (loss)	(9,513)		4,219	144,830	139,536	114,943	251,617	506,096
Investment fees	(3,883)		(1,381)	(8,502)	(13,766)	(2,231)	(14,125)	(30,122)
Loss on disposal of assets			(11,643)		(11,643)			(11,643)
Other	55,958				55,958	4,983		60,941
Support provided from designated funds	402,000		430,260	(832,260)				
Net assets released from restrictions	808,914	\$ 739,273	(427,636)		1,120,551	(1,120,551)		
Total revenues and other support	7,211,181	739,273	63,678	(641,612)	7,372,520	(371,377)	330,744	7,331,887
Expenses:								
Program services:								
Facilities	1,984,019	1,206,437	950		3,191,406			3,191,406
Visitor services	274,513				274,513			274,513
Summer Saturday evenings	17,041				17,041			17,041
Animal interpretive collections	172,115				172,115			172,115
Raptor Free Flight	165,941				165,941			165,941
Botany	473,617				473,617			473,617
Herpetology and invertebrate zoology	359,306				359,306			359,306
Mammalogy and ornithology	709,216				709,216			709,216
Publications	22,000		1,000		23,000			23,000
Center for Sonoran Desert Studies	1,021,769				1,021,769			1,021,769
Exhibits	217,796				217,796			217,796
Design and planning	160,220				160,220			160,220
Art Institute	310,004				310,004			310,004
Supporting services:								
Administration	446,486		48,542		495,028			495,028
Finance	463,408				463,408			463,408
Marketing	229,077				229,077			229,077
Fundraising:								
Development and membership	403,065		24,054	28	427,147			427,147
Total expenses	7,429,593	1,206,437	74,546	28	8,710,604			8,710,604
Change in net assets before transfers	(218,412)	(467,164)	(10,868)	(641,640)	(1,338,084)	(371,377)	330,744	(1,378,717)
Transfers	237,000		(237,000)	162,471	162,471	120,594	(283,065)	
Change in net assets	18,588	(467,164)	(247,868)	(479,169)	(1,175,613)	(250,783)	47,679	(1,378,717)
Net assets, beginning of year	531,961	17,475,820	832,632	2,772,135	21,612,548	1,544,077	3,888,846	27,045,471
Net assets, end of year	\$ 550,549	\$17,008,656	\$ 584,764	\$ 2,292,966	\$20,436,935	\$ 1,293,294	\$ 3,936,525	\$25,666,754

See notes to financial statements.

ARIZONA-SONORA DESERT MUSEUM, INC.

STATEMENT OF CASH FLOWS

YEAR ENDED SEPTEMBER 30, 2010

Cash flows from operating activities:	
Change in net assets	\$ (1,378,717)
Adjustment to reconcile change in net assets to net cash used in operating activities:	
Depreciation and amortization	1,206,437
Amortization of discount on long-term pledges receivable	(12,525)
Net unrealized gains on investments	(879,065)
Net realized losses on investments	372,969
Donations of stock	(13,999)
Loss on disposal of assets	11,643
Changes in operating assets and liabilities:	
Estates and pledges receivable	(29,946)
Other receivables	14,312
Inventory	30,677
Other assets	57,244
Accounts payable	(9,142)
Accrued liabilities	5,938
Unearned revenue	31,622
Deferred revenue, membership dues	(2,596)
Liability under trust agreement	(4,997)
Total adjustments	<u>778,572</u>
Net cash used in operating activities	<u>(600,145)</u>
Cash flows from investing activities:	
Proceeds from sales and redemptions of investments	3,296,943
Purchases of investments	(2,062,650)
Purchases of property and equipment	<u>(377,517)</u>
Net cash provided by investing activities	<u>856,776</u>
Cash flows from financing activities:	
Repayment of capital lease obligation	<u>(19,550)</u>
Net cash used in financing activities	<u>(19,550)</u>
Net increase in cash and cash equivalents	237,081
Cash and cash equivalents, beginning	<u>512,421</u>
Cash and cash equivalents, ending	<u>\$ 749,502</u>

See notes to financial statements.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED SEPTEMBER 30, 2010

1. Organization and summary of significant accounting policies:

Organization:

The Arizona-Sonora Desert Museum, Inc. (the "Museum") is an independent natural history institution in Tucson, Arizona. The Museum operates as a nonprofit, educational corporation supported by admission, membership dues and contributions, which come primarily from the private sector.

Financial statement presentation:

The Museum reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. Resources are reported for accounting purposes in separate classes of net assets based on the existence or absence of donor-imposed restrictions. In the accompanying financial statements, net assets that have similar characteristics have been combined into similar categories as follows:

- Permanently restricted - Net assets that are subject to donor-imposed stipulations that assets be maintained permanently by the Museum. The donors of these assets permit the Museum to use all or part of the investment return of these assets on continuing operations, which may be subject to certain restrictions.
- Temporarily restricted - Net assets whose use by the Museum is subject to donor-imposed stipulations that can be fulfilled by actions of the Museum pursuant to those stipulations or that expire through the passage of time.
- Unrestricted - Net assets that are not subject to donor-imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of the Board of Trustees or may otherwise be limited by contractual agreements with outside parties.

Accounting estimates:

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

Recognition of donor-restricted 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 the entire amount of a restriction is fulfilled in the same time period in which the contribution is received, the Museum reports the support as unrestricted.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

1. Organization and summary of significant accounting policies (continued):

Recognition of donor-restricted contributions (continued):

Contributions of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Museum reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

Revenue recognition:

The Museum recognizes revenue earned on government grant and cooperative contracts as exchange transactions utilizing the percentage-of-completion method measured by the cost-to-cost method or level-of-effort method, as applicable. The percentage complete is estimated based upon the percentage that the incurred costs on each grant bears to the estimated total costs of the grant.

Revenue and costs on grants are subject to revision throughout the terms of the grants and required adjustments, if any, are made in the period in which the revisions become known.

Unearned revenue represents advance payments received for educational classes and other activities offered by the Museum.

The Museum sells annual memberships entitling the purchaser to unlimited admission during the year. Fees for membership dues are recognized ratably and in the fiscal year to which the membership applies.

Cash and cash equivalents:

Cash and cash equivalents include securities with an original purchased maturity of three months or less. Cash and cash equivalents received with donor-imposed stipulations restricting the use of the cash to long-term purposes and cash designated for long-term purposes are classified as investments.

The Museum maintains deposit accounts, certificates of deposit and money market funds with various institutions. At times, such investments may be in excess of the FDIC insurance limit; however, management does not believe it is exposed to any significant credit risk on cash and cash equivalents.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

1. Organization and summary of significant accounting policies (continued):

Estates and pledges receivable:

Unconditional promises to give are recognized as revenues when notice of the promise is received. Conditional promises to give are recognized only upon the Museum's substantial satisfaction of the donor imposed condition or if in management's judgment, the possibility the condition will not be met is remote. Promises to give, which are collectible over future periods, are discounted to their net present value using a rate of interest equal to government securities issued near the date of the promise and having a maturity date equal to the life of the promise. The Museum records bad debt losses and an allowance when promises to give are considered uncollectible.

Investments:

Investments in equity securities with readily determinable fair values and all investments in debt securities are valued at their fair values in the statement of financial position. Donated investments are recorded at their fair value at the date of gift. Investment gains and losses are included in the statement of activities as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor-imposed stipulation or by law.

Realized gains or losses on disposition of investments are recorded on a trade date basis using the specific identification method. The fair value of investment securities is estimated based upon the last trade price on a national securities exchange or in the over-the-counter market. If no trade price is reported for the measurement date, the fair value is estimated based upon the current bid price at the close of business on the measurement date.

The Museum has a total return policy on permanently restricted investments. The investment balance in the permanently restricted net asset group is maintained on an inflation-adjusted basis to include the investment corpus as well as an annual inflation adjustment amount. The inflation adjustment amount is based on annual changes to the Consumer Price Index. When necessary, unrestricted dollars are transferred to the permanently restricted net asset group to maintain the inflation adjusted balance.

Inventory:

Inventory consists primarily of supplies and publications and is stated at cost on a first-in, first-out basis. Minerals included in inventory are held for sale and are stated at the lower of average cost or net realizable value.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

1. Organization and summary of significant accounting policies (continued):

Property and equipment:

Property and equipment are stated at cost or, if acquired by gift, at estimated fair market value at the date of donation. Depreciation is computed on the straight-line method over the estimated useful lives of the related assets which range from 3 to 30 years. Maintenance, repairs and minor renewals are expensed as incurred while expenditures for additions and improvements with a useful life greater than 3 years are capitalized. Contributions of cash that must be used to acquire property and equipment are reported as temporarily restricted support. The Museum reports expirations of donor restrictions when the acquired assets are placed in service as instructed by the donor. The Museum reclassifies temporarily restricted net assets to unrestricted net assets at that time.

Property and equipment under capital lease is stated at cost or the assets' net present value of future lease payments at the date of the lease. Amortization is provided using the straight-line method over the estimated useful lives of the assets, or lease term, and is included with depreciation expense.

Pima County owns the land and some permanent structures on which the Museum is located. The Museum has a lease with Pima County, which entitles the Museum to exclusive right and use of the land and to operate the properties as a museum of natural history. The lease expires on September 30, 2028, with an option to renew for an additional 25 years under the same terms. Although the lease provides that the title to the Museum's property and exhibits is vested with the County, such assets are recorded on the books of the Museum to reflect the Museum's responsibility for management of these assets. The fair value of the leased premises has not been reported in the financial statements of the Museum.

Collections:

The collections, which were acquired through purchases and contributions since the Museum's inception, are not recognized as assets on the statement of financial position. Purchases of collection items are recorded as decreases in unrestricted net assets in the year in which the items are acquired, or as decreases in temporarily or permanently restricted net assets if the assets used to purchase the items are restricted by donors. Contributed collection items are not reflected in the financial statements. Proceeds from de-accessions or insurance recoveries are reflected as increases in the appropriate net asset classes.

Contributed services:

Contributed services are reported as contribution revenue and as assets or expenses only if the services create or enhance a non financial asset or:

- Would typically need to be purchased by the Museum if such services had not been contributed,
- Require specialized skills, and
- Are provided by individuals possessing those skills.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

1. Organization and summary of significant accounting policies (continued):

Contributed services (continued):

Many individuals volunteer their time and perform a variety of tasks that assist the Museum. During 2010, approximately 175 docents contributed over 74,000 hours in interpretive and educational programs on Museum grounds and in southern Arizona communities. In addition, 256 other volunteers contributed over 60,200 hours in serving as clerical and library aides, greeters, botany and geology assistants, and in various other capacities. No amounts have been recorded in the financial statements for contributed services from docents and other volunteers as the criteria specified above were not met.

Fair value of financial instruments:

The Museum's financial instruments include cash and cash equivalents, receivables, accounts payable, accrued expenses, and capital leases payable. For all of the Museum's financial instruments that are carried at cost, that cost approximates fair value.

Fair value measurements:

Under GAAP, the provisions of fair value are defined as the price to sell an asset or transfer a liability between market participants as of the measurement date. Fair value measurements assume the asset or liability is exchanged in an orderly manner; the exchange is in the principal market for that asset or liability (or in the most advantageous market when no principal market exists); and that the market participants are independent, knowledgeable and able and willing to transact an exchange. GAAP also clarifies that the reporting entity's nonperformance risk (credit risk) should be considered in valuing liabilities.

GAAP establishes a framework for measuring fair value by creating a hierarchy for observable independent market inputs and unobservable market assumptions and expands disclosures about fair value measurements. Considerable judgment is required in interpreting market data used to develop the estimates of fair value. Accordingly, the estimates presented in the financial statements are not necessarily indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions and estimation methodologies may have a material effect on the estimated fair value.

During the year, the Museum adopted updated provisions for fair value measurements and disclosures related to certain alternative investments. This guidance permits the use of a qualifying investment's net asset value per share to estimate fair value. The update also requires additional disclosures about the nature and risks of investments within its scope.

Program expense allocations:

Expenses that can be identified with a specific program are charged directly to the program according to their natural expense classification. Costs incurred that share a common purpose are allocated to programs based upon their percentage of employees or square foot usage depending upon the nature of the expense.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

1. Organization and summary of significant accounting policies (continued):

Advertising:

Advertising costs are expensed as incurred. Total advertising expense was \$109,842 for 2010.

Income taxes:

The Museum is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. The Museum is also exempt from state income taxes. Accordingly, no provision is made for income taxes in the financial statements. Management is not aware of any matters which would cause the Museum to jeopardize its tax-exempt status.

Effective October 1, 2009, the Museum was required to adopt the revised provisions of ASC 740, relating to uncertain tax positions. These standards require management to perform an evaluation of all tax positions taken or expected to be taken in the course of preparing the Museum's tax returns to determine whether the tax positions meet a "more likely than not" standard of being sustained under examination by the applicable taxing authorities. This evaluation is required to be performed for all open tax years, as defined by the various statutes of limitations, for federal and state purposes.

The Museum is only subject to income taxes on unrelated business taxable income (UBTI). As a result, the Museum is required to file informational returns for federal and state purposes and, if it has UBTI, federal and state income tax returns. With limited exceptions, the Museum is no longer subject to tax examination for any years earlier than 2006 for federal and 2005 for state. Management has performed its evaluation of tax positions taken on all open tax returns and has determined that there were no positions taken that do not meet the "more likely than not" standard.

From time to time, the Museum may be subject to penalties and interest assessed by various taxing authorities, which are classified as supporting services when they occur.

Subsequent events:

The Museum's management has evaluated the events that have occurred subsequent to September 30, 2010 through December 16, 2010, the date that the financial statements were available to be issued. Management has determined that no events have occurred during this period that require adjustment to or disclosure in the financial statements. Management has no responsibility to update these financial statements for events and circumstances occurring after this date.

2. Estates and pledges receivable:

The Museum accounts for contributions to be made in future years as unconditional promises in the year the promise is made. Long-term pledges receivable are discounted to their present value with rates ranging from .27% to 4.14 %.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

2. Estates and pledges receivable (continued):

At September 30, 2010, the amounts receivable as a result of these promises are as follows:

Year ending <u>September 30,</u>	
2011	\$ 1,215,951
Less allowance for uncollectible pledges	100
Less unamortized discount to present value	<u>13,130</u>
	<u>\$ 1,202,721</u>

Estates and pledges receivable are due from various private estates, foundations, businesses and individuals. The Museum recorded an allowance for doubtful pledges receivable totaling \$100 as of September 30, 2010. Estates and pledges receivable from the Board of Trustees totaled \$6,820 as of September 30, 2010. Three donors comprised 90% of estates and pledges receivable at September 30, 2010.

3. Investments:

Investments carried at fair value are comprised of the following amounts at September 30, 2010:

Fixed income securities	\$ 1,126,574
Equity funds	3,685,444
Strategy and private equity funds	<u>1,788,937</u>
	<u>\$ 6,600,955</u>

Net investment gain for the year ended September 30, 2010 is as follows:

Net realized losses on investments	\$ (372,969)
Net unrealized gains on investments	<u>879,065</u>
	<u>\$ 506,096</u>

In addition to the resources set aside to fund capital and special projects, the Board of Trustees designated a portion of unrestricted net assets as a long-term reserve to serve a function similar to an endowment. The amount in the long-term reserve has been established at a minimum of one-half of the annual operating budget and was \$1,971,921 at September 30, 2010.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

4. Fair value measurements:

At September 30, 2010, the fair value of assets measured on a recurring basis is as follows:

	<u>Fair value</u>	<u>Quoted prices (level 1)</u>	<u>Significant other observable inputs (level 2)</u>	<u>Significant unobservable inputs (level 3)</u>
Fixed income securities:				
Corporate bonds	\$ 1,126,574	\$ 1,126,574		
Equity funds:				
US securities	2,446,980	1,533,879	\$ 913,101	
International securities	1,238,464	1,238,464		
Strategy and private equity funds:				
Commodities	225,701	225,701		
Real estate	319,983	319,983		
Hedge fund	<u>1,243,253</u>			<u>\$ 1,243,253</u>
	<u>\$ 6,600,955</u>	<u>\$ 4,444,601</u>	<u>\$ 913,101</u>	<u>\$ 1,243,253</u>

The preceding table is based on the following hierarchy of observable independent market inputs and unobservable market assumptions:

Level 1 – Inputs represent unadjusted quoted prices for identical assets or liabilities exchanged in active markets.

Level 2 – Inputs include directly or indirectly observable inputs other than Level 1 inputs such as quoted prices for similar assets or liabilities exchanged in active or inactive markets; quoted prices for identical assets or liabilities exchanged in inactive markets; other inputs that are considered in fair value determinations of the assets or liabilities, such as interest rates and yield curves that are observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks and default rates; and inputs that are derived principally from or corroborated by observable market data.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

4. Fair value measurements (continued):

Level 3 – Inputs include unobservable inputs used in the measurement of assets and liabilities. The Museum is required to use its own assumptions regarding unobservable inputs because there is little, if any, market activity in the assets or liabilities or related observable inputs that can be corroborated at the measurement date. Measurements of nonexchange traded derivative contract assets and liabilities are primarily based on valuation models, discounted cash flow models or other valuation techniques that are believed to be used by market participants. Unobservable inputs require the Museum to make certain projections and assumptions about the information that would be used by market participants in pricing assets or liabilities.

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

A reconciliation of assets measured at fair value on a recurring basis with the use of significant unobservable inputs (Level 3) from October 1, 2009 to September 30, 2010 is as follows:

	<u>Hedge funds</u>
Balance October 1, 2009	\$ 1,206,860
Gains included in change in net assets	<u>36,393</u>
Balance at September 30, 2010	<u>\$ 1,243,253</u>

The realized and unrealized gains included in change in net assets for the year ended September 30, 2010 are reported in the statement of activities as follows:

	<u>Hedge funds</u>
Unrealized gains relating to assets still held at September 30, 2010 that are included in change in net assets	<u>\$ 36,393</u>

The following is a description of the valuation methodologies used for assets measured at fair value:

The fair value of the Museum's equity securities, governmental agencies and corporate bond fixed income securities, real estate funds and commodity linked funds are valued at the closing price reported in the active market on which the individual securities are traded (Level 1), which represents the net asset value of shares held by the Organization at year end.

The fair value of the Museum's investments in certain equity securities are valued at net asset value as determined by Northern Trust Company of Connecticut (NTCC) and calculated monthly (Level 2). Redemptions occur at net asset value by contract.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

4. Fair value measurements (continued):

The Museum invests in a hedge fund. The Fund operates as a "Fund-of-Funds," investing, either directly or indirectly, in a group of funds or other pooled investment vehicles ("Sub-Funds") managed by investment advisers selected by the Fund's investment manager. The Fund seeks to provide investors with exposure to alternative investment strategies by investing in diversified markets and instruments. Investments in Sub-Funds are valued at fair value, as determined by NTCC. In determining the fair value of each Sub-Fund, NTCC will take into account the estimated net asset value of such Sub-Fund provided to the Fund by the Sub-Fund itself, as well as any other considerations that may, in NTCC's judgment, increase or decrease such estimated value. Accordingly, because of the inherent uncertainty of these valuations, these estimated values may differ significantly from the values that could have been used had a readily available market for the investments existed, and the differences could be material. Cash equivalents are valued at cost, which approximates fair value. The Fund charges various administrative and management fees as defined in the Fund administration agreement. The Sub-Fund investments are subject to various redemption restrictions with typical redemption notice periods ranging from five to 90 days.

5. Property and equipment:

A summary of property and equipment at September 30, 2010 is as follows:

	<u>Pima County</u>	<u>Museum</u>	<u>Total</u>
Idle land and building		\$ 490,000	\$ 490,000
Land held for investment		226,500	226,500
Buildings and improvements	\$ 31,355,325	220,669	31,575,994
Furniture and equipment		2,325,711	2,325,711
Construction in progress		100,138	100,138
Total property and equipment	<u>31,355,325</u>	<u>3,363,018</u>	<u>34,718,343</u>
Less accumulated depreciation	<u>15,792,313</u>	<u>1,817,235</u>	<u>17,609,548</u>
Property and equipment, net	<u>\$ 15,563,012</u>	<u>\$ 1,545,783</u>	<u>\$17,108,795</u>

During 2002, \$490,000 in real property was donated to the Museum. There was no time or purpose restrictions imposed on the property; however, the property may not be sold by the Museum. In the event the Museum is unable to use the property, the Museum is required to donate the property to a nature conservation organization.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

6. Collections:

The Museum's collections consist substantially of living and nonliving natural history objects related to the Museum's interpretive region (the Sonoran Desert and adjacent habitats). Collections are held for educational, research, scientific, and curatorial purposes. With the exception of certain free-living organisms, collections are catalogued, preserved, and cared for, and activities verifying their existence and assessing their condition are performed continuously.

Objects are de-accessioned according to their value and replaceability. Living plants and animals for which there is no foreseeable future need are donated to other accredited institutions. No significant collection items were de-accessioned during the year ended September 30, 2010.

7. Beneficial interest in perpetual trust:

The Museum is the beneficiary of the J. Benton Trust (the Trust). The Trust is a perpetual trust administered by a financial institution for the sole benefit of the Museum. Distributions from the Trust are restricted for the care of the Museum's animal collections. The unrealized gain on Trust assets for the year ended September 30, 2010 was \$1,069.

8. Liability under trust agreement:

The Museum is the trustee of the Helene Brown Charitable Remainder Annuity Trust dated January 25, 2001, (the Annuity Trust). The Annuity Trust requires annual payments of 8% of the net fair market value of the assets of the Annuity Trust, as valued on the date of contribution, over a twenty-year term to the Grantor. The remainder of the assets of the Annuity Trust are to be distributed to the Museum upon expiration of the annuity payments. The assets of the Annuity Trust were valued at \$148,378 on the date of contribution and the annuity payments are \$11,870 per year. The liability under the Annuity Trust was determined to be \$116,544 based on an annuity payment over twenty years at the Museum's discount rate of 8% per annum. The assets of the Annuity Trust and liability under the trust agreement are adjusted for changes in the market value of the assets, annuity payments and amortization of the discount.

The market value of the assets of the Annuity Trust was \$45,225 as of September 30, 2010 and are included in temporarily restricted other assets in the accompanying financial statements. The remaining liability under the trust agreement was \$80,923 as of September 30, 2010.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

9. Irrevocable trust agreements:

The Museum is the remainder beneficiary of an irrevocable trust agreement with a market value of \$836,404 as of September 30, 2010. The trust assets are held in money market accounts and U.S. treasury notes monitored by the trustee. Income earned on trust assets is paid to designated income beneficiaries in an amount not less than \$35,000 per year. Upon the death of the income beneficiaries, the Museum will receive the remaining value of the trust's assets. The value of the trust agreement is recorded in the accompanying financial statements based upon the estimated present value of the trust assets to be received by the Museum. The assets are discounted at 4.02% over a 16-year period, which represents the remaining life expectancy of the income beneficiaries. These assets are included in temporarily restricted other assets with a value of \$487,976 as of September 30, 2010.

The Museum was also the remainder beneficiary of an irrevocable trust agreement with a market value of \$21,907,705 as of September 30, 2009. The trust assets were held in money market accounts, fixed income securities, equities, alternative investments, real estate and specialty assets monitored by the trustee. Income earned on trust assets was paid to the designated income beneficiary. Upon the death of the income beneficiary, the Museum was to receive 0.2% of the remaining value of the trust's assets. During the year ended September 30, 2010, the income beneficiary passed away and the Museum received a distribution from trust assets of approximately \$17,000. The Museum expects to receive an additional \$22,000 upon final distribution of the trust. This asset is included in temporarily restricted other assets as of September 30, 2010.

The discount rates on the Museum's interest in the above irrevocable trust agreements are based on the September 30, 2010 U.S. Treasury Bill rate corresponding to the estimated life expectancy of the trust beneficiaries.

10. Line of credit:

The Museum has entered into a one-year agreement with Northern Trust for a \$500,000 revolving line of credit (the "Agreement") through October 2011. The Agreement requires monthly interest only payments with any remaining principal balance due upon termination of the Agreement. Interest is calculated at the financial institution's prime rate less 1% with a minimum rate of 3%. The prime rate at September 30, 2010 was 3.25%. As of September 30, 2010, there was no outstanding balance on the line. Total interest incurred during 2010 on the line of credit aggregated \$167. The line of credit is collateralized by a security interest in the Museum's general intangibles and accounts receivable.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

11. Capital leases payable:

The Museum leases equipment under capital leases having a cost of \$83,505 and accumulated amortization of \$28,513. The following is a schedule of future minimum lease payments under the capitalized equipment leases as of September 30, 2010:

<u>Year ending September 30,</u>	<u>Total</u>	<u>Interest</u>	<u>Net minimum lease payments</u>
2011	\$ 21,408	\$ 3,815	\$ 17,593
2012	22,653	2,602	20,051
2013	16,654	1,099	15,555
2014	<u>2,062</u>	<u>125</u>	<u>1,937</u>
	<u>\$ 62,777</u>	<u>\$ 7,641</u>	<u>\$ 55,136</u>

12. Temporarily restricted net assets:

Temporarily restricted net assets were restricted for the following as of September 30, 2010:

Education	\$ 210,906
Science	134,863
Time restricted funds	645,108
Collections	104,005
Art Institute	49,971
Design and planning	9,276
Henderson House	25,895
Other miscellaneous programs	<u>113,270</u>
	<u>\$ 1,293,294</u>

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

13. Permanently restricted net assets:

At September 30, 2010, permanently restricted net assets are restricted for investment in perpetuity, the income from which is expendable to support the following:

Animal care (perpetual trust)	\$ 134,034
Research	54,670
Education	53,592
Earth science	58,411
Art Institute	1,240,568
Any museum activities	<u>2,395,250</u>
	<u>\$ 3,936,525</u>

14. Endowment:

The Museum's endowment consists of an individual fund established for a variety of purposes. The endowment includes both donor-restricted funds and as required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of relevant law:

The Board of Trustees of the Museum has interpreted Arizona's version (titled the "Management of Charitable Funds Act" (the Act)) of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Museum classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Museum in a manner consistent with the standard of prudence prescribed by the Act.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

14. Endowment (continued):

Changes in endowment net assets for the year ended September 30, 2010 are as follows:

	Board designated endowment	Donor temporarily restricted	Donor permanently restricted	Total
Endowment net assets, beginning	\$ 2,772,135	\$ 99,324	\$ 3,888,846	\$ 6,760,305
Investment return:				
Investment income	54,320	14,254	88,349	156,923
Net realized losses	(121,167)	(31,326)	(189,115)	(341,608)
Net unrealized gains	<u>265,997</u>	<u>146,269</u>	<u>440,732</u>	<u>852,998</u>
Total investment return	199,150	129,197	339,966	668,313
Contributions			4,903	4,903
Appropriation/transfer of assets for expenditures	162,471	120,594	(283,065)	
Support provided from designated funds	(832,260)			(832,260)
Administrative fees and expenses	<u>(8,530)</u>	<u>(2,231)</u>	<u>(14,125)</u>	<u>(24,886)</u>
	<u>\$ 2,292,966</u>	<u>\$ 346,884</u>	<u>\$ 3,936,525</u>	<u>\$ 6,576,375</u>

Permanently restricted net assets:

The portion of perpetual endowment funds that is required to be retained permanently

\$ 3,936,525

Temporarily restricted net assets:

Portion of perpetual endowment funds subject to purpose restrictions under the Act

\$ 346,884

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 the Act requires to retain as a fund of perpetual duration. In accordance with GAAP, such deficiencies are reported in unrestricted net assets. As of September 30, 2010, there were no deficiencies of this nature.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

14. Endowment (continued):

Return objectives and risk parameters:

The Museum has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Museum must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the S&P 500 Index while assuming a moderate level of investment risk. The Museum expects its endowment funds over time to provide an average rate of return of approximately 5.5% annually, adjusted for inflation. Actual returns in any given year may vary from this amount.

Strategies employed for achieving objectives:

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

Spending policy and how the investment objectives relate to spending policy:

The Museum has a policy of appropriating for distribution each year up to 5.5% of its endowment fund's average fair value over the three fiscal year-ends preceding the fiscal year in which the distribution is planned. In establishing this policy, the Museum considered the long-term expected return on its endowment. Historically, the Museum has spent less than the 5.5% which has allowed its endowment to grow. This is consistent with the Museum's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term, as well as to provide additional real growth through new gifts and investment return. Management of the Museum reports this as a transfer out.

15. Contingent rentals:

The Museum receives rent based upon a percentage of the gross sales from a gift shop and restaurant located on the Museum premises. Contingent rentals earned for the year ended September 30, 2010 totaled \$604,710 and is reported as concessions and museum food services.

ARIZONA-SONORA DESERT MUSEUM, INC.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

YEAR ENDED SEPTEMBER 30, 2010

16. Retirement plan:

The Museum has established a voluntary retirement plan (the "Plan") under Section 403(b) of the Internal Revenue Code. Full-time employees with over 1,000 hours of annual service are eligible to participate in the Plan. Subject to statutory limits, employees may contribute up to \$15,000 of annual compensation. The Museum contributes three percent of compensation to the Plan for all employees who contribute a minimum of three percent of their annual compensation and who have completed two years of service. Participants may invest all contributions in any of several options offered by Charles Schwab and TIAA Cref. The Museum's contribution to the Plan for the year ended September 30, 2010 was \$98,725.

17. Functional expenses:

Program services	\$ 7,095,944
Supporting services	1,187,513
Fundraising	<u>427,147</u>
	<u>\$ 8,710,604</u>

18. Concentrations:

Substantially all nonmanagement employees of the Museum are subject to a three year collective bargaining agreement with United Food and Commercial Workers Union Local 99 that expires on September 30, 2011.

19. Statement of cash flows:

Supplemental disclosure of cash flow information:

Cash paid for interest during 2010 was \$5,625.

20. Related party transactions:

During 2010, the Museum received approximately \$255,000 in cash contributions and \$5,500 in in-kind contributions from certain board members.

During 2010, the Museum paid approximately \$26,600 in investment fees to Northern Trust, of which a board member is an employee. The Museum also paid approximately \$14,000 in legal fees to a firm of which a board member is an employee.

ARIZONA-SONORA DESERT MUSEUM, INC.

SCHEDULE OF FUNCTIONAL EXPENSES

YEAR ENDED SEPTEMBER 30, 2010

	<u>Program services</u>	<u>Supporting services</u>	<u>Fundraising</u>	<u>Total expenses</u>
Accounting fees	\$ 34,108	\$ 4,897	\$ 1,520	\$ 40,525
Advertising	3,108	106,734		109,842
Conferences, conventions, and meetings	4,053	19,972	216	24,241
Depreciation and amortization	1,206,437			1,206,437
General insurance	90,648	7,634	201	98,483
Information technology	9,666	1,170	363	11,199
Legal fees	10,525	1,511	469	12,505
Occupancy	445,155			445,155
Office expenses	236,483	32,142	110,722	379,347
Other employee benefits	382,601	72,061	20,545	475,207
Other expenses	1,292,119	78,388	30,135	1,400,642
Other fees for services	37,578	46,151	24,802	108,531
Payroll taxes	291,826	58,712	16,754	367,292
Pension plan contributions	65,450	21,136	4,998	91,584
Royalties	7,674			7,674
Salaries and wages	2,913,366	526,069	156,845	3,596,280
Salaries and wages - officers	49,349	209,598	59,577	318,524
Travel	15,798	1,338		17,136
	<u>\$ 7,095,944</u>	<u>\$ 1,187,513</u>	<u>\$ 427,147</u>	<u>\$ 8,710,604</u>