Stoltey & Associates
Certified Public Accountant

MUSIC ACADEMY OF THE WEST

FINANCIAL STATEMENTS

December 31, 2018

Stoltey & Associates
Certified Public Accountant

INDEPENDENT AUDITORS' REPORT

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

We have audited the accompanying financial statements of Music Academy of the West (a California nonprofit organization), which comprise the statement of financial position as of December 31, 2018, and the related statements of activities, net assets, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Report on Summarized Comparative Information

We have previously audited the Music Academy of the West's financial statements, and our report dated May 23, 2018, expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2017 is consistent, in all material respects, with the audited financial statements from which it has been derived.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Music Academy of the West as of December 31, 2018, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Stoltey & Associates

September 27, 2019
Los Olivos, California

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Music Academy of the West

STATEMENT OF FINANCIAL POSITION
December 31, 2018
(With Comparative Totals for December 31, 2017)

ASSETS

	Without Donor Restrictions	With Donor Restrictions	2018	2017
CURRENT ASSETS				
Cash and equivalents	$ 5,249,914	$ -	$ 5,249,914	$ 4,403,729
Contributions receivable (Note 2)	-	2,465,743	2,465,743	1,930,166
Bequests receivable (Note 2)	-	4,475,159	4,475,159	1,515,000
Accounts receivable	25,435	-	25,435	27,435
Other receivables	11,694	-	11,694	56,143
Prepaid expenses and other current assets	223,695	-	223,695	127,551
Total Current Assets	5,510,738	6,940,902	12,451,640	8,060,024
Property and equipment, net (Note 5)	38,536,688	-	38,536,688	39,252,301
OTHER ASSETS				
Investments (Note 3)	35,166,969	3,815,858	38,982,827	36,433,878
Contributions receivable (Note 2)	-	1,780,064	1,780,064	1,371,783
Bequests receivable (Note 2)	-	2,666,476	2,666,476	7,240,533
Other investment (Note 6)	427,598	-	427,598	427,598
Contributions in trust (Note 7)	-	3,814,259	3,814,259	4,173,645
Total Other Assets	35,594,567	12,076,657	47,671,224	49,647,437
TOTAL ASSETS	$ 79,641,993	$ 19,017,559	$ 98,659,552	$96,959,762

The accompanying notes are an integral part of these financial statements

MUSIC ACADEMY OF THE WEST

STATEMENT OF FINANCIAL POSITION
December 31, 2018
(With Comparative Totals for December 31, 2017)

LIABILITIES AND NET ASSETS

	Without Donor Restrictions	With Donor Restrictions	2018	2017
CURRENT LIABILITIES				
Accounts payable	$ 103,581	$ -	$ 103,581	$ 61,409
Accrued expenses	251,087	-	251,087	152,338
Deposits	4,070	-	4,070	705
Deferred revenue	74,487	-	74,487	80,911
Current portion of long-term debt (Note 8)	506,355	-	506,355	488,234
Total Current Liabilities	939,580	-	939,580	783,597
LONG-TERM LIABILITIES				
Notes payable, net of current portion (Note 8)	11,679,855	-	11,679,855	12,171,221
Total Long-Term Liabilities	11,679,855	-	11,679,855	12,171,221
Total Liabilities	12,619,435	-	12,619,435	12,954,818
NET ASSETS (Note 9)				
Without donor restriction - undesignated	29,965,868	-	29,965,868	30,462,145
Without donor restriction - designated	37,056,690	-	37,056,690	33,947,748
With donor restriction - temporary in nature	-	18,507,559	18,507,559	17,577,191
With donor restriction - permanent in nature	-	510,000	510,000	502,860
Total Net Assets	67,022,558	19,017,559	86,040,117	82,489,944
TOTAL LIABILITIES AND NET ASSETS	$ 79,641,993	$ 19,017,559	$ 98,659,552	$ 95,444,762

The accompanying notes are an integral part of these financial statements

MUSIC ACADEMY OF THE WEST

STATEMENT OF ACTIVITIES
For the Year Ended December 31, 2018
(With Comparative Totals for December 31, 2017)

	Without Donor Restrictions	With Donor Restrictions	2018	2017
PUBLIC SUPPORT				
Contributions (note 1)	$ 8,535,603	$ 3,811,640	$ 12,347,243	$ 5,883,226
Concert program advertising	42,808	-	42,808	43,125
Other support	-	-	-	-
TOTAL PUBLIC SUPPORT	8,578,411	3,811,640	12,390,051	5,926,351
REVENUE CENTERS				
Rack and Treasure House sales	355,228	-	355,228	266,011
Rack and Treasure House expenses	(213,775)	-	(213,775)	(158,513)
TOTAL REVENUE CENTERS	141,453	-	141,453	107,498
SPECIAL EVENTS				
Gross revenue	875,515	-	875,515	850,708
Direct costs	(241,243)	-	(241,243)	(208,421)
SPECIAL EVENTS, NET	634,272	-	634,272	642,287
REVENUE				
Concerts, recitals and master classes	877,603	-	877,603	912,643
Fees	198,178	-	198,178	224,918
Rentals	185,200	-	185,200	216,951
Gain (loss) on sale of assets	(72,603)	-	(72,603)	(17,537)
Other revenue	57,349	-	57,349	47,248
Investment income (note 5)	(725,209)	(33,915)	(759,124)	5,062,061
Total Revenue	520,518	(33,915)	486,603	6,446,284
TOTAL PUBLIC SUPPORT AND REVENUE	9,874,654	3,777,725	13,652,379	13,122,420
Assets Released From Restriction	2,840,217	(2,840,217)	-	-
FUNCTIONAL EXPENSES				
Program Expenses:				
Summer School and Festival (note 1)	8,210,463	-	8,210,463	8,805,207
Supporting Services				
Management and general	784,945	-	784,945	831,531
Fundraising	1,106,798	-	1,106,798	1,180,123
Total Functional Expenses	10,102,206	-	10,102,206	10,816,861
CHANGES IN NET ASSETS	$ 2,612,665	$ 937,508	$ 3,550,173	$ 2,305,559

The accompanying notes are an integral part of these financial statements

MUSIC ACADEMY OF THE WEST

STATEMENT OF CHANGES IN NET ASSETS
For the Year Ended December 31, 2018
(With Comparative Totals for 2017)

	Without Donor Restrictions	With Donor Restrictions	2018	2017
Beginning Balance	$ 64,409,893	$ 18,080,051	$ 82,489,944	$ 80,184,385
Changes in Net Assets	2,612,665	937,508	3,550,173	2,305,559
Ending Balance	$ 67,022,558	$ 19,017,559	$ 86,040,117	$ 82,489,944

The accompanying notes are an integral part of these financial statements

MUSIC ACADEMY OF THE WEST

STATEMENT OF FUNCTIONAL EXPENSES
For the Year Ended December 31, 2018
(with comparative Totals for 2017)

	Program Expenses	Management and General	Fundraising	2018 Total	2017 Total
Salaries	$ 1,909,767	$ 169,220	$ 338,440	$ 2,417,427	$ 2,355,096
Pension plan contributions	64,943	5,754	11,509	82,206	77,424
Other employee benefits	162,646	14,412	28,823	205,881	216,430
Payroll taxes	137,600	12,192	24,385	174,177	167,326
Fees:					
Accounting and legal	-	51,979	-	51,979	54,826
Other	500,144	29,420	58,840	588,404	385,345
Advertising and promotion	226,317	20,053	40,107	286,477	299,502
Office expenses	69,959	6,199	12,398	88,556	86,161
Information technology	111,357	9,867	19,734	140,958	169,180
Occupancy	1,654,148	97,303	194,606	1,946,057	1,825,853
Travel	236,168	20,926	41,853	298,947	314,742
Interest	364,176	32,269	64,537	460,982	478,501
Depreciation	903,335	180,667	45,167	1,129,169	1,105,339
Insurance	65,175	5,775	11,550	82,500	91,655
Festival productions	1,804,728	128,909	214,849	2,148,486	3,189,481
Total Expenses	$ 8,210,463	$ 784,945	$ 1,106,798	$ 10,102,206	$ 10,816,861

MUSIC ACADEMY OF THE WEST

STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2018
(with comparative Totals for 2017)

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	$ 3,550,173	$ 2,305,559
Adjustments to reconcile change in net assets to net cash provided in operating activities:		
Depreciation	1,129,169	1,105,339
Amortization of loan issuance costs	12,444	12,444
Loss (gain) on value of securities	1,596,538	(6,250,193)
Loss (gain) on sale of securities	(148,765)	1,539,335
Loss (gain) on sale of fixed assets	72,603	17,537
Loss (gain) on value of charitable trusts	359,386	(186,754)
(Increase) decrease in operating assets:		
Contributions receivable	(844,960)	2,805,940
Accounts and other receivables	46,449	(83,578)
Prepaid expenses	(96,144)	103,874
Increase (decrease) in operating liabilities:		
Accounts payable	42,172	(275,493)
Accrued expenses	98,749	(39,075)
Deposits	3,365	535
Deferred revenue	(6,424)	(23,959)
NET CASH FLOWS FROM OPERATING ACTIVITIES	5,814,755	1,031,511
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of long-term investments	(9,712,581)	(32,076,183)
Proceeds from maturity and sale of long-term investments	5,715,859	33,431,558
Payments for property and equipment	(486,159)	(3,865,294)
NET CASH FROM INVESTING ACTIVITIES	(4,482,881)	(2,509,919)
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments on notes payables	(485,689)	(470,697)
NET CASH FLOWS FROM FINANCING ACTIVITIES	(485,689)	(470,697)
NET INCREASE IN CASH	846,185	(1,949,105)
CASH - Beginning of year	4,403,729	6,352,834
End of year	$ 5,249,914	$ 4,403,729
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the year for interest	$ 448,538	$ 448,584

Note 1: <u>Summary of Significant Accounting Policies</u>

This summary of significant accounting policies of Music Academy of the West (The Academy) is presented to assist in understanding the Academy financial statements. The financial statements and notes are representations of the Academy's management, who are responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America (GAAP) and have been consistently applied in the preparation of the financial statements.

Nature of Activities

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

The academy annually provides 140 musicians (fellows) full scholarship for the summer school and festival, including tuition, room, and board. Fellows are selected from more than 1,800 worldwide applicants to study with eminent faculty and visiting guest artists. Fellows participate in one of five programs: instrumental (strings, woodwinds, brass, and percussion), solo piano, collaborative piano, vocal piano, and voice. The voice program, led by legendary mezzo-soprano Marilyn Horne, has been featured in a fully staged opera production presented in the community every year since 1997.

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

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

The Academy is located in Santa Barbara, California.

Prior-Year Summarized Comparative Information

The financial statements include certain prior-year summarized comparative information in total but are not presented by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with GAAP. Accordingly, such information should be read in conjunction with The Academy's financial statements for the year ended December 31, 2017 from which the summarized information was derived.

Cash and Cash Equivalents
For purposes of the statement of cash flows, cash and cash equivalents consists of cash on hand, cash in banks, and cash in money market funds.

Contributions and Bequests Receivable
The Academy initially records and subsequently carries unconditional contributions and bequests receivable at fair value using present value techniques incorporating risk-adjusted discount rates designed to reflect the assumptions market participants would use in pricing the asset.

Fixed Assets
The Academy records fixed asset additions over $2,500 at cost, or if donated, at fair value on the date of donation. When assets are sold or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts, and any resulting gain or loss is included in the statement of activities. Costs of maintenance and repairs that do not improve or extend the useful lives of the respective assets are expensed currently. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, or in the case of capitalized leased assets or leasehold improvements, the lesser of the useful life of the asset or the lease term. Management has estimated the useful lives of depreciable assets as follows:

• Buildings	50 years
• Building Improvements	5-15 years
• Land Improvements	10-15 years
• Art	25 years
• Furniture and Equipment	5-15 years
• Library Texts	25 years
• Musical Instruments	25 years
• Vehicles	5 years

The Academy reviews the carrying values of property and equipment for impairment whenever events or circumstances indicate that the carrying value of an asset may not be recoverable from the estimated cash flows expected to result from its use and eventual disposition. When considered impaired, an impairment loss is recognized to the extent carrying value exceeds the fair value of the asset. Management has determined there were no indicators of asset impairment during the year ended December 31, 2018.

Investments
The Academy records investment purchases at cost, or if donated, at fair value on the date of donation. Thereafter, investments are reported at their fair values in the statement of financial position. Net investment return/(loss) is reported in the statement of activities and consists of

interest and dividend income, realized and unrealized capital gains and losses, less external investment management expenses.

Net Assets

Net assets, revenues, gains, and losses are classified based on the existence or absence of donor or grantor-imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

Net Assets without Donor Restrictions

Net assets available for use in general operations and not subject to donor restrictions are reported as net assets without donor restriction. The governing Board has designated, from net assets without donor restrictions, net assets for future loan repayment and as a quasi-endowment.

Net Assets with Donor Restrictions

Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity.

The Academy reports contributions restricted by donors as increases in net assets without donor restrictions if the restrictions expire (that is, when a stipulated time restriction ends or purpose restriction is accomplished) in the reporting period in which the revenue is recognized. All other donor-restricted contributions are reported as increases in net assets with donor restrictions, depending on the nature of the restrictions. When a restriction expires, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statement of activities as net assets released from restrictions.

Revenue Recognition

Exchange Transactions

Revenue is recognized when earned. Program service fees and payments under cost-reimbursable contracts received in advance are deferred to the applicable period in which the related services are performed or expenditures are incurred.

Contributions

Contributions are recognized when cash, securities or other assets, an unconditional promise to give, or notification of a beneficial interest is received. Conditional promises to give are not recognized until the conditions on which they depend have been substantially met.

Donated Services and In-Kind Contributions

Volunteerism and contributed services are critical to the Academy. During the year ended December 31, 2018, numerous volunteers donated their time and services. The donated services were not recognized in the financial statements because they do not meet the criteria for recognition under generally accepted accounting principles.

The Academy reports donated noncash contributions at the estimated fair value at the date of the contribution. The Academy reports gifts of furniture and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used at the estimated fair market value on the date gift is received.

Advertising Costs
Advertising costs are expensed as incurred and approximated $286,477 during the year ended December 31, 2018.

Functional Expenses
The cost of providing The Academy programs and other activities is summarized on a functional basis in the statement of functional expenses. The statement of functional expenses presents the natural classification detail of expenses by function. Expenses that can be identified with a specific program or support service are charged directly to that program or support service. Expenses that are attributed to more than one program or supporting function require allocation on a reasonable basis that is consistently applied. The expenses allocated are as follows:

Information Technology	Time and Effort
Insurance – Property	Square Footage
Insurance – Workers Compensation	Time and Effort
Occupancy	Square Footage
Office Expenses	Time and Effort
Payroll Taxes	Time and Effort
Personnel Compensation	Time and Effort

Tax Exempt Status
The Academy is organized as a California nonprofit corporation and has been recognized by the IRS as exempt from federal income taxes under Internal Revenue Code (IRC) as an organization described in IRC Section 501(c)(3) and qualifies for the charitable contribution deduction under IRC and has been determined not to be a private foundation under IRC. The Academy is annually required to file a Return of Organization Exempt from Income Tax (Form 990) with the IRS. In addition, The Academy is subject to tax on income that is derived from business activities that are unrelated to its exempt purpose. Management has determined the Academy is not subject to unrelated business income tax and has not filed an Exempt Organization Business Income Tax Return (Form 990-T) with the IRS.

The Academy tax filings are subject to examination by the IRS, generally for three years after they are filed. The Academy is not aware of any activities that would jeopardize its tax-exempt status.

Use of Estimates
The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses during the reporting period and the reported amounts of assets and liabilities at the date of the financial statements. On an ongoing basis, The Academy's management evaluates the estimates and assumptions based upon historical experience and various other factors and circumstances. The Academy

management believes that the estimates and assumptions are reasonable in the circumstances; however, the actual results could differ from those estimates. Significant estimates used in the preparation of these financial statements include:

- Allocation of functional expenses
- Fair value of contributions and bequests receivable
- Fair value of nonmarketable securities

Reclassifications

Certain items in the 2017 financial statements were reclassified in order to conform to the 2018 presentation.

Change in Accounting Principle

On August 18, 2016, FASB issued Accounting Standards Update (ASU) 2016-14, Not-for-Profit Entities (Topic 958) – Presentation of Financial Statements of Not-for-Profit Entities. The update addresses the complexity and understandability of net asset classification, deficiencies in information about liquidity and availability of resources, and the lack of consistency in the type of information provided about expenses and investment return. The Academy has implemented ASU 2016-14 and have adjusted the presentation in these consolidated financial statements accordingly. The ASU has been applied retrospectively to all periods presented with no material reclassifications between net asset without donor restrictions and net assets with donor restrictions.

Subsequent Events

Management has evaluated subsequent events through September 27, 2019, the date that the financial statements were available to be issued. Management has determined that no event, with exception of the following discussion regarding extension of the line of credit, requiring disclosure or significantly impacting disclosure has occurred.

The Academy extended the maturity date of the $1,500,000 line of credit held at First Republic Bank from June 30, 2019 to November 29, 2019. The terms of the lone of credit remained the same as described in note 13.

Note 2: Contributions and Bequests Receivable

Contributions Receivable

The Academy anticipates contributions receivable to be collected in the following years:

Year ending December 31:

2019	$ 2,465,743
2020-2024	1,827,500
2025-2028	145,000
	4,438,243
Less Fair Value Adjustments:	
Reserve for Doubtful Accounts	(10,208)
Present Value Discount	(182,228)
	$ 4,245,807

Bequests Receivable

The Academy anticipates bequests receivable to be collected in the following years:

Year ending December 31:

2019	$ 4,475,159
2020-2024	2,695,000
2025-2029	300,000
Thereafter	155,000
	7,625,159
Less Fair Value Adjustment:	
Present Value Discount	(483,524)
	$ 7,141,635

Contributions Receivable – Conditional and Revocable

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

On September 1, 1990, the Ridley - Tree Foundation set up a scholarship fund of $50,000 in the name of the Academy. The Ridley - Tree Foundation has subsequently added an additional $275,000 to the original contribution amount. The earnings of the fund are paid to the Academy semiannually. Due to the revocable nature of the arrangement the principal amount held by

Paine Webber has not been recorded as an asset of the Academy, nor has the principal been recorded as a contribution to the Academy.

Note 3: Fair Value Measurements and Disclosures

The Academy reports certain assets at fair value in the financial statements. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal, or most advantageous, market at the measurement date under current market conditions regardless of whether that price is directly observable or estimated using another valuation technique. Inputs used to determine fair value refer broadly to the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability based on the best information available. A three-tier hierarchy categorizes the inputs as follows:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities that The Academy can access at the measurement date.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, and market-corroborated inputs.

Level 3 – Unobservable inputs for the asset or liability. In these situations, The Academy develops inputs using the best information available in the circumstances.

In some cases, the inputs used to measure the fair value of an asset or a liability might be categorized within different levels of the fair value hierarchy. In those cases, the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement. Assessing the significance of a particular input to entire measurement requires judgment, taking into account factors specific to the asset or liability. The categorization of an asset within the hierarchy is based upon the pricing transparency of the asset and does not necessarily correspond to management's assessment of the quality, risk, or liquidity profile of the asset or liability.

Investments

Valuation Methodology

To the extent available, the Academy's investments are recorded at fair value based on quoted prices in active markets on a trade-date basis. The Academy's investments that are listed on any U.S. or non-U.S. recognized exchanges are valued based on readily available market quotations. When such inputs do not exist, fair value measurements are based on the best available information and usually require a degree of judgment. For alternative investments, which are principally private equity and hedge funds, the value is primarily based on the Net Asset Value (NAV) of the underlying investments. The NAV is reported by the external investment managers, including general partners, in accordance with their policies as described in their respective financial statements and offering memoranda. The most recent NAV reported is adjusted for capital calls, distributions and significant known valuation changes, if any, of its related portfolio through the end of the fiscal year. These investments are generally less liquid than other investments, and the value reported may differ from the values that would have been reported had a ready market for these investments existed.

The Academy exercises due diligence in assessing the policies, procedures, and controls implemented by its external investment managers and believes the Academy's proportionate share of the carrying amount of these alternative investments is a reasonable estimate of fair value. Such due diligence procedures include, but are not limited to, ongoing communication and review of information from the external investment managers as well as review of performance. In conjunction with these procedures, estimated fair value is determined by consideration of a wide range of factors, such as market conditions, redemption terms and restrictions, and risks inherent in the inputs of the external investment managers' valuation.

For alternative investments which are direct investments in closed ended funds, the Academy considers various factors to estimate fair value, such as, but not limited to, the timing of the transaction, the market in which the company operates, comparable transactions, company performance and projections as well as discounted cash flow analysis. The selection of an appropriate valuation technique may be affected by the availability and general reliability of relevant inputs. In some cases, one valuation technique may provide the best indication of fair value while in other circumstances, multiple valuation techniques may be appropriate. Furthermore, the Academy may review the investment's underlying portfolio as well as engage external appraisers, depending on the nature of the investment.

Derivative Activity

The Academy has approved the use of derivatives by outside investment managers, based on investment guidelines negotiated at the time of a manager's appointment. The derivatives are used to adjust fixed income durations and rates, to create "synthetic exposures" to certain types of investments, and to hedge inflation fluctuations. The Academy records the fair value of a derivative instrument within the applicable portfolio. The change in the fair value of a derivative instrument held for investment is included in investment return in the statement of activities.

Investment Related Commitments

The Academy is obligated under certain alternative investment agreements to advance additional funding up to specified levels over a period of several years. At December 31, 2018 the Academy is obligated to advance an additional $991,555 under such agreements.

Contributions and Bequests Receivable

Valuation Methodology

Contributions and bequests receivable fair value are estimated using present valuation techniques based on a discount rate of 2.5% as well as an estimated reserve for uncollectible contributions receivable.

Valuation Hierarchy

The following table presents assets and liabilities measured at fair value on a recurring basis, except those measured at cost or by using net asset value per share as a practical expedient as identified in the following, at December 31, 2018:

	Level 1	Level 2	Level 3	NAV
Investments				
Mutual funds –				
fixed income	$ 3,051,261	$ -	$ -	$
equity	18,063,676	-	-	-
Overlay funds	-	-	-	2,047,797
Closed ended funds	-	-	-	5,223,016
Hedge funds	-	-	-	1,930,747
Private equity funds	-	-	-	217,412
Corporate bonds	4,482,107	-	-	-
U.S. federal agencies debt instruments	448,242	-	-	-
U.S. Treasury notes	1,512,307	-	-	-
Treasury inflation Protected securities	2,006,262	-	-	-
Total Investments	29,563,855	-	-	9,418,972
Contributions and bequests receivable	-	-	11,387,442	-
Contributions in trust	-	-	3,814,259	-
Totals	$ 29,563,855	$ -	$ 15,201,701	$ 9,418,972

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

Contributions and Bequests Receivable

Balance at beginning of year	$ 10,542,482
Additions	6,172,523
Collections	(5,327,563)
Balance at end of year	$ 11,387,442

Contributions in Trust

Balance at beginning of year	$ 4,173,645
Additions	-
Unrealized loss	(359,386)
Balance at end of year	$ 3,814,259

Note 4: Liquidity and Availability

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

Operating cash and cash Equivalents without donor restrictions	$ 5,249,914
Contributions and bequests receivable to be collected in 2019	6,940,902
Endowment spending-rate distributions and appropriations	1,357,122
Total	$ 13,547,938

The Academy Endowment funds consist of Board Designated and donor restricted endowments which are subject to an annual spending policy as described in Note 10.

Note 5: Fixed Assets

Fixed Assets at December 31, 2018 are summarized by major classifications as follows:

Land and improvements	$ 505,736
Buildings	43,202,098
Furniture, fixtures and equipment	1,551,749
Construction in process	7,273
Library text and music	18,612
Instruments	2,617,940
Vehicles	43,153
	47,946,561
Less Accumulated Depreciation	(9,409,873)
Fixed Assets, Net	$ 38,536,688

Depreciation expense for the year ended December 31, 2018 and 2017 was $1,129,169 and $1,105,339, respectively.

Note 6: Other Investment

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

Note 7: Contributions in Trust

During the year ended September 30, 1991, a pooled income trust fund was established. The present value of the trust as of the date of the contribution was $4,444. At December 31, 2018, the fair market value of the Academy's share of trust assets was $55,380. These assets are recorded as net assets with donor restrictions.

During the year ended December 31, 2005, the Academy was named as a 20% beneficiary of the Maximus Fund to be held by the Santa Barbara Foundation. The Academy is to receive an annual payment equal to 5% of the fund's fair market value as determined on January 1 of each year. The estimated fair market value of the gift has been determined to equal the underlying assets at the time of the gift. The Academy has recorded the gift as an increase to net assets with donor restrictions. The Academy's share of the net assets of the fund at December 31, 2018 was $2,389,723.

During the year ended December 31, 2012, the Academy was named as a 20% beneficiary of the Thomas E & Elenor H. Hugunin Endowment Fund to be held by the Santa Barbara Foundation. The Academy is to receive an annual payment equal to 5% of the fund's fair market value as determined on January 1 of each year. The estimated fair market value of the gift has been determined to equal the underlying assets at the time of the gift. The Academy has recorded the gift as an increase to net assets with donor restrictions. The Academy's share of the net assets of the fund at December 31, 2018 was $1,369,156.

For the year ended December 31, 2018, the Academy reported a decrease in value in the value of contributions in trust of $359,386 as part of contributions.

Note 8: Note Payable

In September 2012, the Academy entered into a note payable agreement with First Republic Bank. Under the agreement the Academy borrowed $15,200,000. The note payable bears interest at 3.65% per annum, is to be repaid with monthly principal and interest payments of $79,221 and matures in September 2036. The proceeds of the note were used to retire $14,884,925 of certificates of participation. In connection with the note payable, the Academy incurred $298,661 of issuance costs which are being amortized over the life of the note. At December 31, 2018 the Academy reported unamortized loan issuance costs of $220,367. The note payable is secured by a lien on all of the Academy's assets other than its real property and permanently restricted assets. The note requires the Academy to maintain liquidity of $14,000,000.

Minimum maturities of the note payable are as follows:

2019	$ 506,355
2020	523,936
2021	544,597
2022	564,810
2023	585,774
Thereafter	9,681,105
Total minimum maturities	12,406,577
Less unamortized debt issuance costs	(220,367)
Note payable, net	$ 12,186,210

The Academy reported $12,444 of amortization of the debt issuance costs as interest expense

Note 9: Designations and Restrictions of Net Assets

Board Designated Net Assets

The Board of Directors have designated net without donor restrictions for the following purposes:

Future loan repayments	$ 4,098,514
Campus maintenance	1,755,015
Future operations – Endowment subject to endowment spending policy	31,203,161
Total board designated funds	$ 37,056,690

Net Assets with Donor Restrictions

Net assets with donor restrictions temporary in nature are restricted for the following purpose or periods:

Purpose Restrictions:	
Building construction	$ 95,000
AVF Program	457,500
London Symphony Orchestra Partnership	2,617,086
Various programs	469,082
Other restrictions	195,587
	3,834,255
Time Restricted for Future Period:	
Contributions and bequest receivable without donor purpose Restrictions	9,055,708
Contributions in trust	3,814,259
Endowments:	
Subject to Endowment Policy and Appropriation:	
Building and maintenance	1,749,824
Scholarship	53,513
Total donor restricted net assets – temporary in nature	$ 18,507,559

Net assets with donor restrictions permanent in nature the income from which are restricted for scholarships totaled $510,000 at December 31,2018.

Note 10: Endowment Funds

The Academy's Endowment (the Endowment) consists of board designated funds and funds with donor restrictions. The endowment was established for the specific purpose of long-term stability and insuring the continuance of the mission of The Academy. As required by generally accepted accounting principles (GAAP), net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The Board of Directors of the Academy has interpreted the California 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. At December 31, 2018, there were no such donor stipulations. As a result of this interpretation, The Academy retains in perpetuity (a) the original value of initial and subsequent gift amount (including contributions receivable at fair value donated to the Endowment and (b) any accumulations to the Endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added. Donor-restricted amounts not retained in perpetuity are subject to appropriation for expenditure by The Academy in a manner consistent with the standard of prudence prescribed by UPMIFA. The Academy considers the following factors in making a determination to appropriate or accumulate Donor-Restricted Endowment Funds:

- The duration and preservation of the fund
- The purposes of The Academy and the fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of Academy
- The investment policies of Academy

Funds with Deficiencies

From time to time, certain Donor-Restricted Endowment Funds may have fair values less than the amount required to be maintained by donors or by law (underwater endowments). Academy has interpreted UPMIFA to permit spending from underwater endowments in accordance with prudent measures required under law. At December 31, 2018, there were no endowment funds underwater.

Changes in Endowment Assets

Changes in Endowment Net Assets for the year ended December 31, 2018 are as follows:

	Without Donor Restriction	With Donor Restriction
Endowment Net Assets, Beginning of Year	$ 33,947,748	$ 3,942,261
Contributions	4,014,852	100,000
Investment income	(553,976)	(33,915)
Draw per Spending Policy	(1,287,047)	(251,028)
Reclassifications	(4,918,416)	(1,443,981)
Endowment Net Assets, End of Year	$ 31,203,161	$ 2,313,337

During the year ended December 31, 2018 management completed a research project regarding endowment assets. Management identified assets that had been previously reported as endowment assets subject to the Academy's spending policy that were either designated by the Board of Directors or restricted by donors for a specific purpose but not restricted to the Academy's endowment. The amount of the those identified assets have been reclassified to board designated or with donor restriction net assets according to the nature of the net asset group.

Investment and Spending Policies

Endowment funds may be appropriated for expenditure in amounts not to exceed, on an annual basis, four percent of the endowment's total average value for the preceding calendar year. The Board of Directors may, at its own discretion, appropriate for expenditure an amount that exceeds the four percent threshold.

Note 11: Employee Benefits

In 2001, the Academy adopted The Music Academy of the West Tax-Deferred Annuity Plan under section 403(b) of the Internal Revenue Code. Eligible employees are at minimum twenty-one years of age, have completed one year of service, and work full time. The Academy matches employee contributions 100% for the first 5% of deferred salary. Retirement plan contributions and operating expenses for the year ended December 31, 2018 was $82,206.

Note 12: Customer and Credit Risk Concentrations

Academy manages deposit concentration risk by placing cash, money market accounts, and certificates of deposit with financial institutions believed by management to be creditworthy. At times, amounts on deposit may exceed insured limits or include uninsured investments in money market mutual funds. To date, Academy has not experienced losses in any of these accounts. Credit risk associated with contributions receivable is considered to be limited due to high historical collection rates. Investments are made by diversified investment managers whose performance is monitored by Academy and the Investment Committee of the Board of Directors. Although the fair values of investments are subject to fluctuation on a year-to-year basis, management and the Investment Committee believe that the investment policies and guidelines are prudent for the long-term welfare of Academy.

Academy maintains bank account at various local financial institutions. The deposits at the institution are insured by the Federal Deposit Insurance Corporation up to $250,000. Cash balances held in brokerage accounts are insured by the Securities Investor Protection Corporation (SIPC) up to $250,000 per institution. From time to time cash held during the year exceeded the insured thresholds. At December 31, 2018 Academy held $2,515,040 of cash deposits in excess of FDIC insurance limits.

Note 13: Commitments

Operating Leases

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

Line of Credit

The Academy has available a bank line of credit for any amount up to $1,500,000 at December 31, 2018. The line of credit is secured by a lien on all of the Academy's assets other than its real property and permanently restricted assets. Draws on the line of credit bear interest at 4.5%. The Academy did not draw on the line during the year ended December 31, 2018. The line of credit expires June 30, 2019. The Academy plans to renew the line of credit upon expiration (see note 1 for subsequent event discussion).