Indianapolis Museum of Art

Accountants' Report and Consolidated Financial Statements

June 30, 2012 and 2011

Indianapolis Museum of Art
June 30, 2012 and 2011

Contents

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Independent Accountants' Report

Board of Governors
Indianapolis Museum of Art
Indianapolis, Indiana

We have audited the accompanying consolidated statements of financial position of Indianapolis Museum of Art (Museum) as of June 30, 2012 and 2011, and the related consolidated statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Museum's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Indianapolis Museum of Art as of June 30, 2012 and 2011, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

BKD, LLP

December 4, 2012

Indianapolis Museum of Art

Consolidated Statements of Financial Position

June 30, 2012 and 2011

(In Thousands)

Assets

	2012	2011
Cash	$ 458	$ 3,361
Accounts receivable	289	403
Contributions receivable	3,893	3,841
Government grant reimbursements receivable	101	500
Inventories	538	596
Prepaid expenses	1,098	679
Investments	330,464	354,099
Estate notes and charitable lead trusts	13,866	14,891
Unamortized bond issue costs	808	840
Library accessions	1,029	978
Property and equipment	124,382	129,541
Collections - Note 1	-	-
Total assets	$ 476,926	$ 509,729

Liabilities

	2012	2011
Accounts payable	$ 967	$ 1,131
Accrued salaries, wages and employee benefits	978	911
Accrued pension expense	4,482	2,406
Deferred revenue	597	696
Other liabilities	931	1,020
Fair value of interest rate swap	5,976	2,324
Tax-exempt bonds payable	122,600	122,600
Total liabilities	136,531	131,088

Net Assets

	2012	2011
Unrestricted	96,672	116,225
Temporarily restricted	114,610	133,453
Permanently restricted	129,113	128,963
Total net assets	340,395	378,641
Total liabilities and net assets	$ 476,926	$ 509,729

Indianapolis Museum of Art

Consolidated Statements of Activities
Years Ended June 30, 2012 and 2011
(In Thousands)

	2012			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue, Gains and Other Support				
Gifts, grants and memberships				
Annual giving, including memberships	$ 1,384	$ -	$ -	$ 1,384
Other contributions	1,626	1,768	150	3,544
Grants	327	-	-	327
Revenue from activities				
Admissions, fees and sales	2,669	28	-	2,697
Investment return designated for current operations and art acquisitions	4,079	16,168	-	20,247
	10,085	17,964	150	28,199
Net assets released from restrictions	16,337	(16,337)	-	-
Total revenue, gains and other support	26,422	1,627	150	28,199
Expenses				
Curatorial	9,853	-	-	9,853
Educational	6,513	-	-	6,513
Horticultural	1,593	-	-	1,593
Museum stores	1,624	-	-	1,624
Management and general	2,988	-	-	2,988
Fundraising	1,571	-	-	1,571
Total expenses	24,142	-	-	24,142
Change in Net Assets Before Depreciation and Interest	2,280	1,627	150	4,057
Depreciation	6,362	-	-	6,362
Interest	1,391	-	-	1,391
Total depreciation and interest	7,753	-	-	7,753
Change in Net Assets From Operations	(5,473)	1,627	150	(3,696)
Nonoperating Revenue (Expense)				
Investment return greater than (less than) amounts designated for current operations and art acquisitions	(8,196)	(19,990)	-	(28,186)
Changes in projected benefit obligation arising during the period	(1,718)	-	-	(1,718)
Amortization included in net periodic pension cost	(394)	-	-	(394)
Change in fair value of interest rate swap agreement	(3,652)	-	-	(3,652)
Proceeds from sales of art	6	108	-	114
Purchases of art	(714)	-	-	(714)
Net assets released from restriction - art acquisition	588	(588)	-	-
Net asset reclassifications	-	-	-	-
Change in Net Assets	(19,553)	(18,843)	150	(38,246)
Net Assets, Beginning of Year	116,225	133,453	128,963	378,641
Net Assets, End of Year	$ 96,672	$ 114,610	$ 129,113	$ 340,395

2011			
Unrestricted	Temporarily Restricted	Permanently Restricted	Total
$ 1,315	$ -	$ -	$ 1,315
1,433	8,944	3,721	14,098
857	-	-	857
2,837	171	-	3,008
79	14,937	-	15,016
6,521	24,052	3,721	34,294
18,438	(18,438)	-	-
24,959	5,614	3,721	34,294
11,233	-	-	11,233
6,197	-	-	6,197
1,530	-	-	1,530
1,691	-	-	1,691
2,726	-	-	2,726
1,274	-	-	1,274
24,651	-	-	24,651
308	5,614	3,721	9,643
6,227	-	-	6,227
1,676	-	-	1,676
7,903	-	-	7,903
(7,595)	5,614	3,721	1,740
23,749	22,800	-	46,549
382	-	-	382
619	-	-	619
367	-	-	367
-	313	-	313
(1,351)	-	-	(1,351)
1,251	(1,251)	-	-
8,316	(16,263)	7,947	-
25,738	11,213	11,668	48,619
90,487	122,240	117,295	330,022
$ 116,225	$ 133,453	$ 128,963	$ 378,641

Indianapolis Museum of Art

Consolidated Statements of Cash Flows
Years Ended June 30, 2012 and 2011
(In Thousands)

	2012	2011
Operating Activities		
Change in net assets	$ (38,246)	$ 48,619
Items not requiring (providing) cash		
Depreciation and amortization of bond issue costs	6,362	6,227
Noncash contributions	(113)	(90)
Loss on disposal of property and equipment	217	-
Acquisition and sales of art, net	600	1,038
Contributions restricted for long-term investment	(2,561)	(6,678)
Realized gains on investments	(2,660)	(11,665)
Unrealized (gains) losses on investments	11,571	(48,514)
Change in fair value of interest rate swap agreement	3,652	(367)
Changes in		
Accounts receivable	513	(307)
Contributions receivable	(52)	720
Prepaid expenses and other assets	(361)	(329)
Estate notes and charitable lead trusts	1,025	(4,506)
Accounts payable	(137)	(805)
Accrued expenses and other liabilities	2,010	(900)
Net cash used in operating activities	(18,180)	(17,557)
Investing Activities		
Acquisitions of art	(714)	(1,351)
Proceeds from sale of art	114	313
Purchases of property and equipment	(1,498)	(5,735)
Purchases of investments	(49,056)	(202,645)
Sales and maturities of investments	63,893	222,450
Net cash provided by investing activities	12,739	13,032
Financing Activities		
Proceeds from contributions restricted for		
Investments in endowment	1,828	4,624
Investments in art and property and equipment	93	158
Investments subject to annuity and trust agreements	585	(25)
Investments subject to various purchases	55	1,921
Payments on capital lease obligations	(23)	(38)
Net cash provided by financing activities	2,538	6,640
Increase (Decrease) in Cash	(2,903)	2,115
Cash, Beginning of Year	3,361	1,246
Cash, End of Year	$ 458	$ 3,361
Supplemental Information		
Interest paid	$ 1,384	$ 1,885
Property and equipment in accounts payable	112	139

Note 1: Nature of Operations and Summary of Significant Accounting Policies

General

Indianapolis Museum of Art (Museum) was incorporated as a not-for-profit organization in May 1892, under the laws of the State of Indiana.

The consolidated financial statements include the accounts of the Indianapolis Museum of Art and Oldfields, LLC, its wholly owned subsidiary. Oldfields, LLC was established during 2004 to hold certain real estate. The consolidated financial statements also include the Museum's affiliated organizations: Alliance of the Indianapolis Museum of Art, the Asian Art Society, the Contemporary Art Society, the Design Arts Society, the Fashion Arts Society and the Horticultural Society. The affiliated organizations are special interest groups within the Museum membership which operate for the benefit of the Museum donating cash and services of volunteers to various Museum activities. No amounts are included in the consolidated financial statements for services of volunteers.

The Museum provides art education opportunities for its members and the general public through the acquisition, preservation and exhibition of its permanent collections. The Museum's primary sources of revenue and support are contributions and earnings on investments.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of the revenues, expenses, gains, losses and other changes in net assets during the reporting period. Actual results could differ from those estimates.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the Museum has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Museum in perpetuity.

Cash

Effective July 21, 2010, the FDIC's insurance limits were permanently increased to $250,000. At June 30, 2012, the Museum's cash accounts exceeded federally insured limits by approximately $893,000.

Investments and Investment Return

Investments are carried at fair value. For those investments without quoted market prices, the fair value was provided by the managers of the investment funds. These estimated values are subject to uncertainty, and therefore, may differ significantly from the value that would have been used had a market for such investments existed. Such differences could be material. Investment return includes dividend, interest and other investment income and realized and unrealized gains and losses.

Investment return is reflected in the consolidated statements of activities as unrestricted, temporarily restricted or permanently restricted based upon the existence and nature of any donor or legally imposed restrictions.

The Museum maintains pooled investment accounts for its endowments. Investment income and realized and unrealized gains and losses from securities in the pooled investment accounts are allocated quarterly to the individual endowments based on the relationship of the fair value of the interest of each endowment to the total fair value of the pooled investment accounts, as adjusted for additions to or deductions from those accounts.

Property and Equipment

Expenditures for property and equipment and items which substantially increase the useful lives of existing assets are capitalized at cost. The Museum provides for depreciation on the straight-line method at rates designed to depreciate the costs of assets over estimated useful lives as follows:

Furnishings and equipment	10 years
Buildings and grounds	50 years
Land improvements	20 years

Long-Lived Asset Impairment

The Museum evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value. No asset impairment was recognized during the years ended June 30, 2012 or 2011.

Collections - Art Objects

According to the Museum's policy, collections include all works of art, historical treasures, library accessions and similar assets that are (a) held for public service rather than financial gain, (b) protected, kept unencumbered, cared for and preserved, and (c) subject to the Museum's policy that requires the proceeds of items that are sold to be used to acquire other items for collections. The collections, which have been acquired through purchases and contributions since the Museum's inception, are not recognized as an asset on the consolidated statements of financial position. Purchases of collection items are recorded as decreases in unrestricted or temporarily restricted net assets in the year in which the items are acquired. Proceeds from deaccessions or insurance recoveries, if any, are reflected as increases in the appropriate net asset class.

Income Taxes

The Museum is exempt from federal income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. The Museum is not considered to be a private foundation. However, the Museum is subject to federal income tax on any unrelated business taxable income.

The Museum files tax returns in the U.S. federal jurisdiction. With a few exceptions, the Museum is no longer subject to U.S. federal, state and local or non-U.S. income tax examinations by tax authorities for years before 2009.

Contributions Receivable

Unconditional promises to give are recognized as revenues or gains in the period received and as assets, decreases of liabilities or expenses depending on the form of the benefits received.

While contributions, including promises to give, are required to be recorded as revenue in the year received, expenses funded by such contributions normally occur in subsequent years. This means fluctuations between years in the amount of contributions received or receivable can have a significant impact on the total change in net assets of the Museum, as can the timing of program expenses which result therefrom. Management reviews promises to give and writes off any promises at the time they become uncollectible past their due date. The Museum has estimated an allowance for uncollectible promises to give of $175,000 as of June 30, 2012 and 2011.

Support and Revenue

The Museum reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions. Gifts and investment income that are originally restricted by the donor and for which the restriction is met in the same time period are recorded as temporarily restricted and then released from restriction.

Estate Notes and Charitable Lead Trusts

The Museum is the beneficiary under various estate notes and charitable lead trusts. Estate notes represent an irrevocable pledge (or debt) against a donor's estate, to the extent the pledge is not satisfied during the donor's lifetime. Estate notes are initially recorded at fair value determined by using the discounted present value of the amounts to be received in the future. The resulting discount is amortized using the level-yield method and is reported as contribution revenue. Discount rates utilized were 1.07% to 8.23% for 2012 and 2011. Charitable lead trusts are arrangements in which a donor establishes and funds a trust to provide distributions to a designated beneficiary organization for a specified period of time. Upon termination of the trust, the remainder of the trust assets is paid to the donor or to another beneficiary designated by the donor. Charitable lead trusts administered by the Museum are recorded at fair value only upon initial recognition, while those being administered by third parties are adjusted to fair value annually using discount rates based on current market conditions.

Donated Property and Equipment

The Museum reports gifts of land, buildings and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts 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 regarding how long those long-lived assets must be maintained, the Museum reports expirations of donor restrictions as the donated or acquired long-lived assets are placed in service.

Government Grants

Support funded by grants is recognized as the Museum performs the contracted services under grant agreements. Grant revenue is recognized as earned as the eligible expenses are incurred. Grant expenditures are subject to audit and acceptance by the granting agency and, as a result of such audit, adjustments could be required.

Functional Expenses

In 2012 and 2011, expenses have been classified as program services, management and general, fund raising and membership development based on the actual direct expenditures and cost allocations based upon estimates of salaries incurred by Museum personnel.

Transfers Between Fair Value Hierarchy Levels

Transfers in and out of Level 1 (quoted market prices), Level 2 (other significant observable inputs) and Level 3 (significant unobservable inputs) are recognized on the actual date of transfer.

(Table Dollar Amounts in Thousands)

Reclassifications

Certain reclassifications have been made to the 2011 consolidated financial statements to conform to the 2012 consolidated financial statement presentation. These reclassifications had no effect on the change in net assets.

Subsequent Events

Subsequent events have been evaluated through the date of the Independent Accountants' Report, which is the date the consolidated financial statements were available to be issued.

Note 2: Contributions Receivable

	2012		
	Temporarily Restricted	Permanently Restricted	Total
Due within one year	$ 1,005	$ 500	$ 1,505
Due in one to five years	951	2,000	2,951
	1,956	2,500	4,456
Discount	(69)	(319)	(388)
Allowance	(175)	-	(175)
	$ 1,712	$ 2,181	$ 3,893

	2011		
	Temporarily Restricted	Permanently Restricted	Total
Due within one year	$ 845	$ 500	$ 1,345
Due in one to five years	673	2,000	2,673
Due in more than five years	-	500	500
	1,518	3,000	4,518
Discount	(63)	(439)	(502)
Allowance	(175)	-	(175)
	$ 1,280	$ 2,561	$ 3,841

Discount rates ranged from 0.23 to 4.9 percent in 2012 and 0.75 to 5.0 percent in 2011.

(Table Dollar Amounts in Thousands)

Note 3: Investments

The fair value of the Museum's investments are as follows:

	2012	2011
Savings accounts	$ 174	$ 163
Certificates of deposit	247	246
Short-term investments	4,462	5,433
Corporate bonds	782	1,204
Corporate stocks		
Domestic	22,134	27,129
International	2,668	3,691
Mutual funds		
Equity - domestic	233	365
Equity - international	25,048	36,958
Fixed income	14,896	19,429
Alternative investments		
Equity - international	40,373	45,181
Fixed income	10,771	10,973
Absolute return marketable alternatives	43,847	42,296
Equity-oriented marketable alternatives	60,341	61,468
Inflation hedging	58,579	61,662
Private equity/Venture capital	43,010	35,002
Real estate held for investment	2,899	2,899
Total	$ 330,464	$ 354,099

The following schedules summarize the investment return and its classification in the consolidated statements of activities for the years ended June 30, 2012 and 2011:

	2012		
	Unrestricted	Temporarily Restricted	Total
Dividends and interest (net of expenses of $2,973)	$ 352	$ 620	$ 972
Net realized gains on investments	897	1,763	2,660
Net unrealized losses on investments	(5,366)	(6,205)	(11,571)
Total return on investments	(4,117)	(3,822)	(7,939)
Investment return designated for			
Current operations	(4,221)	(15,133)	(19,354)
Art acquisitions	142	(1,035)	(893)
Investment return less than amounts designated for current operations and art acquisitions	$ (8,196)	$ (19,990)	$ (28,186)

(Table Dollar Amounts in Thousands)

	2011 Unrestricted	2011 Temporarily Restricted	2011 Total
Dividends and interest (net of expenses of $4,280)	$ 495	$ 891	$ 1,386
Net realized gains on investments	4,040	7,625	11,665
Net unrealized gains on investments	19,293	29,221	48,514
Total return on investments	23,828	37,737	61,565
Investment return designated for			
Current operations	(197)	(14,215)	(14,412)
Art acquisitions	118	(722)	(604)
Investment return greater than amounts designated for current operations and art acquisitions	$ 23,749	$ 22,800	$ 46,549

Note 4: Property and Equipment

The Museum's property and equipment are as follows:

	2012	2011
Buildings and grounds	$ 166,232	$ 165,201
Furnishings and equipment	21,782	21,288
Land improvements	12,368	12,368
	200,382	198,857
Accumulated depreciation	(76,922)	(70,560)
	123,460	128,297
Land	922	922
Construction in progress	-	322
	$ 124,382	$ 129,541

Note 5: Tax-Exempt Bonds Payable

During 2001, the Indiana Finance Authority (the Authority) issued Variable Rate Demand Educational Facilities Revenue Bonds amounting to $30,000,000, the proceeds of which were loaned to the Museum in order to finance and reimburse all or a portion of the costs of the acquisition, construction, installation, rehabilitation, renovation or enlargement of land, site improvements, infrastructure improvements, buildings, structures, machinery, equipment, furnishings or facilities comprising or being functionally related to the operation of the Museum. The bonds are due February 1, 2036, and are secured by a letter of credit.

During 2002, the Authority issued an additional $44,000,000 of Variable Rate Demand Educational Facilities Revenue Bonds, the proceeds of which were loaned to the Museum to continue the construction projects noted above. These bonds are due February 1, 2037, and are also secured by a letter of credit.

During 2004, the Authority issued an additional $51,000,000 of Variable Rate Demand Educational Facilities Revenue Bonds, the proceeds of which were loaned to the Museum to continue the construction projects noted above. These bonds are due February 1, 2039, and are also secured by a letter of credit.

The total outstanding balance of the aforementioned bonds at June 30, 2012 and 2011 was $122,600,000. The bonds are subject to remarketing agreements. In the event of a remarketing failure, the bonds would be repaid through a draw on the letter of credit. The interest rate applicable to such a loan would be prime rate, and would be in effect until the bonds could be remarketed. In the event the bonds could not be remarketed, repayment of the advance could be deferred until the earlier of 180 days or maturity of the letter of credit. The letters of credit expire September 15, 2014.

Under the Indenture, the bond issues may operate in one or more of four Modes of Operation provided that certain requirements are met. The four modes generally have different operating features, including different demand features, purchase features, redemption provisions, interest periods and interest payment dates. At June 30, 2012, the bonds were operating under the floating rate mode whereby the interest rate is adjusted weekly and interest is payable monthly. At June 30, 2012, the interest rate on these bonds was 0.18%.

Costs associated with executing the loan and other agreements with the aforementioned parties have been classified as unamortized bond issue costs in the accompanying consolidated financial statements and are being amortized over the life of the bonds using a method that approximates the level yield method.

The bonds are subject to certain covenants, including a financial coverage ratio. At June 30, 2012, the Museum was in compliance with these financial covenants.

Note 6: Derivative Financial Instruments

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations, the Museum has entered into interest rate swap agreements for a portion of its floating rate debt. The agreements provide for the Museum to receive interest from the counterparty at LIBOR times 70% and to pay interest to the counterparty at fixed rates ranging between 1.890% and 2.911% on the notional amount of $55,000,000. Under the agreements, the Museum pays or receives the net interest amount monthly, with the monthly settlements included in interest expense. The agreements have expirations ranging from 2016 to 2024.

(Table Dollar Amounts in Thousands)

The table below presents certain information regarding the Museum's interest rate swap agreement:

	2012	2011
Fair value of interest rate swap agreements	$ 5,976	$ 2,324
Statement of financial position location of fair value amount	Liability	Liability
Gain (loss) recognized in change in net assets	(3,652)	367
Location of loss recognized in change in net assets	Nonoperating revenue (expense)	Nonoperating revenue (expense)

Note 7: Temporarily Restricted Net Assets

Temporarily restricted net assets are available for the following purposes or periods:

	2012	2011
Program activities		
Art purchases	$ 12,573	$ 11,135
Educational program activities	494	527
Other program activities	3,289	3,501
Facility operations and personnel	3,986	7,220
Unappropriated endowment earnings	84,430	100,309
For periods after June 30	9,838	10,761
	$ 114,610	$ 133,453

Note 8: Permanently Restricted Net Assets

Permanently restricted net assets are restricted to:

	2012	2011
Investment in perpetuity, the income of which is expendable to support		
Art purchases	$ 19,148	$ 19,885
Educational program activities	613	613
Other program activities	3,470	3,470
Facility operations and personnel	44,635	44,016
Any activity of the Museum	61,247	60,979
	$ 129,113	$ 128,963

(Table Dollar Amounts in Thousands)

Note 9: Net Assets Released From Restrictions

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors.

	2012	2011
Purpose restrictions accomplished		
Curatorial program expenses	$ 539	$ 1,274
Educational program expenses	84	378
Other program expenses	190	1,033
Appropriation of accumulated endowment earnings	15,240	15,491
Time restrictions expired - passage of time	284	262
	16,337	18,438
Art acquisition	588	1,251
	$ 16,925	$ 19,689

Note 10: Net Asset Reclassifications

During the fiscal year 2011 and in conjunction with the implementation of its new endowment management software, Museum staff performed an in-depth review of all of the Museum's endowment funds. In so doing, Museum staff researched the original designations and/or restrictions assigned to each fund. Pursuant to this review, certain net assets were reclassified during the year. Reclassifications from temporarily restricted net assets to permanently restricted net assets, amounting to $8,021,620, resulted from the discovery of additional donor-related documentation that supported a classification as permanently restricted. All other reclassifications were primarily due to changes in net assets released from restrictions. The net effect of the latter was to increase unrestricted net assets by $8,316,000 and to decrease temporarily and permanently restricted net assets by $8,241,380, and $74,620, respectively.

Note 11: Endowment

The Museum's endowment consists of approximately 130 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the governing body to function as endowments (board-designated endowment funds). Temporarily restricted board-designated endowment funds include funds with purpose or time restrictions that the board has designated to function as endowment funds. As required by accounting principles generally accepted in the United States of America (GAAP), net assets associated with endowment funds, including board-designated endowment funds, are classified and reported based on the existence or absence of donor-imposed restrictions.

(Table Dollar Amounts in Thousands)

The Museum's governing body has interpreted the State of Indiana Prudent Management of Institutional Funds Act (SPMIFA) as requiring 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 donor-restricted endowment funds is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Museum in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, the Museum considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. Duration and preservation of the fund
2. Purposes of the Museum and the fund
3. General economic conditions
4. Possible effect of inflation and deflation
5. Expected total return from investment income and appreciation or depreciation of investments
6. Other resources of the Museum
7. Investment policies of the Museum

The composition of net assets by type of endowment fund at June 30, 2012 and 2011, was:

	2012			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ (2,170)	$ 92,090	$ 121,959	$ 211,879
Board-designated endowment funds	114,447	-	-	114,447
Total endowment funds	$ 112,277	$ 92,090	$ 121,959	$ 326,326

	2011			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ (814)	$ 112,036	$ 120,132	$ 231,354
Board-designated endowment funds	120,968	-	-	120,968
Total endowment funds	$ 120,154	$ 112,036	$ 120,132	$ 352,322

(Table Dollar Amounts in Thousands)

Changes in endowment net assets for the years ended June 30, 2012 and 2011 was:

	2012			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ 120,154	$ 112,036	$ 120,132	$ 352,322
Investment return				
Investment income	1,233	2,383	-	3,616
Net depreciation	(4,012)	(7,517)	-	(11,529)
Total investment return	(2,779)	(5,134)	-	(7,913)
Contributions	577	-	1,827	2,404
Appropriation of endowment assets for expenditure	(4,079)	(16,168)	-	(20,247)
Transfers for underwater funds	(1,356)	1,356	-	-
Transfers out of endowment	(240)	-	-	(240)
Endowment net assets, end of year	$ 112,277	$ 92,090	$ 121,959	$ 326,326

	2011			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	$ 90,837	$ 108,542	$ 108,685	$ 308,064
Investment return				
Investment income	464	632	-	1,096
Net appreciation	21,112	37,548	-	58,660
Total investment return	21,576	38,180	-	59,756
Contributions	212	92	4,642	4,946
Appropriation of endowment assets for expenditure	(79)	(14,937)	-	(15,016)
Reclassification of restrictions	6,598	(14,545)	7,947	-
Transfers for underwater funds	2,574	(2,574)	-	-
Transfers out of endowment	(1,564)	(2,722)	(1,142)	(5,428)
Endowment net assets, end of year	$ 120,154	$ 112,036	$ 120,132	$ 352,322

(Table Dollar Amounts in Thousands)

Amounts of donor-restricted endowment funds classified as permanently and temporarily restricted net assets at June 30, 2012 and 2011 consisted of:

	2012	2011
Permanently restricted net assets - portion of perpetual endowment funds required to be retained permanently by explicit donor stipulation or SPMIFA	$ 121,959	$ 120,132
Temporarily restricted net assets - portion of perpetual endowment funds subject to a time restriction under SPMIFA		
With purpose restrictions	$ 7,660	$ 11,727
Without purpose restrictions	84,430	100,309
	$ 92,090	$ 112,036

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level the Museum is required to retain as a fund of perpetual duration pursuant to donor stipulation or SPMIFA. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets and aggregated $2,170,000 and $814,000 at June 30, 2012 and 2011, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after investment of new permanently restricted contributions and continued appropriation for certain purposes that was deemed prudent by the governing body.

The Museum has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding for current operations, capital additions and artifact acquisitions supported by its endowment while seeking to maintain the purchasing power of the endowment. Endowment assets include those assets of donor-restricted endowment funds the Museum must hold in perpetuity or for donor-specified periods, as well as those of board-designated endowment funds. Under the Museum's policies, endowment assets are invested in a manner that is intended to produce results that exceed the spending rate plus inflation. The Museum expects its endowment funds to provide an average rate of return of approximately 8.5% annually over time. Actual returns in any given year may vary from this amount.

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 current yield (investment income such as dividends and interest) and capital appreciation (both realized and unrealized). The Museum targets a diversified asset allocation to assure no single security, class of securities or individual investment will have a disproportionate negative impact on the endowment's overall return.

(Table Dollar Amounts in Thousands)

The Museum has a policy (the spending policy) of appropriating for current operations each year 5.5% of its endowment fund's average fair value for the 12 quarters ended December 31 of the previous year. For the years ended June 30, 2012 and 2011, the Board of Governors approved a temporary increase in the spending rate to support current operations. Based on the 12-quarter average market value, the approved spending rates for operations were 7.95% and 8.30% for the years ended June 30, 2012 and 2011, respectively. All other restricted funds currently spend at or below 5.5%. In establishing this policy, the Museum considered the long-term expected return on its endowment. Accordingly, over the long-term, the Museum expects the current spending policy to allow its endowment to grow at an average of 3% annually. This is consistent with the Museum's objective to maintain the purchasing power of endowment assets held in perpetuity or for a specified term, as well as to provide additional real growth through new gifts and investment return.

For the separate funds in the donor-restricted art endowment, 5 percent of the average market value of such funds for the 12 quarters ending December 31 of the previous year is appropriated to support art acquisitions.

Note 12: Functional Expenses

Expenses by functional classification are as follows:

	2012	2011
Program services	$ 25,890	$ 27,024
Management and general	3,908	3,815
Fundraising	2,097	1,715
	$ 31,895	$ 32,554

Note 13: Employee Benefits

The Museum has a defined-contribution employee's retirement savings plan covering all full-time employees meeting certain eligibility requirements. The Museum makes contributions to the plan to match employee contributions and pays the cost of administering the plan. Employee benefit expense under this plan was $400,000 and $467,000 for 2012 and 2011, respectively.

The Museum also has a noncontributory defined-benefit pension plan covering substantially all of its employees. Effective December 31, 2007, the Museum froze the defined-benefit plan and discontinued accrual of future benefits. The Museum's funding policy is to make the minimum annual contribution that is required by applicable regulations, plus such amounts as the Museum may determine to be appropriate from time to time. The amount the Museum expects to contribute to the plan in 2013 is $718,000.

(Table Dollar Amounts in Thousands)

Information about the plan's funded status follows:

	2012	2011
Projected benefit obligation	$ 10,575	$ 8,754
Fair value of plan assets	6,093	6,348
Funded status	$ (4,482)	$ (2,406)

Liabilities recognized in the consolidated statements of financial position:

	2012	2011
Accrued pension expense	$ 4,482	$ 2,406

The amount recognized in unrestricted net assets not yet recognized as components of net periodic benefit cost is a net loss of $4,258,000 and $2,146,000 as of June 30, 2012 and 2011, respectively. The accumulated benefit obligation was approximately $10,575,000 as of June 30, 2012 and $8,754,000 as of June 30, 2011.

Other significant balances and costs are:

	2012	2011
Benefit cost	$ 110	$ 229
Employer contribution	146	190
Benefits paid	393	455

The following amounts have been recognized in the consolidated statements of activities for the years ended June 30, 2012 and 2011:

	2012	2011
Amounts arising during the year:		
Net gain (loss)	$ (1,718)	$ 382
Amounts reclassified as components of net periodic benefit cost of the year:		
Net gain (loss)	(394)	619
	$ (2,112)	$ 1,001

The estimated net loss for the defined-benefit pension plan that will be amortized from unrestricted net assets into net periodic benefit cost over the next fiscal year is $229,000.

(Table Dollar Amounts in Thousands)

Significant assumptions include:

	2012	2011
Weighted-average assumptions used to determine benefit obligations:		
Discount rate	4.13%	5.67%
Weighted-average assumptions used to determine benefit costs:		
Discount rate	5.67%	5.45%
Expected return on plan assets	7.50%	7.50%
Rate of compensation increase	0.00%	0.00%

The Museum has estimated the long-term rate of return on plan assets based primarily on historical returns on plan assets, adjusted for changes in target portfolio allocations and recent changes in long-term interest rates based on publicly available information.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid as of June 30, 2012:

2013	$ 403
2014	406
2015	490
2016	501
2017	558
2018 - 2022	2,858

Plan assets are held by a bank-administered trust fund, which invests the plan assets in accordance with the provisions of the plan agreement. The plan agreement permits investment in common and preferred stocks, bonds, debentures, mortgages, certain notes of indebtedness or ownership, U.S. Government, State, and certain municipal securities, share or savings accounts in any bank, savings and loan or building and loan, any common trust fund, any group trust, any pooled fund, certain insurance contracts, and real, personal and mixed properties of all kinds.

Asset allocation is primarily based on a strategy to provide stable earnings while still permitting the plans to recognize potentially higher returns through a limited investment in equity securities. The target asset allocation percentages for 2013 are as follows:

	Range
Equity securities	60 - 70%
Debt securities	25 - 35%
Other	0 - 10%

(Table Dollar Amounts in Thousands)

At June 30, 2012 and 2011, plan assets by category were as follows:

	2012	2011
Equity securities	61%	62%
Debt securities	36%	34%
Other	3%	4%
	100%	100%

Pension Plan Assets

Following is a description of the valuation methodologies used for pension plan assets measured at fair value on a recurring basis and recognized in the accompanying consolidated statements of financial position, as well as the general classification of pension plan assets pursuant to the valuation hierarchy.

Where quoted market prices are available in an active market, plan assets are classified within Level 1 of the valuation hierarchy. Level 1 plan assets include cash equivalents (which consist of money market mutual funds), equity mutual funds and fixed income mutual funds.

The fair values of Museum's pension plan assets at June 30, 2012 and 2011, by asset class are as follows:

		2012 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash equivalents	$ 169	$ 169	$ -	$ -
Mutual funds				
Equity	3,692	3,692	-	-
Fixed income	2,232	2,232	-	-
Total	$ 6,093	$ 6,093	$ -	$ -

(Table Dollar Amounts in Thousands)

		2011 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash equivalents	$ 255	$ 255	$ -	$ -
Mutual funds				
Equity	3,943	3,943	-	-
Fixed income	2,150	2,150	-	-
Total	$ 6,348	$ 6,348	$ -	$ -

Note 14: Disclosures About Fair Value of Assets and Liabilities

ASC Topic 820, *Fair Value Measurements,* defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Topic 820 also specifies a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

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

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

Following is a description of the inputs and valuation methodologies used for assets measured at fair value on a recurring basis and recognized in the accompanying consolidated statements of financial position, as well as the general classification of such assets pursuant to the valuation hierarchy.

Investments

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include savings accounts, certificates of deposit, short-term investments, corporate stocks and certain mutual funds. If quoted market prices are not available, then fair values are estimated by a third-party pricing service using pricing models, quoted market prices of securities with similar characteristics or discounted cash flows. For investments, other than alternative investments, the inputs used by the pricing service to determine fair value may include one, or a combination of, observable inputs such as benchmark securities, bids, offers and reference data market research publications and are classified within Level 2 of the valuation hierarchy. Level 2 securities include corporate bonds. Real estate held for investment is valued based on appraisals of the property and is also classified within Level 2 of the valuation hierarchy. As a practical expedient, the fair value of certain alternative investments is determined using the net asset value (or its equivalent) provided by the fund assuming the Museum can redeem such investments at the net asset value per share at June 30 or within the near term. These Level 2 alternative investments include equity and fixed income comingled funds, absolute return marketable alternatives, equity-oriented marketable alternatives and inflation hedging and private equity/venture capital investments. For alternative investments that are not redeemable at net asset value at June 30 or in the near term, the net asset value (or its equivalent) provided by the fund is utilized, as a practical expedient, to determine fair value and are classified within Level 3 of the valuation hierarchy. These Level 3 securities include equity-oriented marketable alternatives, inflation hedging and private equity/venture capital securities.

Charitable Lead Trust Held by a Third Party

The fair value is estimated using a discounted cash flow model. Due to the nature of the valuation inputs, the interest is classified within Level 3 of the hierarchy.

Interest Rate Swap Agreements

Fair value is estimated by the counterparty using a proprietary model. The interest rate swaps are classified within Level 3 of the valuation hierarchy.

(Table Dollar Amounts in Thousands)

The following tables present the fair value measurements of assets and liabilities recognized in the accompanying consolidated statements of financial position measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at June 30, 2012 and 2011:

		2012 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Investments				
Savings accounts	$ 174	$ 174	$ -	$ -
Certificates of deposit	247	247	-	-
Short-term investments	4,462	4,462	-	-
Corporate bonds	782	-	782	-
Corporate stocks				
Domestic	22,134	22,134	-	-
International	2,668	2,668	-	-
Mutual funds				
Equity - domestic	233	233	-	-
Equity - international	25,048	25,048	-	-
Fixed income	14,896	14,896	-	-
Alternative investments				
Equity - international comingled funds	40,373	-	40,373	-
Fixed income comingled funds	10,771	-	10,771	-
Absolute return marketable alternatives	43,847	-	43,847	-
Equity-oriented marketable alternatives	60,341	-	59,336	1,005
Inflation hedging	58,579	-	29,838	28,741
Private equity/venture capital	43,010	-	-	43,010
Real estate held for investment	2,899	-	2,899	-
Total investments	330,464	69,862	187,846	72,756
Interest in charitable lead trust	4,402	-	-	4,402
	$ 334,866	$ 69,862	$ 187,846	$ 77,158
Liabilities				
Interest rate swap	$ (5,976)	$ -	$ -	$ (5,976)

Indianapolis Museum of Art
Notes to Consolidated Financial Statements
June 30, 2012 and 2011
(Table Dollar Amounts in Thousands)

		2011 Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Investments				
Savings accounts	$ 163	$ 163	$ -	$ -
Certificates of deposit	246	246	-	-
Short-term investments	5,433	5,433	-	-
Corporate bonds	1,204	-	1,204	-
Corporate stocks				
Domestic	27,129	27,129	-	-
International	3,691	3,691	-	-
Mutual funds				
Equity - domestic	365	365	-	-
Equity - international	36,958	36,958	-	-
Fixed income	19,429	19,429	-	-
Alternative investments				
Equity - international comingled funds	45,181	-	45,181	-
Fixed income comingled funds	10,973	-	10,973	-
Absolute return marketable alternatives	42,296	-	42,296	-
Equity-oriented marketable alternatives	61,468	-	54,372	7,096
Inflation hedging	61,662	-	39,399	22,263
Private equity/venture capital	35,002	-	-	35,002
Real estate held for investment	2,899	-	2,899	-
Total investments	354,099	93,414	196,324	64,361
Interest in charitable lead trust	4,045	-	-	4,045
	$ 358,144	$ 93,414	$ 196,324	$ 68,406
Liabilities				
Interest rate swap	$ (2,324)	$ -	$ -	$ (2,324)

(Table Dollar Amounts in Thousands)

The following is a reconciliation of the beginning and ending balances of recurring fair value measurements recognized in the accompanying consolidated statements of financial position using significant unobservable (Level 3) inputs:

	Equity-Oriented Marketable Alternatives	Inflation Hedging	Private Equity/ Venture Capital	Interest in Charitable Lead Trusts	Fair Value of Interest Rate Swap
Balance, July 1, 2010	$ 4,755	$ 16,714	$ 24,100	$ -	$ (2,691)
Total unrealized gains	95	4,711	4,852	-	-
Purchases, issuances and settlements	6,497	838	6,050	4,045	-
Gain on interest rate swap	-	-	-	-	367
Transfers out of Level 3	(4,251)	-	-	-	-
Balance, June 30, 2011	7,096	22,263	35,002	4,045	(2,324)
Total unrealized gains (losses)	(94)	1,689	1,038	357	-
Purchases and issuances	3	7,787	13,221	-	-
Settlements	-	(2,998)	(6,251)	-	-
Loss on interest rate swap	-	-	-	-	(3,652)
Transfers out of Level 3	(6,000)	-	-	-	-
Balance, June 30, 2012	$ 1,005	$ 28,741	$ 43,010	$ 4,402	$ (5,976)
Total gains for the period included in change in net assets attributable to the change in unrealized gains (losses) related to assets and liabilities still held at June 30, 2011	$ 95	$ 4,711	$ 4,852	$ -	$ -
Total gains (losses) for the period included in change in net assets attributable to the change in unrealized gains (losses) related to assets and liabilities still held at June 30, 2012	$ (94)	$ 1,689	$ 1,038	$ 357	$ -

(Table Dollar Amounts in Thousands)

The following tables present information regarding funds with fair value that is determined using the net asset value (or its equivalent) provided by the fund.

2012	Fair Value	Unfunded Commitments	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Assets				
Investments				
Alternative investments				
Equity - international (a)	$ 40,373	$ -	daily to quarterly	7 - 60 days
Fixed income (b)	10,771	-	daily to monthly	7 - 45 days
Absolute return marketable alternatives (c)	43,847	-	quarterly to 2 year	30 - 180 days
Equity-oriented marketable alternatives (d)	60,341	-	monthly to 3 years	30 - 90 days
Inflation hedging (e)	58,579	7,069	monthly to not available	60 days to not available
Private equity/venture capital (f)	43,010	24,341	not available	
	$ 256,921	$ 31,410		

2011	Fair Value	Unfunded Commitments	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Assets				
Investments				
Alternative investments				
Equity - international (a)	$ 45,181	$ -	daily	6 - 7 days
Fixed income (b)	10,973	-	daily	0 - 7 days
Absolute return marketable alternatives (c)	42,296	-	quarterly to 1 year	30 - 180 days
Equity-oriented marketable alternatives (d)	61,468	-	quarterly to 3 years	30 - 180 days
Inflation hedging (e)	61,662	12,243	monthly to not available	10 days to not available
Private equity/venture capital (f)	35,002	32,558	not available	
	$ 256,582	$ 44,801		

(a) International equity mutual funds are commingled funds. Their underlying assets are daily priced and traded public equities; however, trades in and out of the investment vehicle are executed at net asset value (NAV).

(b) Fixed income mutual funds are commingled funds. Their underlying assets are daily priced and traded public equities; however, trades in and out of the investment vehicle are executed at NAV.

(c) Absolute return marketable alternative funds consist of funds of funds and limited partnerships that seek to achieve maximum capital appreciation through diversified investments. Many of the funds had lock-up periods, which have expired. Redemptions vary between quarterly and annually with notice periods between 30 days and 180 days. The fair values of these funds are estimated using NAV.

(d) Equity-oriented marketable alternative funds consist of funds of funds and limited partnerships that seek to achieve capital appreciation primarily through trading, investing in and selling equity securities. Many of the funds had lock-up periods, which have expired. Redemptions vary between quarterly, annually and every three years with notice periods between 30 days and 180 days. The fair value of these funds are estimated using NAV.

(e) Inflation hedging funds consist of real estate funds, natural resources and hedge funds. Real estate funds totaling $20,736,000 at June 30, 2012, invest across the major four categories of commercial real estate: office, industrial, multi-family and retain. These are limited partnerships with 10 to 12 year lives and cannot be sold. The underlying investments in the real estate funds are valued using comparable sales, dividend discount and income approach methods. Distributions are made as underlying investments are sold.

Natural resource funds totaling $7,820,000 at June 30, 2012, primarily invest in mid-stream and down-stream oil and gas opportunities and timber opportunities. Most partnerships have a 10 to 12 year life and valuation techniques include, but are not limited to, the income approach and public market equivalent methods. Funds cannot be sold, but distributions are received as underlying investments are liquidated.

Hedge funds totaling $30,023,000 at June 30, 2012, consist of credit and equity funds. Underlying equity positions are valued using market quotes or dealer pricing. These funds can be redeemed either monthly or annually.

(f) Private equity/venture capital funds consist of venture capital and special situations. The venture capital funds have lives that range from 10 to 12 years and cannot be sold. Distributions are received as individual portfolio holdings are liquidated.

Special situations funds seek to exploit debt opportunities across several sectors and is geographically diversified. These funds have lives that range from 10 to 12 years and the Museum will receive distributions from the underlying funds.

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying consolidated statements of financial position at amounts other than fair value.

Cash and cash equivalents - the carrying amount approximates fair value because of the short maturities of these instruments.

Contributions receivable - the carrying amount is a reasonable estimate of fair value.

Interest in estate notes - the carrying amount is a reasonable estimate of fair value.

Tax-exempt bonds payable - the carrying amount is a reasonable estimate of fair value.

Note 15: Concentrations and Contingencies

Approximately 76% of total contributions were received from four donors in 2011.

The Museum is subject to claims and lawsuits which arise primarily in the ordinary course of conducting operations. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the financial position of the Museum.

Current Economic Conditions

The current protracted economic decline continues to present not-for-profit organizations with difficult circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair value of investments and other assets, declines in contributions, constraints on liquidity and difficulty obtaining financing. The consolidated financial statements have been prepared using values and information currently available to the Museum.

Current economic conditions have made it difficult for many donors to continue to contribute to not-for-profit organizations. A significant decline in contribution revenue or investment return could have an adverse impact on the Museum’s future operating results.

In addition, given the volatility of current economic conditions, the values of assets and liabilities recorded in the consolidated financial statements could change rapidly, resulting in material future adjustments in investment values and allowances for contributions receivable that could negatively impact the Museum’s ability to meet debt covenants or maintain sufficient liquidity.