



NATIONAL GALLERY OF ART

Financial Statements

September 30, 2016

(With Independent Auditors' Reports Thereon)



KPMG LLP
1676 International Drive
McLean, VA 22102

Independent Auditors' Report

The Board of Trustees
The National Gallery of Art:

Report on the Financial Statements

We have audited the accompanying financial statements of the National Gallery of Art (the Gallery), which comprise the statement of financial position as of September 30, 2016, and the related statements of activities 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 U.S. generally accepted accounting principles; 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 and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Gallery of Art as of September 30, 2016, and the changes in its net assets and its cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.



Report on Summarized Comparative Information

We have previously audited the Gallery's 2015 financial statements, and we expressed an unmodified audit opinion on those financial statements in our report dated November 16, 2015. In our opinion, the summarized comparative information presented herein as of and for the year ended September 30, 2015 is consistent, in all material respects, with the audited financial statements from which it has been derived.

Other Matters

Supplementary and Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary private and federal information on the financial statements, the federal Supplementary Schedules and related notes and other supplementary information are presented for purposes of additional analysis and are not a required part of the financial statements.

The information included in the supplementary private and federal information on the financial statements, the federal Supplementary Schedules and related notes to the federal Supplementary Schedules is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary private and federal information on the financial statements, the federal Supplementary Schedules and related notes are fairly stated in all material respects in relation to the financial statements as a whole.

The other information in the September 30, 2016 Management's Discussion and Analysis, Performance Report, and the Other Supplementary Information has not been subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 15, 2016 on our consideration of the Gallery's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Gallery's internal control over financial reporting and compliance.

KPMG LLP

November 15, 2016

NATIONAL GALLERY OF ART

Statement of Financial Position

September 30, 2016

(with summarized financial information as of September 30, 2015)

(In thousands)

Assets	2016			2015
	Private	Federal	Total	Total
Cash and cash equivalents	\$ 13,726	41,048	54,774	60,101
Accounts receivable and other assets, net	6,338	–	6,338	5,093
Pledges receivable, net	21,497	–	21,497	9,112
Investments and trusts held by others	808,105	–	808,105	759,738
Property, plant and equipment, net	69,835	262,322	332,157	310,886
Art collections	–	–	–	–
Total assets	\$ 919,501	303,370	1,222,871	1,144,930
Liabilities and Net Assets				
Liabilities:				
Accounts payable and other liabilities	\$ 20,355	21,880	42,235	35,486
Unexpended federal one-year and two-year appropriations	–	14,891	14,891	18,859
Environmental liability	–	22,981	22,981	23,671
Total liabilities	20,355	59,752	80,107	78,016
Net assets:				
Unrestricted	322,846	226,922	549,768	499,780
Temporarily restricted	168,105	16,696	184,801	176,324
Permanently restricted	408,195	–	408,195	390,810
Total net assets	899,146	243,618	1,142,764	1,066,914
Total liabilities and net assets	\$ 919,501	303,370	1,222,871	1,144,930

See accompanying notes to financial statements.

NATIONAL GALLERY OF ART

Statement of Activities
 Year ended September 30, 2016
 (with summarized financial information for the year ended September 30, 2015)
 (In thousands)

	Unrestricted private	Unrestricted federal	Total Unrestricted	Temporarily restricted	Permanently restricted	Total 2016	Total 2015
Operating:							
Support and revenue:							
Federal appropriations	\$ -	115,046	115,046	7,900	-	122,946	117,790
Gifts and grants	3,494	-	3,494	2,859	-	6,353	13,429
Gallery shops sales, net	7,822	-	7,822	-	-	7,822	8,641
Spending policy appropriated for operations	2,602	-	2,602	16,555	-	19,157	19,971
Royalties and other income	1,232	-	1,232	-	-	1,232	2,929
	<u>15,150</u>	<u>115,046</u>	<u>130,196</u>	<u>27,314</u>	<u>-</u>	<u>157,510</u>	<u>162,760</u>
Net assets released from restrictions to fund operating expenses	19,884	8,488	28,372	(28,372)	-	-	-
Total support and revenue	<u>35,034</u>	<u>123,534</u>	<u>158,568</u>	<u>(1,058)</u>	<u>-</u>	<u>157,510</u>	<u>162,760</u>
Expenses:							
Collections	3,778	45,924	49,702	-	-	49,702	48,436
Special exhibitions	5,126	15,686	20,812	-	-	20,812	18,644
Education, gallery shops, and public programs	15,681	25,689	41,370	-	-	41,370	39,969
Editorial and photography	1,495	5,092	6,587	-	-	6,587	6,184
General and administrative	5,700	29,143	34,843	-	-	34,843	32,905
Development	2,391	1,777	4,168	-	-	4,168	4,044
Total operating expenses	<u>34,171</u>	<u>123,311</u>	<u>157,482</u>	<u>-</u>	<u>-</u>	<u>157,482</u>	<u>150,182</u>
Change in net assets from operating activities	<u>863</u>	<u>223</u>	<u>1,086</u>	<u>(1,058)</u>	<u>-</u>	<u>28</u>	<u>12,578</u>
Nonoperating:							
Federal appropriations	-	10,096	10,096	18,242	-	28,338	19,663
Nonoperating gifts and grants	-	-	-	20,505	15,395	35,900	8,834
Spending policy appropriated for art acquisitions	-	-	-	3,257	-	3,257	9,254
Change in value of split-interest agreements	62	-	62	12	425	499	(1,134)
Investment return less amounts appropriated for operations and art acquisitions	27,559	-	27,559	11,927	1,517	41,003	(64,315)
Acquisitions of works of art	(17,670)	-	(17,670)	-	-	(17,670)	(18,979)
Depreciation and amortization expense	(3,865)	(11,657)	(15,522)	-	-	(15,522)	(14,642)
Income tax expense	(595)	-	(595)	-	-	(595)	(726)
Environmental liability benefit (expense)	-	612	612	-	-	612	(1,123)
Provision for bad debts	-	-	-	-	-	-	(247)
Reclassifications of net asset balances	-	-	-	(48)	48	-	-
Net assets released from restrictions to fund nonoperating expenses	<u>23,765</u>	<u>20,595</u>	<u>44,360</u>	<u>(44,360)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Change in net assets from nonoperating activities	<u>29,256</u>	<u>19,646</u>	<u>48,902</u>	<u>9,535</u>	<u>17,385</u>	<u>75,822</u>	<u>(63,415)</u>
Increase (decrease) in net assets	30,119	19,869	49,988	8,477	17,385	75,850	(50,837)
Net assets at beginning of year	<u>292,727</u>	<u>207,053</u>	<u>499,780</u>	<u>176,324</u>	<u>390,810</u>	<u>1,066,914</u>	<u>1,117,751</u>
Net assets at end of year	\$ <u>322,846</u>	<u>226,922</u>	<u>549,768</u>	<u>184,801</u>	<u>408,195</u>	<u>1,142,764</u>	<u>1,066,914</u>

See accompanying notes to financial statements.

NATIONAL GALLERY OF ART
Statement of Cash Flows
Year ended September 30, 2016
(with summarized financial information for the year ended September 30, 2015)
(In thousands)

	<u>Private</u>	<u>Federal</u>	<u>Total 2016</u>	<u>Total 2015</u>
Cash flows from operating activities:				
Federal operating appropriations	\$ —	118,978	118,978	118,533
Operating gifts and grants	8,442	—	8,442	8,196
Gallery shops sales	7,824	—	7,824	8,639
Investment income and dividends, net	3,548	—	3,548	4,927
Royalties and other income	833	—	833	3,438
Payments to employees	(19,159)	(82,610)	(101,769)	(99,142)
Payments to suppliers	(17,201)	(37,336)	(54,537)	(56,600)
Interest payments	—	(29)	(29)	(55)
Income tax payments	(595)	—	(595)	(330)
Net cash used in operating activities	<u>(16,308)</u>	<u>(997)</u>	<u>(17,305)</u>	<u>(12,394)</u>
Cash flows from investing activities:				
Purchase of investments	(87,588)	—	(87,588)	(93,016)
Proceeds from sale of investments	99,786	—	99,786	109,230
Acquisitions of works of art	(11,264)	—	(11,264)	(18,962)
Purchase of property, plant and equipment	(5,445)	(33,959)	(39,404)	(30,609)
Net cash used in investing activities	<u>(4,511)</u>	<u>(33,959)</u>	<u>(38,470)</u>	<u>(33,357)</u>
Cash flows from financing activities:				
Contributions and net investment income for permanently restricted investments	7,753	—	7,753	397
Federal appropriations for capital projects	—	28,338	28,338	19,663
Gifts and grants for art acquisitions and capital projects	14,673	—	14,673	18,163
Principal payment on capital lease obligation	—	(316)	(316)	(289)
Net cash provided by financing activities	<u>22,426</u>	<u>28,022</u>	<u>50,448</u>	<u>37,934</u>
Net change in cash and cash equivalents	1,607	(6,934)	(5,327)	(7,817)
Cash and cash equivalents, at beginning of year	12,119	47,982	60,101	67,918
Cash and cash equivalents, at end of year	<u>\$ 13,726</u>	<u>41,048</u>	<u>54,774</u>	<u>60,101</u>

(Continued)

NATIONAL GALLERY OF ART

Statement of Cash Flows
 Year ended September 30, 2016
 (with summarized financial information for the year ended September 30, 2015)
 (In thousands)

	<u>Private</u>	<u>Federal</u>	<u>Total 2016</u>	<u>Total 2015</u>
Reconciliation of Change in Net Assets to Net Cash Used in Operating Activities:				
Increase (decrease) in net assets	\$ 58,922	16,928	75,850	(50,837)
Adjustments to reconcile increase (decrease) in net assets to net cash used in operating activities:				
Depreciation and amortization	3,865	11,657	15,522	14,642
Amortization of discount on pledges receivable	(339)	-	(339)	(565)
Provision for bad debts	-	-	-	247
Contributions and net investment income for permanently restricted investments	(7,753)	-	(7,753)	(397)
Federal appropriations for capital projects	-	(28,338)	(28,338)	(19,663)
Gifts and grants for art acquisitions and capital projects	(14,673)	-	(14,673)	(18,163)
Acquisitions of works of art	11,264	-	11,264	18,962
Realized and unrealized (gains) losses on investments, net	(59,238)	-	(59,238)	43,414
Reinvested dividends and interest, net	(1,289)	-	(1,289)	(2,142)
Donated investment securities	(1,692)	-	(1,692)	(5,733)
Proceeds from donated investment securities	1,688	-	1,688	5,757
Change in value of split-interest agreements	144	-	144	249
Change in accounts receivable and other assets, net	(1,245)	-	(1,245)	785
Change in pledges receivable, net	(12,046)	-	(12,046)	4,670
Change in accounts payable and other liabilities	6,084	3,414	9,498	(4,252)
Change in unexpended one-year federal appropriations	-	(3,968)	(3,968)	743
Change in environmental liability	-	(690)	(690)	(111)
Net cash used in operating activities	<u>\$ (16,308)</u>	<u>(997)</u>	<u>(17,305)</u>	<u>(12,394)</u>
Supplemental disclosure of non-cash information:				
Capital additions included in accounts payable	\$ 2,764	3,200	5,964	8,577

See accompanying notes to financial statements.

NATIONAL GALLERY OF ART

Notes to Financial Statements
September 30, 2016
(In thousands)

(1) Organization

The National Gallery of Art (the Gallery) was created in 1937 for the people of the United States of America by a joint resolution of Congress, accepting the gift of financier and art collector Andrew W. Mellon. The Gallery is a nonprofit organization exempt from federal income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code.

The Gallery serves the United States in a national role by preserving, collecting, exhibiting, and encouraging the understanding by the American public of original, great works of art. This mission and standard of excellence is central to every activity of the Gallery, from caring for and strengthening the collection to presenting special exhibitions and organizing public programs.

A substantial portion of the Gallery's operations is funded from annual federal appropriations. Since its founding, federal funds ensure the operation and maintenance and the protection and care of the nation's art collection enabling the Gallery to remain open 363 days a year at no charge to visitors. The Gallery also receives federal appropriations for the repair and restoration of its facilities.

In addition to federal appropriations, the Gallery receives private donations and earns income from investments. Private donations from individuals, foundations and corporations have provided support for art acquisitions and conservation, scholarly and scientific research, exhibitions, and education outreach programs.

(2) Summary of Significant Accounting Policies

(a) General

The financial statements are prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles (U.S. GAAP) under *FASB ASC 958, Not-for-Profit Presentation of Financial Statements*.

The Gallery receives annual federal appropriations to cover its core programs and renovation of its buildings as part of the budget approved annually by Congress and signed by the President. This is supplemented with income from endowments designated for current operating expenditures as well as gifts and grants designated by donors for other specific expenditures. All monies, related activities and balances from federal sources are referred to herein as "federal", while all other monies, related activities and balances are referred to herein as "private".

(b) Measure of Operations

The Gallery includes in its measure of operations federal and private support and revenue and expenses that are integral to its core program services: collections; special exhibitions; education, Gallery shops and public programs; and editorial and photography. The measure of operations excludes certain nonoperating activities such as nonoperating gifts and grants

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Notes to Financial Statements
September 30, 2016
(In thousands)

(endowment gifts, gifts for art acquisitions, and capital projects), investment return less amounts designated for operations, acquisitions of works of art, and income tax and depreciation expense.

The Gallery's Board of Trustees appropriates only a portion of the Gallery's cumulative investment return for support of current operations and art acquisitions; the remainder is retained to support operations of future years and to offset potential market declines. The amount appropriated is computed under the Gallery's spending policy and is appropriated for use based on the underlying donor-imposed restrictions (see notes 4 and 11).

(c) **Summarized Financial Information**

The financial statements include certain summarized prior-year information in total only. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. GAAP. Accordingly, such information should be read in conjunction with the Gallery's financial statements for the year ended September 30, 2015, from which the summarized information was derived.

(d) **Net Assets**

The Gallery's net assets, support and revenue, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Gallery are classified and reported as follows:

- *Unrestricted* net assets consist of the Gallery's net investment in building improvements and other equipment purchased or constructed using federal funds less unfunded liabilities and all other resources which are not subject to donor-imposed restrictions. At the discretion of the Gallery's Board of Trustees, private funds which are not expended for operating activities may be set aside in designated reserves and earmarked to cover future program costs or other contingencies.
- *Temporarily restricted* net assets carry specific donor-imposed stipulations on the expenditure or other use of the contributed funds. In addition, the Gallery's unexpended "no-year" federal appropriations for special exhibitions and for the repair, renovation and restoration of its buildings are classified as temporarily restricted net assets.

Temporary restrictions may expire by the passage of time or as a result of fulfillment of the donor's stipulations. For gifts restricted for capital additions, net assets are released when capital expenditures are incurred.
- *Permanently restricted* net assets have donor-imposed stipulations that require that the corpus of the gifts be retained permanently. In some cases, the donor has also permanently restricted the use of excess income and any realized or unrealized gains attributable to the corpus. When the investment earnings in subsequent years are not sufficient to support expenditures under the Gallery's endowment spending policy, the necessary funds are transferred from permanently restricted net assets not to exceed

NATIONAL GALLERY OF ART

Notes to Financial Statements
September 30, 2016
(In thousands)

the original corpus. The amount transferred in FY 2016 totaled \$60 and is reported as a "reclassification of net asset balances" on the statement of activities.

(e) Cash and Cash Equivalents

Cash and cash equivalents include interest-bearing demand deposits and appropriated amounts yet to be disbursed remaining on deposit with the U.S. Department of Treasury (or U.S. Treasury). The Gallery considers all highly liquid investments with an original maturity of three months or less at the date of purchase to be cash equivalents, except where such cash equivalents are held as part of a long-term investment strategy (see note 4).

The fund balances with U.S. Treasury consists of appropriated funds that are available to pay current liabilities and finance authorized purchase commitments of the Gallery. The Gallery's fund balances with U.S. Treasury are carried forward until such time as goods or services are received and payments are made, or until the funds are returned to the U.S. Treasury.

(f) Pledges Receivable

Unconditional promises to give to the Gallery in the future (pledges receivable) are recorded at the fair value of future cash flows, after providing an allowance for uncollectibility (Level 3 inputs). For unconditional promises to give recognized prior to October 1, 2008, a risk-free rate of return at the date of the gift was used. For unconditional promises to give recognized on or after October 1, 2008, a discount rate approximating the current market rate at the date of the gift is used. The resulting discount rates range from 2.4% to 4.6%. Conditional promises to give are recognized as income when the conditions stipulated by the donor are substantially met.

(g) Investments and Trusts Held by Others

Investments are generally reported at fair value. Common and preferred stocks and mutual funds are valued using readily determinable market prices. Alternative investments are reported at the estimated fair value as provided by the investment managers. The Gallery reviews and evaluates valuation methods and assumptions the investment managers use in determining the fair value. For investments valued based on manager reported net asset values, the Gallery applies procedures to assess the valuation including comparing performance to relevant market indices and verifying the underlying asset values to quoted market prices. Due to the uncertainty of valuation of alternative investments, values may differ from values that would have been used had a ready market for the investments existed.

Purchases and sales of securities are reflected on a trade-date basis. Gains and losses on sales of securities are based on average historical value (cost of securities if purchased or the fair market value at the date of gift if received by donation). Dividend and interest income is recorded when earned on an accrual basis. In accordance with the policy of stating investments at fair value, the net change in unrealized appreciation or depreciation for the year is reflected in the statement of activities (see note 4).

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Notes to Financial Statements
September 30, 2016
(In thousands)

The Gallery has been named as beneficiary in several irrevocable charitable trusts held by third parties. The Gallery's share of these trusts is generally recorded at current fair value. Income distributions from these trusts are recorded as investment income and changes in the value of these trusts are recorded as "change in value of split-interest agreements" in the statement of activities.

(h) Property, Plant and Equipment

The land occupied by the Gallery's buildings was appropriated and reserved by the Congress of the United States for that purpose. No value has been assigned in the accompanying financial statements. Property, plant and equipment with a cost of \$50 or more is capitalized at cost and depreciated using the straight-line method over the useful life of the assets. These assets have been assigned a useful life as follows:

Buildings	50 years
Building improvements	up to 25 years
Equipment under capital lease	14 years
Equipment	5 - 10 years
Computer software	3 - 5 years

Other property items are expensed when purchased. Normal repairs and maintenance are charged to expense as incurred.

(i) Art Collections

The Gallery's art collections focus upon European and American paintings, sculpture, decorative arts, works on paper and photographs. In conformity with accounting policies generally followed by art museums, the value of art has been excluded from the statement of financial position.

The Gallery's collections are maintained for public exhibition, education and research in furtherance of public service, rather than for financial gain.

The Gallery acquires its art collections through purchase or by donations-in-kind. Only current year purchases made from specifically designated funds, not donations-in-kind, are reflected in the statement of activities. The Gallery does not deaccession any of its permanent collections.

(j) Accrued Leave

Annual leave is accrued as it is earned by employees and is included in personnel compensation and benefit costs. An unfunded liability as of the date of the financial statements is recognized for earned but unused annual leave by federal employees since this annual leave will be paid from future federal appropriations when the leave is used by employees. The amount accrued is based upon current pay of the employees.

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Notes to Financial Statements
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(In thousands)

(k) Unexpended Federal One-Year and Two-Year Appropriations

The Gallery's federal one-year and two-year appropriations are recognized as revenue as expenditures are incurred throughout the year. The portion of these appropriations which are not obligated or expended are retained by the Gallery in accordance with federal guidelines and returned to the U.S. Department of Treasury after five years. The remaining unexpended balances of these funds are classified as a liability on the statement of financial position.

(l) Employee Benefits

The pension expense recognized in the Gallery's financial statements is equal to the current service cost for the Gallery's employees for the accounting period less the amount contributed by the employees. The measurement of the pension service cost requires the use of an actuarial cost method and assumptions with factors applied by the Gallery. These factors are supplied by the Office of Personnel Management (OPM), the agency that administers the plan. The excess of the recognized pension expense over the amount contributed by the Gallery represents the amount being financed directly through the Civil Service Retirement and Disability Fund administered by OPM; therefore the excess financing costs are not recognized in the statement of activities. This amount is considered imputed financing by the Gallery.

All permanent employees of the Gallery, both federal and nonfederal, hired subsequent to January 1, 1984 participate in both the Social Security Retirement System and the Federal Employees' Retirement System (FERS). Employees hired prior to January 1, 1984 had the option of remaining under the Civil Service Retirement System (CSRS) or electing FERS. All employees have the option to make tax-deferred contributions to a Thrift Savings Plan and, in some instances, receive a matching portion from the Gallery. The Gallery funds all retirement contributions on a current basis, and accordingly there are no unfunded retirement costs (see note 12).

The Federal Employees Compensation Act (FECA) provides income and medical cost protection to covered federal civilian employees injured on the job, to employees who have incurred work-related occupational diseases, and to beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. The FECA program is administered by the U.S. Department of Labor (DOL), which pays valid claims and subsequently seeks reimbursement from the Gallery for these paid claims.

The actuarial FECA liability represents the liability for expected future workers' compensation benefits, which includes the liability for death, disability, medical, and miscellaneous costs for approved cases. The actuarial liability is determined by DOL annually, as of September 30, using a method that utilizes historical benefits payment patterns related to a specific incurred period, wage inflation factors, medical inflation factors and other variables. These actuarially computed projected annual benefit payments are discounted to present value using discount rates derived from the Treasury Nominal Coupon-Issue Yield Curve based on an average of the quarterly spot rates presented from September 30, 2015, through June 30, 2016. Specific rates were selected by interpolation for Treasury notes with maturities that matched average

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Notes to Financial Statements
September 30, 2016
(In thousands)

FECA compensation and medical cash flow duration. The change in the projected FECA liability is reported in the statement of activities. The FECA actuarial liability is recorded for financial reporting purposes only. This liability constitutes an extended future estimate of cost which will not be obligated against budgetary resources until the fiscal year in which DOL actually bills the cost to the Gallery. The cost associated with this liability cannot be met by the Gallery without further appropriation action.

(m) Imputed Financing Sources

In certain cases, costs of the Gallery are paid out of funds appropriated to other federal agencies. As an example, the law requires certain costs of retirement programs to be paid by OPM and certain legal judgments against the Gallery to be paid from the Judgment Fund maintained by U.S. Treasury. Costs that are identifiable to the Gallery and directly attributable to the Gallery's operations are paid by these federal agencies; however, imputed costs and offsetting federal funding amounts are not recognized in the statement of activities.

Imputed costs and offsetting federal funding amounts for pension and post-retirement health and life insurance benefits are computed and presented in note 12.

(n) Contributed Services and Donated Assets

The Gallery has volunteers who provide assistance in various departments. Such contributed services do not meet the criteria for recognition of contributed services and accordingly, are not reflected in the accompanying financial statements.

Donated assets, which do not become part of the Gallery's art collections, are recorded at their fair value at the date of the gift. The Gallery does not imply time restrictions for gifts of long-lived assets. As a result, in the absence of donor-imposed restrictions, gifts of long-lived assets are reported as unrestricted revenue.

(o) Functional Allocation of Expenses

The cost of providing various programs and other activities summarized on a functional basis is shown in note 10. Certain costs including depreciation, utilities, building maintenance, security, information systems and other operating costs have been allocated among program and supporting services.

Included under the Collections category are the costs of the care and display of the Gallery's collections. Special exhibition expenses include travel, transportation of items, and other services necessary for the display of special exhibitions. Education, Gallery shops and public programs includes the cost of providing a wide array of lectures, tours, films, music, symposia and academic programs to the general public, in addition to Gallery shops' cost of goods sold and expenses. Editorial and photography expenses include the costs to produce the many publications produced by the Gallery. General and administrative expenses include costs for executive management, financial administration, human resources and legal services. Development expenses include those costs associated with individual and corporate gifts and grants, annual appeals and other fundraising efforts.

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Notes to Financial Statements

September 30, 2016

(In thousands)

(p) *Estimates*

The preparation of the financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingencies at the date of the financial statements, and the reported amounts of support and revenue and expenses during the reporting period. Actual results could differ from these estimates.

(q) *Risks and Uncertainties*

The Gallery invests in a variety of investment securities. Investment securities are exposed to risks such as interest rate, market, and credit risks. As a result, changes in the values of investment securities may occur that could materially affect the value of the Gallery's investments and its financial position.

(r) *Reclassifications*

Certain prior year balances have been reclassified to conform to current year presentation.

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Notes to Financial Statements
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(3) Pledges Receivable, Net

As of September 30, 2016 and 2015, pledges receivable, net, consisted of the following:

	2016	2015
Due in one year or less	\$ 8,882	3,100
Due between one year and five years	12,973	6,508
Due in more than five years	500	-
Subtotal	22,355	9,608
Less discounts of \$708 and \$346 and allowances of \$150 and \$150, respectively	(858)	(496)
Total	\$ 21,497	9,112

The fiscal year 2015 balance includes \$1,073 of pledges receivable from related parties.

(4) Investments, Trusts Held by Others and Fair Value Measurement

As of September 30, 2016 and 2015, investments and trust held by others consisted of the following:

	2016	2015
Investments	\$ 790,696	742,861
Trusts held by others	12,409	11,877
Subtotal	803,105	754,738
Loan to U.S. Treasury	5,000	5,000
Total	\$ 808,105	759,738

In 1942, the Gallery, under authority of an Act of Congress, made a \$5,000 permanent loan to the U.S. Treasury. This loan bears interest at the higher of 4.00% or 0.25% below the average monthly rate for long-term funds paid by the U.S. Treasury (4% during fiscal year 2016). Interest income on this loan was \$203 for the fiscal years ended September 30, 2016 and 2015. The fair value of the loan to the U.S. Treasury approximates the carrying value.

As of September 30, 2016 and 2015, the carrying value of the Gallery's cash, cash equivalents and balances with U.S. Treasury, receivables, deferred charges and other assets, and accounts payable and accrued expenses approximate their fair values because of the terms and relatively short maturity of these assets and liabilities. The Gallery's investments in private equity, venture

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capital, and real estate are generally valued based on the most current net asset value (NAV) adjusted for cash flows when the reported NAV is not at the measurement date.

The fair value of a financial instrument is the exit price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market in an orderly transaction between market participants on the measurement date. The Gallery applies a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy consists of three broad levels:

- *Level 1* – Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the Gallery has the ability to access as of the reporting date. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these securities does not entail a significant degree of judgment. Investments include investments in equity, real estate, and fixed income mutual funds that are traded in an active exchange market.
- *Level 2* – Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly as of the reporting date.
- *Level 3* – Valuations based on inputs that are unobservable and significant to the overall fair value measurement as of the reporting date. The determination of fair value for these financial instruments requires one or more inputs subject to significant management judgment or estimation. Trusts held by others are valued using Level 3 inputs. One trust is invested in real property and has been recorded at the value of the real property as of the date of the gift based on property valuations that involved significant judgments and estimation. Another trust is a perpetual trust invested in equity, fixed income securities, and mutual funds where the Gallery receives annual distributions but will never receive the trust's principal. The remainder of the trusts are invested in cash equivalents, mutual funds, and publicly traded equities.

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The following tables summarize the fair value of investments and trusts held by others as of September 30, 2016 and 2015 for financial assets by pricing observability levels:

	Prices in active markets for identical assets (Level 1)	Other observable inputs (Level 2)	Unobservable inputs (Level 3)	Investments measured at net asset value ¹	Fair value at September 30, 2016
U.S. equities	\$ 117,903	–	–	105,304	223,207
International equities:					
Developed market equities	53,819	–	–	83,448	137,267
Emerging market equities	32,765	–	–	44,211	76,976
Real estate:					
Mutual fund	19,274	–	–	–	19,274
Private Investments	–	–	–	1,765	1,765
Inflation hedging securities	–	–	–	18,897	18,897
Private equity and venture capital funds	–	–	–	41,689	41,689
Hedge fund of funds	–	–	–	162,154	162,154
Multi-asset fund	–	–	–	33,533	33,533
Fixed income securities	–	–	–	69,640	69,640
Charitable gift annuities and other	6,294	–	–	–	6,294
Trusts held by others	–	–	12,409	–	12,409
Total	\$ 230,055	–	12,409	560,641	803,105

¹ Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

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	Prices in active markets for identical assets (Level 1)	Other observable inputs (Level 2)	Unobservable inputs (Level 3)	Investments measured at net asset value ¹	Fair value at September 30, 2015
U.S. equities	\$ 103,792	–	–	88,919	192,711
International equities:					
Developed market equities	54,840	–	–	63,609	118,449
Emerging market equities	17,219	–	–	37,958	55,177
Real estate:					
Mutual fund	17,546	–	–	–	17,546
Private Investments	–	–	–	2,860	2,860
Inflation hedging securities	–	–	–	16,828	16,828
Private equity and venture capital funds	–	–	–	47,327	47,327
Hedge fund of funds	–	–	–	164,416	164,416
Multi-asset fund	–	–	–	46,807	46,807
Fixed income securities	7,391	–	–	67,284	74,675
Charitable gift annuities and other	6,065	–	–	–	6,065
Trusts held by others	–	–	11,877	–	11,877
	<u>\$ 206,853</u>	<u>–</u>	<u>11,877</u>	<u>536,008</u>	<u>754,738</u>
Total	\$ 206,853	–	11,877	536,008	754,738

¹ Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

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The following table summarizes the changes in Level 3 assets, Trusts held by others, measured at fair value on a recurring basis for the years ended September 30, 2016 and 2015:

	2016	2015
Fair value of Level 3 assets, October 1	\$ 11,877	13,168
Unrealized gains (losses)	1,087	(603)
Proceeds from distributions	(555)	(688)
Purchase of investments	–	–
Fair value of Level 3 assets, September 30	\$ 12,409	11,877

The fair values of the following investments have been estimated using the net asset value per share of the investments as of September 30, 2016:

		Fair value	Commitments	Redemption frequency	Redemption notice period
U.S. equities	(a)	\$ 105,304	–	Monthly to Quarterly	30 to 60 days
International equities:	(b)				
Developed market equities		83,448	–	Semi-monthly to monthly	6 to 30 days
Emerging market equities		44,211	–	Monthly	30 to 120 days
Real estate:	(c)				
Private Investments		1,765	549	N/A	N/A
Inflation hedging securities	(d)	18,897	–	Monthly	30 days
Private equity and venture capital funds	(e)	41,689	9,358	N/A	N/A
Hedge fund of funds	(f)	162,154	–	Semi-annually to annually	90 to 95 days
Multi-asset fund	(g)	33,533	–	Annually	365 days
Fixed income securities	(h)	69,640	–	Monthly	30 days
Total		\$ 560,641	9,907		

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The fair values of the following investments have been estimated using the net asset value per share of the investments as of September 30, 2015:

		<u>Fair value</u>	<u>Commitments</u>	<u>Redemption frequency</u>	<u>Redemption notice period</u>
U.S. equities	(a) \$	88,919	–	Monthly to Quarterly	30 to 60 days
International equities:	(b)				
Developed market equities		63,609	–	Semi-monthly	6 to 20 days
Emerging market equities		37,958	–	Monthly	30 to 120 days
Real estate:	(c)				
Private Investments		2,860	575	N/A	N/A
Inflation hedging securities	(d)	16,828	–	Monthly	30 days
Private equity and venture capital funds	(e)	47,327	11,344	N/A	N/A
Hedge fund of funds	(f)	164,416	–	Semi-annually to annually	90 to 95 days
Multi-asset fund	(g)	46,807	–	Annually	365 days
Fixed income securities	(h)	67,284	–	Monthly	30 days
Total		<u>\$ 536,008</u>	<u>11,919</u>		

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- (a) U.S. equities: Investments in equity securities of large cap and small cap U.S. companies comprised of a fund that invests long and short in U.S. equities.
- (b) International equities: Investments in equity securities of international companies in both developed and emerging markets comprised of investments in limited partnerships and limited liability companies.
- (c) Real estate: Investments in privately held real estate comprised of investments in private limited partnerships.
- (d) Inflation hedging securities: Investments in securities which are expected to perform well in periods of high inflation, including precious metals, energy, commodities, natural resources, U.S. Treasury Inflation Protected Securities (TIPS) and energy infrastructure Master Limited Partnership (MLP) comprised of an investment in a limited partnership.
- (e) Private equity and venture capital funds: Investments in limited partnerships which invest in shares of operating companies that are not listed on a publicly traded stock exchange, including leveraged buyouts, growth capital, distressed investments, and start-ups. The limited partnerships are organized as funds of funds.
- (f) Hedge fund of funds: Investments in limited partnerships which invest in shares of hedge funds which employ strategies such as long/short equity, credit and distressed assets, and multi-strategy. The limited partnerships are organized as funds of funds.
- (g) Multi-asset fund: Investment in a side pocket of a limited partnership which contains shares of funds engaged in private equity, venture capital, hedge funds, real estate, and natural resources.
- (h) Fixed income securities: Investment in a limited partnership which invests in investment grade fixed income securities issued by U.S. government and corporate entities.

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The following schedule summarizes the investment return and its classification in the statement of activities for the years ended September 30, 2016 and 2015:

	2016			2015 Total	
	Unrestricted	Temporarily restricted	Permanently restricted		Total
Dividends and interest (net of expenses of \$3,642 and \$3,532, respectively)	\$ 1,417	3,261	–	4,678	7,188
Net investment appreciation (depreciation)	28,744	28,478	1,517	58,739	(42,278)
	30,161	31,739	1,517	63,417	(35,090)
Appropriated for operations	(2,602)	(16,555)	–	(19,157)	(19,971)
Appropriated for art acquisitions	–	(3,257)	–	(3,257)	(9,254)
Investment return less amounts appropriated for operations and art acquisitions	\$ 27,559	11,927	1,517	41,003	(64,315)

(5) Property, Plant and Equipment, Net

As of September 30, 2016 and 2015, net property, plant and equipment consisted of the following:

	2016			2015 Total
	Private funds	Federal funds	Total	
Buildings and improvements	\$ 183,362	310,976	494,338	420,113
Equipment and computer software	7,534	82,822	90,356	83,153
Construction-in-progress	701	1,822	2,523	47,158
Equipment under capital lease	–	2,962	2,962	2,962
Subtotal	191,597	398,582	590,179	553,386
Less accumulated depreciation and amortization	(121,762)	(136,260)	(258,022)	(242,500)
Total	\$ 69,835	262,322	332,157	310,886

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(6) Accounts Payable and Other Liabilities

As of September 30, 2016 and 2015, accounts payable and other liabilities consisted of the following:

	2016			2015 Total
	Private funds	Federal funds	Total	
Accounts payable and accrued expenses	\$ 10,408	3,998	14,406	9,006
Employee-related liabilities	5,238	15,598	20,836	19,612
Other liabilities	4,709	2,284	6,993	6,868
Total	\$ 20,355	21,880	42,235	35,486

(7) Environmental Liability

In 2006 the Gallery, in conjunction with third party consultants, determined the cost of removing asbestos and other hazardous materials from the Gallery's buildings pursuant to the Clean Air Act as amended. The environmental liability was initially recorded at the estimated fair value calculated using inflation rates ranging from 1.9% to 2.6% and discount rates ranging from 4.6% to 4.9% (Level 3 inputs). The cost of the remediation is amortized over the useful life of the asset.

As of September 30, 2016 and 2015 the net remediation costs included in the Gallery's property, plant and equipment consists of the following:

	2016	2015
Remediation costs	\$ 4,201	4,201
Less accumulated depreciation	(3,525)	(3,442)
Net remediation costs	\$ 676	759

The Gallery's financial statements reflect an unfunded liability for environmental remediation clean-up costs as follows:

	2016	2015
Beginning balance	\$ 23,671	23,782
(Decrease) increase in liability	(612)	1,123
Remediation costs incurred	(78)	(1,234)
Total	\$ 22,981	23,671

The actual cost may vary from the current estimated cost at completion in the future due to inflation and the timing of implementing the various remedies. Management annually updates the total estimated costs for completion.

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(8) Federal Appropriations

The Gallery is funded primarily by two Congressional appropriations: one appropriation covers the Gallery's salaries, benefits and expenses, a portion of which is designated for special exhibitions, and the second appropriation provides funds necessary for the repair, restoration and renovation of the Gallery's buildings. The appropriation received for salaries, benefits and expenses is a two-year appropriation that must be obligated by the end of the second fiscal year, with the exception of the portion of the appropriation designated for special exhibitions expenses, which is available until it is expended. The appropriation for the repair, restoration, and renovation of the Gallery's buildings is available until expended. The fiscal year 2016 salaries and expenses appropriation includes \$3,578 for no-year special exhibitions funding.

The Gallery's federal appropriations received in the fiscal years ending 2016 and 2015 are reconciled to federal appropriation revenue recognized as follows:

		2016		
	Salaries and expenses	Repairs, restoration and renovation	Total	2015
Federal appropriations received	\$ 124,988	22,564	147,552	138,500
Unexpended appropriations	(12,455)	-	(12,455)	(12,433)
Amounts expended from prior years' appropriations	16,187	-	16,187	11,386
Federal appropriation revenue recognized	\$ 128,720	22,564	151,284	137,453
Operating	\$ 118,624	4,322	122,946	117,790
Nonoperating	10,096	18,242	28,338	19,663
Total federal appropriation revenue recognized	\$ 128,720	22,564	151,284	137,453

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(9) Net Assets Released from Restrictions

Net assets are released from donor restrictions when the expenses are incurred to satisfy the restricted purposes as specified by donors. The donor-specified restrictions that were met in the reporting period are as follows:

	2016			2015
	Private	Federal	Total	Total
Collections	\$ 2,470	–	2,470	2,172
Special exhibitions	3,807	4,166	7,973	6,342
Education and public programs	5,969	–	5,969	5,616
Editorial and photography	98	–	98	130
Operations	7,540	4,322	11,862	11,460
Subtotal operating	<u>19,884</u>	<u>8,488</u>	<u>28,372</u>	<u>25,720</u>
Acquisition of art	17,433	–	17,433	18,986
Capital projects	6,332	20,595	26,927	32,953
Subtotal nonoperating	<u>23,765</u>	<u>20,595</u>	<u>44,360</u>	<u>51,939</u>
Total	<u>\$ 43,649</u>	<u>29,083</u>	<u>72,732</u>	<u>77,659</u>

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(10) Functional Classification of Expenses

Expenses by functional classification for fiscal years 2016 and 2015 are shown below:

	2016			2015
	Private	Federal	Total	Total
Total operating expenses from the statement of activities	\$ 34,171	123,311	157,482	150,182
Expenses included in the nonoperating section of the statement of activities:				
Depreciation and amortization	3,865	11,657	15,522	14,642
Income tax expense	595	-	595	726
Environmental liability	-	-	-	1,123
Provision for bad debts	-	-	-	247
Total expenses	<u>\$ 38,631</u>	<u>134,968</u>	<u>173,599</u>	<u>166,920</u>
Program services:				
Collections	\$ 5,661	51,538	57,199	56,186
Special exhibitions	5,594	17,027	22,621	20,513
Education, Gallery shops and public programs	16,430	27,913	44,343	42,971
Editorial and photography	1,585	5,396	6,981	6,571
Subtotal program expenses	<u>29,270</u>	<u>101,874</u>	<u>131,144</u>	<u>126,241</u>
Supporting services:				
General and administrative	6,927	31,185	38,112	36,462
Development	2,434	1,909	4,343	4,217
Subtotal supporting services	<u>9,361</u>	<u>33,094</u>	<u>42,455</u>	<u>40,679</u>
Total expenses	<u>\$ 38,631</u>	<u>134,968</u>	<u>173,599</u>	<u>166,920</u>

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(11) Endowments and Net Asset Classifications

The Gallery's endowment consists of eighty-nine individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As required by U.S. GAAP, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The Gallery's Board of Trustees has resolved to be guided by the standards in the Uniform Prudent Management of Institutional Funds Act (UPMIFA), as enacted by the District of Columbia on January 23, 2008, in the management, investment, and expenditure of Gallery endowment funds although it is not required to do so as a matter of law. The Board has interpreted UPMIFA as allowing the Gallery to appropriate for expenditure or accumulate so much of an endowment fund as the Gallery determines is prudent for the uses, purposes and duration for which the endowment fund is established, subject to the intent of the donor as expressed in the gift instrument. Unless stated otherwise in the gift instrument, the assets in an endowment fund shall be donor-restricted assets until appropriated for expenditure by the Gallery. The Gallery classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Gallery in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Gallery considers the following factors when making a determination to appropriate or accumulate donor-restricted funds:

- The duration and preservation of the fund
- The purposes of the Gallery and the donor-restricted endowment 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 the Gallery
- The investment policies of the Gallery

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Endowment net assets were comprised of the following as of September 30, 2016 and 2015:

	2016			2015		
	Donor- restricted endowment funds	Board- designated endowment funds	Total	Donor- restricted endowment funds	Board- designated endowment funds	Total
Unrestricted	\$ (2,589)	8,029	5,440	(12,273)	7,769	(4,504)
Temporarily restricted	67,353	-	67,353	57,784	-	57,784
Permanently restricted	408,195	-	408,195	390,810	-	390,810
Total	\$ 472,959	8,029	480,988	436,321	7,769	444,090

The following table summarizes the change in the endowment funds during the years ended September 30, 2016 (with summarized comparative totals for 2015):

	2016				2015 Total
	Unrestricted	Temporarily restricted	Permanently restricted	Total	
Endowment net assets as of October 1,	\$ (4,504)	57,784	390,810	444,090	489,536
Investment return:					
Investment income	-	-	-	-	4,281
Net appreciation (depreciation)	10,349	26,041	1,941	38,331	(27,731)
Total investment return	10,349	26,041	1,941	38,331	(23,450)
Contributions	-	-	15,395	15,395	203
Appropriation of endowment assets for expenditures	(405)	(16,423)	-	(16,828)	(22,199)
Reclassifications	-	(49)	49	-	-
Endowment net assets as of September 30,	\$ 5,440	67,353	408,195	480,988	444,090

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the Gallery to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were \$2,607 as of September 30, 2016. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets.

The Gallery has adopted investment and spending policies for endowment assets that are intended to provide a predictable stream of funding for programs while maintaining the purchasing power of

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the endowment. Under the investment policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that reduces risk through diversification while obtaining a competitive rate of return. To satisfy its long-term rate-of-return, the Gallery relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yields (interest and dividends). The Gallery targets a diversified asset allocation that utilizes fixed income and equity-based investments to achieve its long-term objectives within prudent risk constraints.

The Gallery's spending policy is based on an annual endowment spending rate of 5% of the average fair value of endowment investments at the end of the previous five years. This spending rate constitutes the Board's annual appropriation for spending endowment earnings to support both the purchase of art and support of operations. Funds appropriated for art acquisition may exceed the 5% based on the availability of works of art for acquisition.

The following table summarizes the purpose of the net asset restrictions as of September 30, 2016 (with summarized comparative totals for 2015):

	2016			2015 Total
	Temporarily restricted	Permanently restricted	Total	
Acquisition of art	\$ 29,209	79,902	109,111	100,256
Collections	8,146	42,182	50,328	50,069
Special exhibitions	32,889	31,854	64,743	62,793
Education and public programs	83,567	104,721	188,288	167,444
Editorial and photography	428	5,305	5,733	6,228
Capital projects	4,711	-	4,711	8,234
Federal repair and renovation projects	16,696	-	16,696	19,637
Operations	9,155	144,231	153,386	152,473
Total	<u>\$ 184,801</u>	<u>408,195</u>	<u>592,996</u>	<u>567,134</u>

(12) Employee Benefits

Total pension expense recognized in the Gallery's financial statements was \$9,097 and \$8,596 for the years ended September 30, 2016 and 2015, respectively. These amounts do not include pension expense financed by OPM and imputed to the Gallery of \$1,695 and \$1,991, respectively. To the extent that Gallery employees are covered by the thrift savings component of FERS, the Gallery's payments to the plan are recorded as operating expenses. The Gallery's costs associated with the thrift savings component of FERS for the years ended September 30, 2016 and 2015, were \$2,776 and \$2,647, respectively.

In addition, the Gallery makes matching contributions for all employees who are eligible for current health and life insurance benefits. The Gallery's contributions for active employees are recognized as operating expenses. During fiscal years 2016 and 2015, the Gallery contributed \$6,301 and \$5,984, respectively. Using the cost factors supplied by OPM, the Gallery has not recognized as

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an expense in its financial statements the future cost of post-retirement health benefits and life insurance for its employees. These costs amounted to approximately \$4,549 and \$4,169 during fiscal years 2016 and 2015, respectively, and are financed by OPM and imputed to the Gallery.

The Gallery has a commitment to certain key employees whereby the Gallery will pay those employees a specified amount at a future point in time. The cost of these benefits is accrued over the key employees' future years of service to the Gallery. The cost of these benefits for fiscal years 2016 and 2015 total \$87 and is recognized as an expense in the statement of activities and as a liability included in accounts payable and other liabilities in the accompanying statement of financial position.

(13) Income Taxes

The Gallery is a nonprofit organization exempt from federal income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code.

Tax positions are recognized or derecognized based on a more-likely than-not threshold. This applies to positions taken or expected to be taken in a tax return. The Gallery is not aware of any uncertain tax positions.

(14) Lease Commitments

The Gallery has entered into several operating leases for warehouse and office space, which continue through April 30, 2024. The terms of these operating leases include additional rent for operating expenses, real estate taxes, utilities and maintenance. Future minimum lease payments under these leases for the fiscal years ended September 30 are as follows:

2017	\$	4,851
2018		4,968
2019		2,283
2020		1,411
2021		1,443
Thereafter		<u>3,880</u>
Total minimum lease payments	\$	<u><u>18,836</u></u>

Rental expense was approximately \$6,031 and \$5,963 for the years ended September 30, 2016 and 2015, respectively.

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(15) Subsequent Events

The Gallery has performed an evaluation of subsequent events through November 15, 2016 which is the date the financial statements were available to be issued, noting no events which affect the financial statements as of September 30, 2016.