

Financial Statements

The Isabella Stewart Gardner Museum, Incorporated, Trustee under the Will of Isabella Stewart Gardner

June 30, 2009 and 2008



Mayer Hoffman McCann P.C.
An Independent CPA Firm
Tofias New England Division

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Financial Statements

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Mayer Hoffman McCann P.C.

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Independent Auditors' Report

To the Trustees of the Isabella Stewart Gardner Museum, Incorporated
Trustee under the Will of Isabella Stewart Gardner
Boston, Massachusetts

We have audited the accompanying statement of financial position of The Isabella Stewart Gardner Museum, Incorporated, Trustee under the Will of Isabella Stewart Gardner (the "Museum") as of June 30, 2009 and the related statements of activities and cash flows for the year 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 audit. The financial statements of The Isabella Stewart Gardner Museum, Incorporated, Trustee under the Will of Isabella Stewart Gardner as of June 30, 2008 were audited by other auditors, Tofias P.C., whose shareholders became shareholders of Mayer Hoffman McCann P.C. as of December 31, 2008, and whose report dated October 8, 2008, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with U.S. generally accepted auditing standards. 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Museum as of June 30, 2009, and the changes in its net assets and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

Mayer Hoffman McCann P.C.

October 5, 2009
Cambridge, Massachusetts

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Statement of Financial Position

	<i>June 30,</i>	
	<i>2009</i>	<i>2008</i>
Assets		
Cash and cash equivalents	\$ 3,186,584	\$ 2,543,649
Receivables:		
Pledges, net	14,888,962	6,278,146
Contributions receivable from remainder trusts	1,519,539	1,379,230
Other receivables	306,544	627,015
Total receivables, net	16,715,045	8,284,391
Inventories	288,589	306,808
Prepaid and other assets	191,662	139,382
Museum property:		
Other museum property	13,180,530	13,180,530
Building improvements	2,666,904	2,662,368
Construction in progress	21,023,422	10,300,171
	36,870,856	26,143,069
Less - accumulated depreciation	(10,818,430)	(9,951,595)
	26,052,426	16,191,474
Historic building, contents and land	4,482,944	4,482,944
Total museum property	30,535,370	20,674,418
Investments, at market	105,969,228	116,229,810
Total assets	\$ 156,886,478	\$ 148,178,458
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses		
Accrued pension expense	\$ 1,063,678	\$ 108,644
Accounts payable and other accrued expenses	2,204,750	1,400,498
Total accounts payable and accrued expenses	3,268,428	1,509,142
Deferred income	32,743	33,388
Loan payable	-	1,740,000
Total liabilities	3,301,171	3,282,530
Net assets:		
Unrestricted	35,168,143	27,897,357
Temporarily restricted	71,080,570	72,837,843
Permanently restricted	47,336,594	44,160,728
Total net assets	153,585,307	144,895,928
Total liabilities and net assets	\$ 156,886,478	\$ 148,178,458

See accompanying notes to the financial statements.

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Statement of Activities

Years Ended June 30,

	<u>2009</u>				<u>2008</u>			
	<i>Unrestricted</i>	<i>Temporarily Restricted</i>	<i>Permanently Restricted</i>	<i>Total</i>	<i>Unrestricted</i>	<i>Temporarily Restricted</i>	<i>Permanently Restricted</i>	<i>Total</i>
Revenue and other support:								
Sales and services:								
Admissions	\$ 1,112,335	\$ -	\$ -	\$ 1,112,335	\$ 1,063,028	\$ -	\$ -	\$ 1,063,028
Museum shop	645,349	-	-	645,349	668,452	-	-	668,452
Café	46,803	-	-	46,803	50,240	-	-	50,240
Corporate events	46,906	-	-	46,906	83,902	-	-	83,902
Concert ticket sales	116,229	-	-	116,229	121,129	-	-	121,129
Other	78,960	-	-	78,960	303,712	-	-	303,712
	<u>2,046,582</u>	<u>-</u>	<u>-</u>	<u>2,046,582</u>	<u>2,290,463</u>	<u>-</u>	<u>-</u>	<u>2,290,463</u>
Contributed, membership and pledged support:								
Grants and gifts	602,940	29,176,937	3,214,482	32,994,359	581,300	12,644,164	243,561	13,469,025
Satisfaction and changes of restricted grants and gifts	12,825,327	(12,825,327)	-	-	7,854,001	(7,854,001)	-	-
Annual appeal	1,608,406	-	-	1,608,406	1,817,269	-	-	1,817,269
Membership	319,990	-	-	319,990	314,807	-	-	314,807
Member and special events	568,420	-	-	568,420	468,195	-	-	468,195
Subtotal contributed, membership and pledged support	<u>15,925,083</u>	<u>16,351,610</u>	<u>3,214,482</u>	<u>35,491,175</u>	<u>11,035,572</u>	<u>4,790,163</u>	<u>243,561</u>	<u>16,069,296</u>
Investments:								
Investment income and net appreciation (depreciation)	(1,427,612)	(14,031,936)	(3,568)	(15,463,116)	452,154	41,467	-	493,621
Allocation of endowment income	4,111,995	(4,076,947)	(35,048)	-	3,756,601	(3,756,601)	-	-
Subtotal investments	<u>2,684,383</u>	<u>(18,108,883)</u>	<u>(38,616)</u>	<u>(15,463,116)</u>	<u>4,208,755</u>	<u>(3,715,134)</u>	<u>-</u>	<u>493,621</u>
Total revenue and other support	<u>20,656,048</u>	<u>(1,757,273)</u>	<u>3,175,866</u>	<u>22,074,641</u>	<u>17,534,790</u>	<u>1,075,029</u>	<u>243,561</u>	<u>18,853,380</u>
Expenses:								
Security and visitor services	1,585,917	-	-	1,585,917	1,508,459	-	-	1,508,459
Museum shop	477,423	-	-	477,423	463,745	-	-	463,745
Café	19,561	-	-	19,561	15,945	-	-	15,945
Corporate events	26,411	-	-	26,411	56,623	-	-	56,623
Public programs	2,211,837	-	-	2,211,837	2,074,203	-	-	2,074,203
Collection, interpretation and conservation	1,473,111	-	-	1,473,111	1,353,781	-	-	1,353,781
Development and external relations	2,703,988	-	-	2,703,988	2,462,261	-	-	2,462,261
Administration	2,125,743	-	-	2,125,743	2,264,755	-	-	2,264,755
Special projects	6,011	-	-	6,011	25,287	-	-	25,287
Facilities and maintenance	953,395	-	-	953,395	1,037,440	-	-	1,037,440
Depreciation	838,485	-	-	838,485	857,975	-	-	857,975
Interest expense	8,346	-	-	8,346	71,531	-	-	71,531
Total expenses	<u>12,430,228</u>	<u>-</u>	<u>-</u>	<u>12,430,228</u>	<u>12,192,005</u>	<u>-</u>	<u>-</u>	<u>12,192,005</u>
Change in net assets before adjustments	8,225,820	(1,757,273)	3,175,866	9,644,413	5,342,785	1,075,029	243,561	6,661,375
Pension expense excluding normal pension costs	(955,034)	-	-	(955,034)	-	-	-	-
Total change in net assets	7,270,786	(1,757,273)	3,175,866	8,689,379	5,342,785	1,075,029	243,561	6,661,375
Net assets, beginning of year	27,897,357	72,837,843	44,160,728	144,895,928	22,554,572	71,762,814	43,917,167	138,234,553
Net assets, end of year	\$ 35,168,143	\$ 71,080,570	\$ 47,336,594	\$ 153,585,307	\$ 27,897,357	\$ 72,837,843	\$ 44,160,728	\$ 144,895,928

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Statement of Cash Flows

	<i>Years Ended June 30,</i>	
	<i>2009</i>	<i>2008</i>
Cash flows from operating activities:		
Change in net assets	\$ 8,689,379	\$ 6,661,375
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation	866,835	891,220
Contributions and change in value of remainder trusts	(140,309)	(33,839)
Net realized and unrealized gains losses on investments	15,399,218	801,297
Changes in:		
Pledges and other receivables	(8,290,345)	3,367,316
Inventories	18,219	22,791
Prepaid and other assets	(52,280)	27,297
Accounts payable and accrued expenses	1,759,286	(688,721)
Deferred income	(645)	12,927
Restricted contributions	(22,158,634)	(15,116,653)
Net cash used in operating activities	<u>(3,909,276)</u>	<u>(4,054,990)</u>
Cash flows from investing activities:		
Expenditures for Museum property	(10,727,787)	(5,914,847)
Purchase of investments	(19,816,802)	(37,302,778)
Proceeds from sale of investments	14,678,166	32,812,035
Net cash used in investing activities	<u>(15,866,423)</u>	<u>(10,405,590)</u>
Cash flows from financing activities:		
Proceeds from contributions restricted for:		
Endowment	3,351,276	409,590
Plant and other	18,807,357	14,707,064
Other financing activities:		
Principal payments on loan payable	(1,740,000)	(145,000)
Net cash provided by financing activities	<u>20,418,634</u>	<u>14,971,653</u>
Net change in cash and cash equivalents	642,935	511,073
Cash and cash equivalents, beginning of year	<u>2,543,649</u>	<u>2,032,576</u>
Cash and cash equivalents, end of year	\$ <u><u>3,186,584</u></u>	\$ <u><u>2,543,649</u></u>
Supplemental disclosures:		
Cash paid for interest	\$ <u><u>8,346</u></u>	\$ <u><u>71,531</u></u>

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Notes to Financial Statements

Note 1 - Description of Organization and Summary of Significant Accounting Policies

The Isabella Stewart Gardner Museum, Incorporated (the “Museum”) is the sole trustee under the will of Isabella Stewart Gardner. The Museum owns the property that is located at 2 Palace Road, Boston, Massachusetts, as well as Mrs. Gardner’s art collection contained therein. The Museum Corporation operates the Museum, which is open to the public and includes three floors of artwork, a garden, a cafe and a gift shop. The following is a summary of the significant accounting policies of the Museum.

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis and in accordance with the reporting principles of not-for-profit accounting. Resources are classified into separate net asset classes in accordance with donor-imposed restrictions and legal restrictions under Massachusetts law. The categories unrestricted, temporarily restricted, and permanently restricted net assets are defined as follows:

Unrestricted

Unrestricted net assets are resources over which the Trustees have discretionary control. The Museum records its property and equipment, other than its historical treasures, in this category because there are no time or use restrictions on the use of these assets.

Temporarily Restricted

Temporarily restricted net assets are those resources subject to donor-imposed restrictions which will be satisfied by the actions of the Museum or the passage of time. Appreciation on permanently restricted net assets is recorded in temporarily restricted net assets and may be expended under the standards of Massachusetts and other applicable laws.

Permanently Restricted

Permanently restricted net assets are those resources subject to the donor-imposed restriction that they be maintained permanently by the Museum. The donors of these resources require that the principal be invested in perpetuity and permit the income earned, including appreciation, to be used, all or in part, for unrestricted or temporarily restricted purposes. The Museum has shown its historical treasures in this category because of their restricted use imposed by the will of Isabella Stewart Gardner.

Financial Instruments Carried at Cost

The Museum’s financial instruments consist mainly of cash and cash equivalents, receivables, and accounts payable. The carrying amounts of these instruments approximate their fair values due to the short-term nature of these instruments.

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Notes to Financial Statements

Note 1 - Description of Organization and Summary of Significant Accounting Policies (Continued)

Cash and Cash Equivalents

Cash and cash equivalents consist of cash, money market accounts and overnight repurchase agreements with initial maturities of three months or less when purchased. These assets are stated at cost, which approximates market value. The Museum, at times, maintains amounts at a single financial institution in excess of federally insured limits.

Pledges, Grants and Gifts and Annual Funds

The Museum recognizes contributions of cash and other property at fair market value. Unconditional promises to give (pledges) are recognized when verifiably committed. The Museum does not recognize conditional promises and intentions to give until conditions have been met.

The Museum reports contributions 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 when expenses are incurred that satisfy the restricted purpose, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Contributions that are subject to restrictions requiring that the principal be invested in perpetuity are reported as increases to permanently restricted net assets.

The Museum recognizes contribution revenue for certain services that would be purchased, if not donated, at the fair value of those services. Those services included legal services of \$19,940 and \$11,800 for the years ended June 30, 2009 and 2008, respectively.

Investments

Investments are carried at fair market value. The Museum measures the fair market values of its financial instruments in accordance with Statement of Financial Accounting Standards No. 157, Fair Value Measurements (“SFAS 157”), which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs to determine the exit price. Also in accordance with SFAS 157, financial instruments must be categorized into a three-level hierarchy, based on the priority of inputs to the valuation technique, as discussed below.

Level 1 – Quoted prices are available in active markets for identical instruments as of the reporting date.

Level 2 – Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.

Level 3 – Pricing inputs are unobservable for the instrument and include situations where there is little, if any, market activity for the instrument. The inputs into the determination of fair value require significant management judgment or estimation.

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Notes to Financial Statements

Note 1 - Description of Organization and Summary of Significant Accounting Policies (Continued)

Investments (Continued)

In some instances, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such instances, an instrument's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

For more information on the fair value of the Museum's financial instruments, see Note 4 - Investments.

Inventories

Inventories for the Museum shop are valued at the lower of cost (first-in, first-out basis) or market.

Museum Property

Museum property which existed in 1936 is stated at appraised values established as of December 24, 1936. Subsequent additions are stated at cost. The Museum capitalizes renovations and other additions that materially add to the value of the related assets and extend their useful lives. Equipment and furnishings of relatively small dollar amounts are expensed.

Depreciation of property, plant and equipment is computed using the straight-line method based on estimates of useful lives. The estimated useful lives are principally 10 to 20 years for buildings and improvements and 3 to 10 years for other property. Depreciation for construction in progress begins upon completion of the related project.

Revenue Recognition

The Museum's revenues from sales and services are recognized when earned which in most cases is when paid for.

Income Taxes

The Museum is recognized by the Internal Revenue Service as an organization described in Section 501(c)(3) of the Internal Revenue Code and is generally exempt from federal and state income taxes on related income. Accordingly, no provision for income taxes is made in the financial statements.

The Museum is evaluating the implications of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with U.S generally accepted accounting principles 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Notes to Financial Statements

Note 1 - Description of Organization and Summary of Significant Accounting Policies (Continued)

Subsequent Events

The Museum has evaluated subsequent events through October 5, 2009, the date the Board of Trustees approved and authorized the financial statements to be issued.

Reclassifications

Certain reclassifications have been made to amounts in prior year's financial statements to conform to current year presentation. There is no effect on previously reported net assets.

Note 2 - Pledges Receivable

Unconditional promises to give (pledges receivable) which are expected to be collected within one year are recorded at their net realizable value. Pledges receivable that are expected to be collected in future years are recorded at the present value of estimated future cash flows, measured at a discount rate of 5%.

The Museum had the following pledges receivable outstanding at June 30:

	<i>2009</i>	<i>2008</i>
General operating support	\$ 140,000	\$ 220,125
Temporarily restricted non-operating support	17,033,260	6,542,461
Permanently restricted endowment	99,960	321,626
	<u>17,273,220</u>	<u>7,084,212</u>
Less: unamortized discount	(1,520,597)	(451,856)
Less: allowance for uncollectibles	<u>(863,661)</u>	<u>(354,210)</u>
Pledges, net	<u>\$ 14,888,962</u>	<u>\$ 6,278,146</u>
Amounts due in:		
Less than one year	\$ 3,426,331	\$ 1,919,849
One to five years	<u>13,846,889</u>	<u>5,164,363</u>
	<u>\$ 17,273,220</u>	<u>\$ 7,084,212</u>

In addition to the unconditional pledges receivable referenced above, the Museum has gross conditional pledges receivable of \$67,360,808 as of June 30, 2009.

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Notes to Financial Statements

Note 3 - Contributions Receivable from Remainder Trusts

The Museum recorded contributions receivable of \$1,519,539 and \$1,379,230 at June 30, 2009 and 2008, respectively, relating to various charitable remainder trusts in its statement of financial position. The receivable is measured at the present value of estimated future cash flows to be received and recorded in the appropriate net asset category based on donor stipulation. During the term of these agreements, changes in the value are recognized based on amortization of discounts and changes in actuarial assumptions.

Note 4 - Investments

The Museum's investments are managed to provide a level of support consistent with the purchasing power of the Museum's endowment being maintained or enhanced over time. The primary objective of the investment portfolio is to attain an average annual real total return (net of investment management fees) of at least 5% over the long term (rolling five-year periods).

The market values of the Museum's investments were as follows as of June 30:

	2009				2008
	<i>Level 1 Market Prices</i>	<i>Level 2 Observable Inputs</i>	<i>Level 3 Management Judgment</i>	<i>Total</i>	<i>Total</i>
Equity funds	\$ 2,693,462	\$ 23,873,204	\$ -	\$ 26,566,666	\$ 33,404,410
Fixed income funds	2,895,080	-	-	2,895,080	7,085,875
Money market funds	28,394,086	-	-	28,394,086	23,990,054
Real asset funds	4,306,407	-	-	4,306,407	9,285,664
Marketable alternative investments	-	37,018,320	4,054,542	41,072,862	38,524,517
Non-marketable alternative investments	-	-	2,734,127	2,734,127	3,939,290
Investments	\$ 38,289,035	\$ 60,891,524	\$ 6,788,669	\$ 105,969,228	\$ 116,229,810

The following summarizes the investment activity for the year ended June 30:

	2009				2008
	<i>Level 1 Market Prices</i>	<i>Level 2 Observable Inputs</i>	<i>Level 3 Management Judgment</i>	<i>Total</i>	<i>Total</i>
Investments at beginning of year	\$ 44,397,724	\$ 62,990,964	\$ 8,841,122	\$ 116,229,810	\$ 112,540,360
Net Purchases (Sales)	(217,466)	5,000,000	420,000	5,202,534	3,195,829
Net Investment Gains (Losses)	(5,891,223)	(7,099,440)	(2,472,453)	(15,463,116)	493,621
Investments at end of year	\$ 38,289,035	\$ 60,891,524	\$ 6,788,669	\$ 105,969,228	\$ 116,229,810

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Notes to Financial Statements

Note 4 - Investments (Continued)

The Museum holds certain investment instruments which are subject to withdrawal restrictions, including initial lock-in periods and specified exit dates with advance notification requirements. The following investment balances are subject to withdrawal restrictions as of June 30, 2009:

No restrictions	\$	38,289,035
Less than 1 year		53,726,679
1 - 2 years		11,219,387
2 - 5 years		-
More than 5 years		<u>2,734,127</u>
Total investments	\$	<u><u>105,969,228</u></u>

The Museum was committed to invest \$60,000 and \$5,540,000 as of June 30, 2009 and 2008, respectively, in two limited investment partnerships.

Note 5 - Endowment

The Museum's endowment consists of about 90 individual funds established for a variety of purposes. These funds include both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments.

The following disclosure required by FASB Statement of Position 117-1 represents the composition of the Museum's endowment assets and those functioning as endowment assets at June 30:

	<i>2009</i>			
	<i>Unrestricted Net Assets</i>	<i>Temporarily Restricted Net Assets</i>	<i>Permanently Restricted Net Assets</i>	<i>Total</i>
Endowments at beginning of year	\$ 10,450,375	\$ 52,744,931	\$ 38,116,415	\$ 101,311,721
Gifts and additions	16,666	-	3,334,610	3,351,276
Net investment gains (losses)	(1,618,298)	(14,054,140)	-	(15,672,438)
Amounts appropriated under endowment spending policy for operations	(484,500)	(4,195,551)	-	(4,680,051)
Reclassification for endowment losses exceeding corpus	<u>(111,285)</u>	<u>149,901</u>	<u>(38,616)</u>	<u>-</u>
Endowments at end of year	<u><u>\$ 8,252,958</u></u>	<u><u>\$ 34,645,141</u></u>	<u><u>\$ 41,412,409</u></u>	<u><u>\$ 84,310,508</u></u>

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Notes to Financial Statements

Note 5 - Endowment (Continued)

	2008			
	<i>Unrestricted</i>	<i>Temporarily</i>	<i>Permanently</i>	
	<i>Net Assets</i>	<i>Restricted</i>	<i>Restricted</i>	<i>Total</i>
	<i>Net Assets</i>	<i>Net Assets</i>	<i>Net Assets</i>	
Endowments at beginning of year	\$ 10,685,112	\$ 56,460,068	\$ 37,706,825	\$ 104,852,005
Gifts and additions	200,000	-	409,590	609,590
Net investment gains (losses)	(162)	41,464	-	41,302
Amounts appropriated under endowment spending policy for operations	(434,575)	(3,756,601)	-	(4,191,176)
Endowments at end of year	\$ 10,450,375	\$ 52,744,931	\$ 38,116,415	\$ 101,311,721

The Museum has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain or enhance the purchasing power of the endowment assets.

To satisfy its long-term rate-of-return objectives, the Museum diversifies its investment portfolio both by asset class (e.g., equities, bonds, cash equivalents, and other alternative investments) and within each asset class (e.g., within equities by economic sector/style, industry, quality, size, etc.). The purpose of diversification is to provide reasonable assurance that no single security or class of securities will have a disproportionate impact on the total portfolio.

The Museum employs external investment managers, with discretion to manage a designated portion of the portfolio to best achieve the investment objectives and requirements of the Museum under guidelines set forth in the Museum's written investment policy statement.

The Board of Trustees authorized the withdrawal of a portion of the cumulative investment return to support operating activities in the amounts of \$4,680,051 and \$4,191,176 in fiscal years ended June 30, 2009 and 2008, respectively. These amounts represent 5% of the 36-month rolling average market values of endowment investments ending March 31 prior to the start of the respective fiscal year starting July 1.

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 Museum to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$111,285 as of June 30, 2009. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the Board of Trustees. There were no such deficiencies as of June 30, 2008.

**THE ISABELLA STEWART GARDNER MUSEUM, INCORPORATED,
TRUSTEE UNDER THE WILL OF ISABELLA STEWART GARDNER**

Notes to Financial Statements

Note 6 - Loan Payable

On September 1, 2005, the Museum entered into a Series M-1A loan agreement with the Massachusetts Health and Educational Facilities Authority (MHEFA), a subdivision of The Commonwealth of Massachusetts, whereby the Museum borrowed \$2,175,000. The proceeds of this loan were used to pay off prior debt. Under the terms of the loan agreement, annual principal payments of the Series M-1A loan began on June 15, 2006. The loan is due in annual installments of \$143,550 with final payment due in June, 2020. During 2009, the loan balance was paid in full.

Note 7 - Defined Benefit Plan

The Museum has a defined benefit pension plan which it froze as of June 30, 2006. Management intends to terminate this plan in the future when it is administratively convenient to do so. A summary of the funded status of the Plan is as follows as of June 30:

	2009	2008
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 3,371,569	\$ 3,134,114
Service cost	-	-
Interest cost	202,807	201,199
Benefits paid	(145,362)	(134,513)
Actuarial (gain)/loss	(64,131)	170,769
Benefit obligation at end of year	3,364,883	3,371,569
Change in plan assets:		
Fair value of plan assets at beginning of year	3,362,925	3,539,671
Actual return on plan assets	(1,016,358)	(42,233)
Employer contributions	100,000	-
Benefits paid	(145,362)	(134,513)
Fair value of plan assets at end of year	2,301,205	3,362,925
Funded status at end of year	(1,063,678)	(8,644)
Reserve for contingencies	-	(100,000)
Total pension liability at end of year	\$ (1,063,678)	\$ (108,644)

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Notes to Financial Statements

Note 7 - Defined Benefit Plan (Continued)

The following assumptions were used to determine the benefit obligation at June 30:

	2009	2008
Discount Rate	6.30%	6.25%
Expected return on Plan assets	8.25%	8.25%

The Museum expects to contribute approximately \$100,000 to the Plan during the year ended June 30, 2010.

The following benefit payments are expected to be paid during the fiscal years ended June 30:

2009	\$	163,000
2010		169,000
2011		179,000
2012		188,000
2013		189,000
2015-2019		1,154,000

The Museum's Plan assets were comprised of the following at June 30:

	2009		2008		
Cash and cash equivalents	\$	1,723,294	75%	\$ 684,952	20%
Equity securities		-	-	2,127,033	63%
Debt securities		577,911	25%	550,940	17%
Fair value of Plan assets	\$	2,301,205	100%	\$ 3,362,925	100%

Note 8 - Defined Contribution Plan

Effective July 1, 2006, the Museum adopted a 403(b) retirement plan in which eligible employees may contribute to the plan. Eligibility is based on the length of service. Employer contributions into the plan on behalf of eligible employees are discretionary and vest over a two year period. Contributions made under this plan totaled \$210,525 and \$197,198 during fiscal years ended June 30, 2009 and 2008, respectively.

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Notes to Financial Statements

Note 9 - Net Assets

Unrestricted net assets include the following categories as of June 30:

	<i>2009</i>	<i>2008</i>
Operating	\$ 1,541,361	\$ 1,368,892
Board-designated	8,062,587	11,012,809
Property	<u>25,564,195</u>	<u>15,515,656</u>
Total	<u>\$ 35,168,143</u>	<u>\$ 27,897,357</u>

Operating fund activity was as follows for the years ending June 30:

	<i>2009</i>	<i>2008</i>
Sales and services	\$ 1,523,186	\$ 1,547,846
Contributed income	4,356,414	4,558,069
Allocation of endowment	4,680,051	4,191,176
Expenses	<u>(10,387,182)</u>	<u>(10,163,017)</u>
Operating net surplus	<u>\$ 172,469</u>	<u>\$ 134,074</u>

Temporarily restricted net assets include the following categories as of June 30:

	<i>2009</i>	<i>2008</i>
Accumulated unspent gains on endowments:		
Not designated for specific purpose	\$ 32,405,368	\$ 44,935,384
Designated for operating activities	<u>1,609,921</u>	<u>7,470,376</u>
Total unspent gains on endowments, subject to Trustee appropriation	34,015,289	52,405,760
Gifts and grants designated for operating activities	1,595,973	1,745,043
Gifts and grants designated for nonoperating activities	20,485,246	12,590,898
Pledges receivable designated for operating activities	131,810	204,414
Pledges receivable designated for nonoperating activities	14,662,191	5,782,247
Contributions receivable from remainder trusts	<u>190,061</u>	<u>109,481</u>
Temporarily restricted net assets	<u>\$ 71,080,570</u>	<u>\$ 72,837,843</u>

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Notes to Financial Statements

Note 9 - Net Assets (Continued)

Permanently restricted net assets are restricted as follows as of June 30:

	<i>2009</i>	<i>2008</i>
Endowed assets designated for the following purposes:		
No specific purpose	\$ 15,268,478	\$ 15,268,477
Curatorial programs and curator	8,613,872	8,438,149
Education programs and educator	3,815,211	3,825,212
Music, contemporary, and horticulture programs	2,595,541	2,552,578
Collection conservation and building preservation	5,861,909	2,774,601
Other	6,698,639	6,818,768
Investment in perpetuity, the income from which is expendable (with appreciation recorded in temporarily restricted endowment)	42,853,650	39,677,784
Historical treasures	4,482,944	4,482,944
Permanently restricted net assets	\$ 47,336,594	\$ 44,160,728

Note 10 - Restrictions on Operating Surplus

The Trustees are directed, under the will of Isabella Stewart Gardner, to pay to certain designated hospitals any surplus of income that, in the opinion of the Director and Trustees, will not be needed for the proper and reasonable maintenance of the Museum. These amounts, if any, are payable at the end of successive five-year periods, the most recent of which ended on December 31, 2004. The Trustees have determined that excesses, if any, are needed for the proper and reasonable maintenance of the Museum.

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Notes to Financial Statements

Note 11 - Functional Expenses

The following summarizes the functional expenses for the year ended June 30:

	<i>2009</i>	<i>2008</i>
Museum programs	\$ 4,364,635	\$ 3,472,134
Collection - exhibition, conservation, protection and management	3,570,941	4,195,552
Gardens and horticulture	807,914	845,071
Management and general	1,537,067	1,638,684
Fundraising	<u>2,149,671</u>	<u>2,040,564</u>
	<u>\$ 12,430,228</u>	<u>\$ 12,192,005</u>

The above functional expenses classifications reflect the ongoing programs of the Museum. Certain departments have been reassigned and depreciation, security and building operation expenses have been functionalized. Methods used in allocating these expenses include actual expenses incurred and proportional percentage allocation.

Note 12 - Commitments and Contingencies

During 2006, the Museum adopted FIN 47, an interpretation of FASB Statement 143, which clarifies that conditional asset retirement obligations that meet the definitions of liabilities should be recognized when incurred if their fair values can be reasonably estimated. As of June 30, 2009, the Museum was unable to estimate the range of settlement dates and the related probabilities for certain asbestos remediation Asset Retirement Obligations (AROs). These conditional AROs are primarily related to the encapsulated structural fireproofing that is not subject to abatement unless the buildings are demolished and non-encapsulated asbestos that the Museum would remediate only if it performed major renovations of certain existing buildings. Because these conditional obligations have indeterminate settlement dates, the Museum could not develop a reasonable estimate of their fair values. The Museum will continue to assess its ability to estimate fair values at each future reporting date. The related liability will be recognized once sufficient additional information becomes available.

On May 18, 2009, the Board of Trustees authorized the construction of a companion building to the Museum's historic structure. In conjunction with that project, the Trustees authorized a comprehensive campaign to provide enhanced operating and endowment support as well as to provide funds toward the construction of that building.