

Financial Statements

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

June 30, 2016 and 2015



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

Financial Statements

Table of Contents

Financial Statements:

Independent Auditors' Report	1-2
Statements of Financial Position	3
Statements of Activities	4-5
Statements of Cash Flows	6
Notes to Financial Statements	7-18



500 Boylston Street ■ Boston, MA 02116
Tel: 617.761.0600 ■ Fax: 617.761.0601 ■ www.cbiztofias.com

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 financial statements of The Isabella Stewart Gardner Museum, Incorporated, Trustee under the Will of Isabella Stewart Gardner (the "Museum"), which comprise the statements of financial position as of June 30, 2016 and 2015, and the related statements of activities, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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



Member of Kreston International – a global network of independent accounting firms



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Isabella Stewart Gardner Museum, Incorporated, Trustee under the Will of Isabella Stewart Gardner as of June 30, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Mayer Hoffmann McCann P.C.

December 6, 2016
Boston, Massachusetts

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

Statements of Financial Position

	<i>June 30,</i>	
	<i>2016</i>	<i>2015</i>
Assets		
Cash and cash equivalents	\$ 4,975,121	\$ 5,390,395
Receivables:		
Pledges receivable, net	1,419,153	2,003,722
Contributions receivable from remainder trusts	4,061,973	2,934,014
Other receivables	1,285,302	1,301,383
Total receivables, net	6,766,428	6,239,119
Prepays, inventory and other assets	800,957	645,157
Short-term investments	8,133,385	15,134,146
Museum property:		
Building improvements and other museum property	133,443,912	133,044,212
Construction in progress	883,755	408,127
	134,327,667	133,452,339
Less - accumulated depreciation	(38,512,714)	(32,828,673)
	95,814,953	100,623,666
Historic building, contents and land	4,482,944	4,482,944
Total museum property	100,297,897	105,106,610
Investments of endowed funds	168,166,775	168,899,136
Total assets	\$ 289,140,563	\$ 301,414,563
Liabilities and Net Assets		
Liabilities:		
Accounts payable and other accrued expenses	\$ 701,594	\$ 1,171,198
Deferred income	688,178	190,601
Bonds payable, net	31,701,544	30,808,128
Total liabilities	33,091,316	32,169,927
Net assets:		
Unrestricted	73,181,170	81,293,993
Temporarily restricted	88,675,089	97,349,034
Permanently restricted	94,192,988	90,601,609
Total net assets	256,049,247	269,244,636
Total liabilities and net assets	\$ 289,140,563	\$ 301,414,563

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, 2016 and 2015

	<i>Unrestricted</i>		<i>Temporarily Restricted</i>	<i>Permanently Restricted</i>	<i>2016 Total</i>	<i>2015 Total</i>
	<i>Operating</i>	<i>Property and Other</i>				
Revenue and other support:						
Admissions	\$ 1,832,366	\$ -	\$ 1,832,366	\$ -	\$ 1,832,366	\$ 1,670,630
Store	1,029,628	-	1,029,628	-	1,029,628	902,696
Membership	742,147	-	742,147	-	742,147	716,613
Rental events	365,256	-	365,256	-	365,256	497,824
Other earned income	424,020	-	424,020	-	424,020	369,860
Grants and gifts	442,750	-	442,750	5,891,123	3,591,379	12,815,359
Satisfaction of restricted grants and gifts	1,574,587	2,322,774	3,897,361	(3,897,361)	-	-
Annual appeal	2,099,223	-	2,099,223	-	2,099,223	1,934,857
Special events	843,673	-	843,673	222,050	-	1,065,723
Investment income and net appreciation (depreciation)	16,137	(190,292)	(174,155)	(4,142,354)	-	(4,316,509)
Allocation of endowment income	6,800,107	(52,704)	6,747,403	(6,747,403)	-	-
Total revenue and other support	16,169,894	2,079,778	18,249,672	(8,673,945)	3,591,379	13,167,106
Expenses:						
Security and museum services	3,091,485	-	3,091,485	-	-	3,091,485
Collection, conservation and public programs	5,282,939	-	5,282,939	-	-	5,282,939
Development and external relations	2,905,082	-	2,905,082	-	-	2,905,082
Administration	2,835,157	-	2,835,157	-	-	2,835,157
Special projects	-	698,642	698,642	-	-	698,642
Facilities and maintenance	2,001,963	-	2,001,963	-	-	2,001,963
Depreciation	-	5,684,041	5,684,041	-	-	5,684,041
Interest expense	-	1,295,100	1,295,100	-	-	1,295,100
Total expenses	16,116,626	7,677,783	23,794,409	-	-	23,794,409
Change in net assets before non-operating items	53,268	(5,598,005)	(5,544,737)	(8,673,945)	3,591,379	(10,627,303)
Loss on debt extinguishment	-	(2,568,086)	(2,568,086)	-	-	(2,568,086)
Total change in net assets	53,268	(8,166,091)	(8,112,823)	(8,673,945)	3,591,379	(13,195,389)
Net assets, beginning of year	1,582,735	79,711,258	81,293,993	97,349,034	90,601,609	269,244,636
Net assets, end of year	\$ 1,636,003	\$ 71,545,167	\$ 73,181,170	\$ 88,675,089	\$ 94,192,988	\$ 256,049,247

See accompanying notes to the financial statements.

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

Statement of Activities

Year Ended June 30, 2015

	<i>Unrestricted</i>			<i>Temporarily Restricted</i>	<i>Permanently Restricted</i>	<i>Total</i>
	<i>Operating</i>	<i>Property and Other</i>	<i>Total Unrestricted</i>			
Revenue and other support:						
Admissions	\$ 1,670,630	\$ -	\$ 1,670,630	\$ -	\$ -	\$ 1,670,630
Store	902,696	-	902,696	-	-	902,696
Membership	716,613	-	716,613	-	-	716,613
Rental events	497,824	-	497,824	-	-	497,824
Other earned income	369,860	-	369,860	-	-	369,860
Grants and gifts	758,150	2,041,385	2,799,535	8,400,786	1,615,038	12,815,359
Satisfaction of restricted grants and gifts	1,542,240	2,661,374	4,203,614	(4,203,614)	-	-
Annual appeal	1,934,857	-	1,934,857	-	-	1,934,857
Special events	749,240	-	749,240	367,950	-	1,117,190
Investment income and net appreciation	15,031	379,983	395,014	2,641,565	-	3,036,579
Allocation of endowment income	6,469,318	(512,625)	5,956,693	(5,956,693)	-	-
	<u>15,626,459</u>	<u>4,570,117</u>	<u>20,196,576</u>	<u>1,249,994</u>	<u>1,615,038</u>	<u>23,061,608</u>
Total revenue and other support						
Expenses:						
Security and museum services	2,899,752	-	2,899,752	-	-	2,899,752
Collection, conservation and public programs	4,973,432	-	4,973,432	-	-	4,973,432
Development and external relations	2,608,492	288,528	2,897,020	-	-	2,897,020
Administration	2,753,114	(350,000)	2,403,114	-	-	2,403,114
Special projects	-	681,773	681,773	-	-	681,773
Facilities and maintenance	1,961,267	-	1,961,267	-	-	1,961,267
Depreciation	400,000	5,274,384	5,674,384	-	-	5,674,384
Interest expense	-	1,399,375	1,399,375	-	-	1,399,375
	<u>15,596,057</u>	<u>7,294,060</u>	<u>22,890,117</u>	<u>-</u>	<u>-</u>	<u>22,890,117</u>
Total expenses						
Total change in net assets	30,402	(2,723,943)	(2,693,541)	1,249,994	1,615,038	171,491
Net assets, beginning of year	1,552,333	82,435,201	83,987,534	96,099,040	88,986,571	269,073,145
Net assets, end of year	\$ 1,582,735	\$ 79,711,258	\$ 81,293,993	\$ 97,349,034	\$ 90,601,609	\$ 269,244,636

See accompanying notes to the financial statements.

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

Statements of Cash Flows

	<i>Years Ended June 30,</i>	
	<i>2016</i>	<i>2015</i>
Cash flows from operating activities:		
Change in net assets	\$ (13,195,389)	\$ 171,491
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation	5,684,041	5,674,384
Contributions and change in value of remainder trusts	(1,127,959)	(41,880)
Restricted contributions	(9,161,161)	(12,367,178)
Net realized and unrealized (gains) losses on investments	4,382,515	(2,976,435)
Loss on debt refinancing	2,568,086	-
Changes in:		
Pledges and other receivables	600,650	1,896,057
Prepays, inventory and other assets	(155,800)	76,967
Accounts payable and accrued expenses	(469,604)	(354,287)
Deferred income	497,577	84,914
	<u>(10,377,044)</u>	<u>(7,835,967)</u>
Net cash used in operating activities	(10,377,044)	(7,835,967)
Cash flows from investing activities:		
Expenditures for museum property	(875,328)	(339,025)
Net sales (purchases) of short-term investments	7,000,761	(2,985,339)
Cash used to purchase long-term investments	(21,063,720)	(32,188,018)
Proceeds from sale and maturity of long-term investments	17,413,566	32,543,562
	<u>2,475,279</u>	<u>(2,968,820)</u>
Net cash provided by (used in) investing activities	2,475,279	(2,968,820)
Cash flows from financing activities:		
Proceeds from contributions restricted for:		
Endowment	3,516,888	2,093,732
Plant and other	5,644,273	10,273,446
Net effect of the 2016 bond issuance	(84,670)	-
Principal payments on bonds payable	(1,590,000)	(1,525,000)
	<u>7,486,491</u>	<u>10,842,178</u>
Net cash provided by financing activities	7,486,491	10,842,178
Net change in cash and cash equivalents	(415,274)	37,391
Cash and cash equivalents, beginning of year	5,390,395	5,353,004
Cash and cash equivalents, end of year	\$ <u>4,975,121</u>	\$ <u>5,390,395</u>
Supplemental disclosures:		
Cash paid for interest	<u>\$ 1,478,763</u>	<u>\$ 1,539,763</u>

See accompanying notes to the financial statements.

**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 25 Evans Way, Boston, Massachusetts, as well as Mrs. Gardner’s art collection contained therein. The Museum Corporation operates the Museum campus which includes a historic building with three floors of artwork, outdoor gardens, as well as additional purpose-built spaces for visitor accommodation, public programs and administration. 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 those resources that have no time or use restrictions. The Museum separates this category of net assets into two sub-categories: Operating and Property and Other. Operating activities are those related to the ongoing operation, programming and maintenance of the Museum. The Property and Other sub-category include activities that are one-time or episodic in nature; also included are resources over which the Trustees have discretionary control, including the unrestricted endowment and reserve funds.

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 terms of the gift instrument or, in the absence of specific terms, in accordance with Massachusetts law.

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 reports its historic building, contents and land in this category because of their restricted use imposed by the will of Isabella Stewart Gardner.

Fair Value Measurements

The Museum reports certain assets and liabilities at fair value on a recurring and non-recurring basis depending on the underlying accounting policy for the particular item. Recurring fair value measures include investments of endowed funds. Non-recurring measures include pledges receivable, and the contributions receivable from remainder trusts.

**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)

Fair Value Measurements (Continued)

Fair value standards require an entity to maximize the use of observable inputs (such as quoted market prices in active markets) and minimize the use of unobservable inputs (such as appraisals or other valuation techniques) to determine fair value. The standards also allow the Museum to report certain investments under the so-called “practical expedient” rule, which allows net asset value per share (“NAV”) to represent fair value for reporting purposes when the criteria for using this method are met. Fair value standards require the Museum to categorize financial instruments (but for those measured using NAV) into a three-level hierarchy based on the priority of inputs to the valuation technique as follows:

Level 1 – Quoted prices are available in active markets for identical instruments as of the reporting date. Instruments which are generally included in this category include listed equity and debt securities that are publicly traded on a stock exchange.

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.

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.

Market price is affected by a number of factors, including the type of instrument and the characteristics specific to the instrument, as well as the effects of market, interest and credit risk. Instruments with readily available actively quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of market price observability and a lesser degree of judgment used in measuring fair value.

It is reasonably possible that different assumptions or changes in values of these instruments could occur which could materially affect amounts reported in these financial statements. For more information on the fair value of the Museum’s financial instruments, see Note 4 - Investments.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash and money market accounts and exclude monies from the capital campaign that are included in short-term investments. These assets are stated at cost, plus accrued interest. Cash and cash equivalents held by investment managers are considered part of investment balances. The Museum may hold amounts at a single financial institution in excess of federally insured limits. The Museum monitors its exposure associated with cash and cash equivalents and has not experienced any losses in such accounts. Included in cash and cash equivalents is approximately \$3,772,617 and \$4,396,164 of restricted cash as of June 30, 2016 and 2015, respectively.

**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)

Pledges, Grants and Gifts and Annual Funds

Unconditional promises to give are recorded at fair value when initially pledged using a Level 2 fair value approach. Pledges that are expected to be collected in more than one year are recorded at present value using a risk-adjusted rate to account for the inherent risk associated with the expected future cash flows. Amortization of the discount is included in gift and grant revenue. Unconditional promises to give are periodically reviewed to estimate an allowance for doubtful collections. Conditional promises to give are not included as revenue until the conditions are substantially met.

Contributions Receivable from Remainder Trusts

The Museum records the fair value of contributions from remainder trusts upon notification that it has an irrevocable interest in trust assets using a Level 3 fair value approach. The receivable is measured at the present value of estimated future cash flows and recorded presuming a time restriction plus the effects of any further donor restriction. Present values are updated annually for remaining life expectancies using the discount rates set when the contributions were initially recorded.

Inventories

Inventories for the Museum shop are recorded at the lower of average cost or market.

Short-term Investments

Short-term investments are comprised of unspent and undesignated capital campaign funds. These funds consist of cash, money market accounts and treasury notes and are stated at fair market value, and using level 1 or level 2 fair value methods, as appropriate.

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 40 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. If fixed assets are received via donation, such items are recorded at fair value using a Level 3 market approach.

**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

Investments are carried at fair value. Interest, dividends and net gains or losses on investments are reported as increases or decreases in permanently restricted net assets if the terms of the original gift require that they be applied to the principal of a permanent endowment fund; as increases or decreases in temporarily restricted net assets if the terms of the gift and/or relevant state law impose restrictions on the current use of the income or net gains and losses; and as increases or decreases in unrestricted net assets in all other cases. For more information on the fair value of the Museum's investments, see Note 4.

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 has determined that its status as a tax exempt entity and its determinations as to its income being related and unrelated are not uncertain tax positions within the meaning of generally accepted accounting principles for its open tax years. The Museum's Federal and state income tax returns are generally open for examination for three years following the date filed.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with generally accepted accounting principles in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant management estimates include reserves for doubtful pledges, discounts on pledges receivable, fair value of certain investments, useful lives of depreciable assets, value of charitable remainder trusts, releases from restriction, and expense allocation by function. Actual results could differ from those estimates.

Reclassifications

During 2016, the Museum retrospectively early adopted an accounting change which now requires that debt issuance costs be presented as a deduction from debt in the financial statements. The accounting standard also requires bond premiums to be reported in the statement of financial position as a direct addition to the face of the bond. Accordingly, bonds payable originally stated at \$30,550,000 in the June 30, 2015 financial statements have been restated to \$30,808,128 to reflect \$360,865 of unamortized issuance costs previously included in prepaids, inventory and other assets, and \$618,993 of unamortized bond premiums. The effect of the change in the June 30, 2015 financial statements has also been to restate prepaids, inventory and other assets from \$1,006,022 to be \$645,157.

**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)

Reclassifications (Continued)

Additionally, during 2016, the Museum retrospectively early adopted accounting changes for presenting investments that are carried at net asset value per share where such items are now presented in a separate column in the related footnote disclosure rather than as part of the fair value leveling tables.

Subsequent Events

The Museum has evaluated subsequent events through December 6, 2016, the date the financial statements were issued.

Note 2 - Pledges Receivable

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>2016</i>	<i>2015</i>
Temporarily restricted non-operating support	\$ 878,715	\$ 1,506,160
Permanently restricted endowment	649,692	698,925
	1,528,407	2,205,085
Less: unamortized discount	(32,834)	(91,109)
Less: allowance for uncollectibles	(76,420)	(110,254)
	\$ 1,419,153	\$ 2,003,722
 Amounts due in:		
Less than one year	\$ 902,715	\$ 943,053
One to five years	625,692	1,262,032
	\$ 1,528,407	\$ 2,205,085

Pledge intentions and conditional pledges were approximately \$10 million and \$10.2 million as of June 30, 2016 and 2015, respectively.

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

Notes to Financial Statements

Note 3 - Investments of Endowed Funds

The Museum's endowed funds are managed by an Investment Committee made up of Trustees with investment experience and with assistance from professional investment consultants. 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.

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 investment portfolio is designed to provide a consistent or enhanced level of support for the Museum's operations, with an average annual real total return (net of investment management fees) of at least 5% over the long term (rolling five-year periods). The Museum believes the investment management fees are comparable to the industry average; however, the fees have not been broken out as some fees are netted by the investment managers against the total investment returns.

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's endowment consists of 144 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 Board of Trustees authorized the withdrawal of a portion of the cumulative investment return to support operating and property activities in the amounts of \$7,300,000 and \$6,469,000 in fiscal years ended June 30, 2016 and 2015, respectively. These amounts represent 5% of the 36-month rolling average market values of endowment funds for which market value exceeded historic cost at the time the withdrawal amount was authorized. The Board has authorized the withdrawal of \$7,845,800 for the fiscal year ending June 30, 2017.

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. There were no such funds below the fund's original value as of June 30, 2016 or 2015.

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

Notes to Financial Statements

Note 3 - Investments of Endowed Funds (Continued)

The change in the Museum's endowment assets was as follows for the years ended June 30:

	<i>2016</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	\$ 13,170,882	\$ 68,990,227	\$ 82,683,245	\$ 164,844,354
Gifts and additions	-	-	3,516,888	3,516,888
Interest and dividends	89,094	1,036,410	-	1,125,504
Unrealized/realized losses	(453,854)	(5,178,764)	-	(5,632,618)
Amounts appropriated under endowment spending policy for operations	(552,704)	(6,747,403)	-	(7,300,107)
Endowments at end of year	\$ 12,253,418	\$ 58,100,470	\$ 86,200,133	\$ 156,554,021
Temporarily restricted funds invested alongside endowment				11,848,191
Balance due from working capital				(235,437)
Total investments				\$ 168,166,775

During 2016, the net investment return on the statement of activities totaled \$(4,316,509) which was comprised of net investment return on the endowment of \$(4,507,114) and \$190,605 of interest and dividends on cash and short-term investments. During 2015, the net investment return on the statement of activities totaled \$3,036,579 which was comprised of net investment return on the endowment of \$2,881,957 and \$154,622 of interest and dividends on cash and short-term investments.

	<i>2015</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	\$ 11,401,731	\$ 72,305,354	\$ 80,589,513	\$ 164,296,598
Gifts and additions	2,041,385	-	2,093,732	4,135,117
Interest and dividends	74,247	887,364	-	961,611
Unrealized/realized gains	166,144	1,754,202	-	1,920,346
Amounts appropriated under endowment spending policy for operations	(512,625)	(5,956,693)	-	(6,469,318)
Endowments at end of year	\$ 13,170,882	\$ 68,990,227	\$ 82,683,245	\$ 164,844,354
Temporarily restricted funds invested alongside endowment				4,263,714
Balance due from working capital				(208,932)
Total investments				\$ 168,899,136

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

Notes to Financial Statements

Note 4 - Investments

Investments were as follows at June 30:

2016			
	<i>Investments Measured at NAV</i>	<i>Level 1</i>	<i>Total</i>
Cash and Cash Equivalents	\$ -	\$ 18,178,791	\$ 18,178,791
Fixed Income Funds	-	3,199,466	3,199,466
Equity Funds	49,424,990	-	49,424,990
Marketable Alternatives Funds			
Multi-strategy/global funds	46,305,597	-	46,305,597
Long/Short equity funds/global sector	36,144,072	-	36,144,072
Other marketable alternatives	14,214,293	-	14,214,293
Non-Marketable Funds	699,566	-	699,566
Total Investments of Endowment Funds	\$ 146,788,518	\$ 21,378,257	\$ 168,166,775
2015			
	<i>Investments Measured at NAV</i>	<i>Level 1</i>	<i>Total</i>
Cash and Cash Equivalents	\$ -	\$ 17,280,276	\$ 17,280,276
Fixed Income Funds	-	3,142,325	3,142,325
Equity Funds	51,720,411	6,151,809	57,872,220
Marketable Alternatives Funds			
Multi-strategy/global funds	44,846,139	-	44,846,139
Long/Short equity funds/global sector	26,771,172	-	26,771,172
Other marketable alternatives	17,999,047	-	17,999,047
Non-Marketable Funds	987,957	-	987,957
Total Investments of Endowment Funds	\$ 142,324,726	\$ 26,574,410	\$ 168,899,136

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

Notes to Financial Statements

Note 4 - Investments (Continued)

The Museum's investments have the following redemption terms at June 30:

	<i>2016</i>	<i>2015</i>
Liquidity		
Daily	\$ 21,378,257	\$ 26,574,410
Monthly	14,765,778	9,797,334
Quarterly	48,159,470	37,990,972
Semi-Annually	10,380,731	10,271,135
Annually and greater	67,828,574	81,004,420
Illiquid	5,653,965	3,260,865
Total investments	\$ 168,166,775	\$ 168,899,136

The Museum has no commitments to invest additional funds as of the reporting date. Management has no intentions or plans to liquidate any NAV practical expedient investments at other than NAV per share.

Under unusual circumstances, fund managers can reserve the right to limit distributions to shareholders; however, the Museum has not experienced any changes or limits over fund distributions.

Note 5 - Bonds Payable

Bonds payable were as follows at June 30:

	<i>2016</i>	<i>2015</i>
Bonds payable:		
2009 Series bonds with fixed interest rates between 4.6 and 5%	\$ 5,195,000	\$ 30,550,000
2016 Series bonds with a fixed interest rate of 1.5%	26,675,000	-
Total bonds payable	31,870,000	30,550,000
Less unamortized bond issuance costs	(265,502)	(360,865)
Unamortized premium on bond payable	97,046	618,993
Bonds payable, net	\$ 31,701,544	\$ 30,808,128

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

Notes to Financial Statements

Note 5 - Bonds Payable (Continued)

In June 2016, the Museum refinanced the majority of its existing debt to take advantage of current interest rates. In connection with this transaction the Museum recognized a loss on debt extinguishment of the old debt of \$2,568,086 which was reported as other non-operating expenses in 2016. The loss was a result of the prefunding of interest to the call date along with the write off of related unamortized premiums and issuance costs from the prior bond arrangement. Since interest rates had declined since the issuance, the amount that had to be funded in the refunding trust to defease the bonds was greater than the book values of the related debt. The old debt is considered legally extinguished, and accordingly, is no longer reported as a liability on the books of the Museum.

The present value cash flow savings as a result of the refinance was analyzed to be \$3,728,305 which is greater than the loss on extinguishment. The 2016 bonds are due in varying amounts through May, 2029. The remaining bonds under the 2009 issuance are due through May, 2019. Bond interest expense was \$1,295,100 and \$1,399,375 in the years ended June 30, 2016 and 2015, respectively, which includes the effects on interest of amortization of bond premiums and issuance costs both of which are being amortized over the life of the bonds.

Under the Series 2016 bonds, the Museum is required to meet certain financial and non-financial covenants. Both the old bonds and new bonds include a pledge of gross receipts from the Museum. Scheduled maturities of the bonds are as follows:

2017	\$ 2,106,000
2018	2,186,000
2019	2,271,000
2020	2,381,764
2021	2,419,233
Thereafter	<u>20,506,003</u>
Total bonds payable	\$ <u><u>31,870,000</u></u>

Note 6 - Employee Retirement Plans

The Museum has a 403(b) retirement plan in which eligible employees may invest a portion of their compensation. Employer contributions into the plan on behalf of eligible employees are discretionary and vest over a two year period. Employees become eligible for employer contributions after one year of service. Employer contributions made under this plan totaled \$227,074 and \$230,506 during fiscal years ended June 30, 2016 and 2015, respectively.

The Museum also offers a tax-deferred retirement plan regulated by U.S. Internal Revenue Code Section 457(b) which allows certain employees to contribute pre-tax compensation deferrals to the plan, subject to annual statutory limitations. The Museum does not contribute to this plan.

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

Notes to Financial Statements

Note 7 - Net Assets

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

	<i>2016</i>	<i>2015</i>
Accumulated unspent gains on endowments:		
Collection conservation and building preservation	\$ 4,663,862	\$ 7,056,444
Curatorial programs	4,581,577	6,273,647
Music, contemporary, and horticulture programs	2,264,232	3,249,687
Education and other public programs	2,173,092	2,833,970
Undesignated	43,447,205	48,280,022
Other purposes	970,502	1,296,457
Total unspent gains on endowments (subject to Trustee appropriation)	58,100,470	68,990,227
Gifts and grants for specific program purposes	1,146,701	1,298,068
Gifts and grants held for building support	27,456,703	25,558,423
Pledges receivable and charitable remainder trusts	1,971,215	1,502,316
Temporarily restricted net assets	\$ 88,675,089	\$ 97,349,034

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

	<i>2016</i>	<i>2015</i>
Endowed assets designated for the following purposes:		
Collection conservation and building preservation	\$ 28,899,819	\$ 28,899,819
Curatorial programs	16,646,311	16,645,218
Music, contemporary, and horticulture programs	12,018,221	11,648,946
Education and other public programs	10,220,131	7,073,611
Undesignated	15,415,651	15,415,651
Other purposes	3,000,000	3,000,000
Investment in perpetuity, the income from which is expendable (with appreciation recorded as temporarily restricted)	86,200,133	82,683,245
Pledges receivable and charitable remainder trusts	3,509,911	3,435,420
Historic building, contents and land	4,482,944	4,482,944
Permanently restricted net assets	\$ 94,192,988	\$ 90,601,609

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

Notes to Financial Statements

Note 8 - 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 of which the next assessment period being December 31, 2019. In the past, the Trustees have determined all of the Museum's resources are needed for the proper and reasonable maintenance of the Museum.

Note 9 - Functional Expenses

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

	<i>2016</i>	<i>2015</i>
Museum programs	\$ 21,159,973	\$ 19,869,050
Management and general	976,971	1,173,005
Fundraising	<u>1,657,465</u>	<u>1,848,062</u>
	<u><u>\$ 23,794,409</u></u>	<u><u>\$ 22,890,117</u></u>

The above functional expense classifications reflect the ongoing programs of the Museum. Certain expenses such as employee benefits, depreciation, security and building operations have been allocated to the functions identified above. Methods used in allocating these expenses include actual expenses incurred and proportional percentage allocation. The functional expenses for 2015 have been restated to reflect expense classification changes in 2016 that more accurately reflect the program expense classification.

Note 10 - Commitments and Contingencies

As of June 30, 2016, 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.