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RSM US LLP

## Independent Auditor's Report

To the Board of Directors  
Rochester Art Center

### Report on the Financial Statements

We have audited the accompanying financial statements of Rochester Art Center, which comprise the statements of financial position as of December 31, 2016 and 2015; the related statements of activities and changes in net assets, functional expenses 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.

### Auditor's 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 of material misstatement.

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

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

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Rochester Art Center as of December 31, 2016 and 2015, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

**Emphasis of Matter Regarding Going Concern**

The accompanying financial statements have been prepared assuming that the Rochester Art Center will continue as a going concern. As discussed in Note 6 to the financial statements, the Organization has suffered recurring losses from operations and has an unrestricted net assets deficiency, and has stated that substantial doubt exists about the Organization's ability to continue as a going concern.

Management's evaluation of the events and conditions and management's plans regarding these matters are also described in Note 6. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

*RSM US LLP*

Rochester, Minnesota  
November 3, 2017

**Rochester Art Center**

**Statements of Financial Position  
December 31, 2016 and 2015**

	2016	2015
<b>Assets</b>		
Current assets:		
Cash	\$ 50,747	\$ 33,125
Receivables:		
Trade	-	28,576
Pledges (Note 2)	63,258	25,033
Inventory	657	657
Prepaid expenses	-	4,164
<b>Total current assets</b>	<b>114,662</b>	<b>91,555</b>
Property and equipment:		
Leasehold interest in facility (Note 5)	6,009,011	6,177,488
Furniture and equipment, net	17,550	14,179
<b>Net property and equipment</b>	<b>6,026,561</b>	<b>6,191,667</b>
Other assets:		
Works of art	84,742	84,742
<b>Total assets</b>	<b>\$ 6,225,965</b>	<b>\$ 6,367,964</b>
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Accounts payable	\$ 148,920	\$ 49,556
Accrued expenses	12,380	15,011
Deferred revenue	60,150	76,305
<b>Total current liabilities</b>	<b>221,450</b>	<b>140,872</b>
Net assets (Notes 3 and 5):		
Unrestricted:		
Undesignated (deficit)	(203,938)	(140,208)
Invested in:		
Equipment	17,550	14,179
Works of art	84,742	84,742
Temporarily restricted	6,098,041	6,260,259
Permanently restricted	8,120	8,120
<b>Total net assets</b>	<b>6,004,515</b>	<b>6,227,092</b>
	<b>\$ 6,225,965</b>	<b>\$ 6,367,964</b>

See notes to financial statements.

**Rochester Art Center**

**Statement of Activities and Changes in Net Assets  
Year Ended December 31, 2016**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Public support:				
General contributions	\$ 123,893	\$ -	\$ -	\$ 123,893
Grants:				
City of Rochester (Note 5)	443,457	-	-	443,457
Others	23,008	160,063	-	183,071
Corporate sponsorships	5,000	-	-	5,000
Membership	20,246	-	-	20,246
Fundraisers	71,131	-	-	71,131
In-kind	18,605	-	-	18,605
<b>Total public support</b>	<b>705,340</b>	<b>160,063</b>	<b>-</b>	<b>865,403</b>
Revenues:				
Admissions	5,099	-	-	5,099
Rentals	145,531	-	-	145,531
Gallery shop	1,133	-	-	1,133
Exhibitions	2,910	-	-	2,910
Education	28,896	-	-	28,896
Special programs	25	-	-	25
Other	10	-	-	10
<b>Total revenues</b>	<b>183,604</b>	<b>-</b>	<b>-</b>	<b>183,604</b>
Net assets released from restrictions	322,281	(322,281)	-	-
<b>Total support and revenues</b>	<b>1,211,225</b>	<b>(162,218)</b>	<b>-</b>	<b>1,049,007</b>
Expenses:				
Program services	695,220	-	-	695,220
Supporting services:				
Fundraising	117,718	-	-	117,718
Management and general	458,646	-	-	458,646
<b>Total expenses</b>	<b>1,271,584</b>	<b>-</b>	<b>-</b>	<b>1,271,584</b>
<b>Change in net assets</b>	<b>(60,359)</b>	<b>(162,218)</b>	<b>-</b>	<b>(222,577)</b>
Net assets, beginning	(41,287)	6,260,259	8,120	6,227,092
Net assets, ending	\$ (101,646)	\$ 6,098,041	\$ 8,120	\$ 6,004,515

See notes to financial statements.

**Rochester Art Center**

**Statement of Activities and Changes in Net Assets  
Year Ended December 31, 2015**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Public support:				
General contributions	\$ 32,048	\$ -	\$ -	\$ 32,048
Grants:				
City of Rochester (Note 5)	342,502	-	-	342,502
Others	8,483	71,838	-	80,321
Corporate sponsorships	58,625	1,000	-	59,625
Membership	27,691	-	-	27,691
Fundraisers	35,151	-	-	35,151
In-kind	88,244	-	-	88,244
<b>Total public support</b>	<b>592,744</b>	<b>72,838</b>	<b>-</b>	<b>665,582</b>
Revenues:				
Admissions	2,705	-	-	2,705
Rentals	186,331	-	-	186,331
Gallery shop	906	-	-	906
Exhibitions	12,055	-	-	12,055
Education	22,096	-	-	22,096
Special programs	1,341	-	-	1,341
Other	1,262	-	-	1,262
<b>Total revenues</b>	<b>226,696</b>	<b>-</b>	<b>-</b>	<b>226,696</b>
Net assets released from restrictions	261,059	(261,059)	-	-
<b>Total support and revenues</b>	<b>1,080,499</b>	<b>(188,221)</b>	<b>-</b>	<b>892,278</b>
Expenses:				
Program services	749,522	-	-	749,522
Supporting services:				
Fundraising	231,251	-	-	231,251
Management and general	190,604	-	-	190,604
<b>Total expenses</b>	<b>1,171,377</b>	<b>-</b>	<b>-</b>	<b>1,171,377</b>
<b>Change in net assets</b>	<b>(90,878)</b>	<b>(188,221)</b>	<b>-</b>	<b>(279,099)</b>
Net assets, beginning	49,591	6,448,480	8,120	6,506,191
Net assets, ending	\$ (41,287)	\$ 6,260,259	\$ 8,120	\$ 6,227,092

See notes to financial statements.

**Rochester Art Center**

**Statement of Functional Expenses  
Year Ended December 31, 2016**

	Program Services				Total
	Exhibitions	Education	Special Programs	Gallery Shop	
Salaries and wages	\$ 78,718	\$ 28,625	\$ 25,047	\$ 10,734	\$ 143,124
Payroll taxes	6,193	2,252	1,971	854	11,270
Employee benefits	8,895	3,234	2,830	1,064	16,023
<b>Total salaries and related expenses</b>	<b>93,806</b>	<b>34,111</b>	<b>29,848</b>	<b>12,652</b>	<b>170,417</b>
Equipment purchase and repair	40,815	70	63	-	40,948
Supplies	920	-	1,868	-	2,788
Postage and printing	33,643	-	-	-	33,643
Shipping and transportation	10,368	-	-	-	10,368
Advertising	41,262	-	2,340	-	43,602
Utilities	69,982	11,664	-	-	81,646
Telephone	12,821	2,137	-	-	14,958
Exhibition openings	38,305	-	-	-	38,305
Fundraising event catering	-	-	-	-	-
Dues and subscriptions	1,281	60	225	-	1,566
Miscellaneous	13,085	783	-	62	13,930
Contract labor	39,402	2,000	4,699	-	46,101
Travel	15,899	-	-	-	15,899
Professional services	-	-	-	-	-
Bank and credit card fees	229	-	-	-	229
Insurance	11,971	2,565	855	684	16,075
<b>Total operating expenses</b>	<b>423,789</b>	<b>53,390</b>	<b>39,898</b>	<b>13,398</b>	<b>530,475</b>
Amortization of leasehold interest	117,934	25,272	8,424	6,738	158,368
Depreciation	4,749	1,018	339	271	6,377
<b>Total other operating expenses</b>	<b>122,683</b>	<b>26,290</b>	<b>8,763</b>	<b>7,009</b>	<b>164,745</b>
<b>Total expenses</b>	<b>\$ 546,472</b>	<b>\$ 79,680</b>	<b>\$ 48,661</b>	<b>\$ 20,407</b>	<b>\$ 695,220</b>

See notes to financial statements.

Supporting Services			
Management		Total	Grand Totals
Fundraising	and General		
\$ 32,203	\$ 182,482	\$ 214,685	\$ 357,809
2,534	14,357	16,891	28,161
3,639	22,749	26,388	42,411
38,376	219,588	257,964	428,381
-	42,117	42,117	83,065
2,270	18,955	21,225	24,013
375	3,475	3,850	37,493
-	-	-	10,368
1,186	6,943	8,129	51,731
-	34,991	34,991	116,637
-	6,410	6,410	21,368
-	-	-	38,305
-	-	-	-
3,588	4,141	7,729	9,295
-	8,616	8,616	22,546
68,075	81,266	149,341	195,442
-	9,666	9,666	25,565
-	12,528	12,528	12,528
-	2,256	2,256	2,485
342	684	1,026	17,101
114,212	451,636	565,848	1,096,323
3,370	6,739	10,109	168,477
136	271	407	6,784
3,506	7,010	10,516	175,261
\$ 117,718	\$ 458,646	\$ 576,364	\$ 1,271,584



**Rochester Art Center**

**Statement of Functional Expenses  
Year Ended December 31, 2015**

	Program Services				Total
	Exhibitions	Education	Special Programs	Gallery Shop	
Salaries and wages	\$ 128,650	\$ 85,767	\$ 12,865	\$ 4,288	\$ 231,570
Payroll taxes	10,626	7,084	1,063	354	19,127
Employee benefits	8,818	5,879	882	294	15,873
<b>Total salaries and related expenses</b>	<b>148,094</b>	<b>98,730</b>	<b>14,810</b>	<b>4,936</b>	<b>266,570</b>
Equipment purchase and repair	53,209	5,258	1,848	891	61,206
Supplies	9,839	4,752	389	53	15,033
Postage and printing	38,305	2,983	934	305	42,527
Shipping and transportation	12,693	-	-	-	12,693
Advertising	5,252	1,726	1,977	501	9,456
Utilities	71,862	10,266	5,133	2,566	89,827
Telephone	8,526	1,218	609	306	10,659
Exhibition openings	7,008	767	2,455	-	10,230
Fundraising event catering	-	-	-	-	-
Dues and subscriptions	377	56	83	28	544
Miscellaneous	7,904	1,982	780	149	10,815
Contract labor	16,671	6,880	100	-	23,651
Travel	9,478	2,302	-	-	11,780
Professional services	-	-	-	-	-
Bank and credit card fees	47	324	30	30	431
Insurance	13,398	1,914	957	3,691	19,960
<b>Total operating expenses</b>	<b>402,663</b>	<b>139,158</b>	<b>30,105</b>	<b>13,456</b>	<b>585,382</b>
Amortization of leasehold interest	117,934	25,272	8,424	6,738	158,368
Depreciation	3,436	687	1,374	275	5,772
<b>Total other operating expenses</b>	<b>121,370</b>	<b>25,959</b>	<b>9,798</b>	<b>7,013</b>	<b>164,140</b>
<b>Total expenses</b>	<b>\$ 524,033</b>	<b>\$ 165,117</b>	<b>\$ 39,903</b>	<b>\$ 20,469</b>	<b>\$ 749,522</b>

See notes to financial statements.

Supporting Services			
	Management		
Fundraising	and General	Total	Grand Totals
\$ 81,479	\$ 115,785	\$ 197,264	\$ 428,834
6,730	9,564	16,294	35,421
5,585	7,936	13,521	29,394
93,794	133,285	227,079	493,649
8,774	8,302	17,076	78,282
2,604	1,368	3,972	19,005
14,930	2,459	17,389	59,916
74	-	74	12,767
53,414	2,046	55,460	64,916
5,133	7,699	12,832	102,659
609	1,230	1,839	12,498
-	-	-	10,230
35,952	-	35,952	35,952
1,295	2,025	3,320	3,864
5,896	4,266	10,162	20,977
3,274	-	3,274	26,925
-	1,245	1,245	13,025
-	17,551	17,551	17,551
763	267	1,030	1,461
957	1,435	2,392	22,352
227,469	183,178	410,647	996,029
3,370	6,739	10,109	168,477
412	687	1,099	6,871
3,782	7,426	11,208	175,348
\$ 231,251	\$ 190,604	\$ 421,855	\$ 1,171,377

**Rochester Art Center**

**Statements of Cash Flows**  
**Years Ended December 31, 2016 and 2015**

	2016	2015
Cash flows from operating activities:		
Change in net assets	\$ (222,577)	\$ (279,099)
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Depreciation	6,784	6,871
Amortization of leasehold interest	168,477	168,477
(Increase) decrease in assets:		
Accounts receivable	(9,649)	22,705
Prepaid expenses	4,164	-
Increase (decrease) in liabilities:		
Accounts payable	99,364	3,015
Accrued expenses	(2,631)	(7,487)
Deferred revenue	(16,155)	17,773
<b>Net cash provided by (used in) operating activities</b>	<b>27,777</b>	<b>(67,745)</b>
Cash flows from investing activities:		
Purchase of property and equipment, net	(10,155)	-
<b>Net increase (decrease) in cash</b>	<b>17,622</b>	<b>(67,745)</b>
Cash, beginning	33,125	100,870
Cash, ending	<b>\$ 50,747</b>	<b>\$ 33,125</b>

See notes to financial statements.

## Rochester Art Center

### Notes to Financial Statements

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#### Note 1. Summary of Significant Accounting Policies

**Nature of business:** The Rochester Art Center (the Organization) is a not-for-profit corporation organized under Chapter 309 of the revised statutes of the State of Minnesota. The Organization's purpose is to provide to the citizens of Rochester and southeastern Minnesota the opportunity to know, practice and enjoy the arts. In addition, the Organization works to show the vital relationship of the arts to our daily lives and to join with schools, churches, libraries and community groups to make Rochester a cultural center worthy of its scientific achievements. The Organization's primary funding comes from the City of Rochester (see Note 5) and through corporate and individual donations, grants and facility rental fees.

**Estimates:** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) 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.

**Cash:** The Organization maintains cash in depository bank accounts.

**Receivables:** Receivables that are expected to be collected within one year are recorded at net realizable value. Amounts not expected to be collected within one year are reported at present value of projected future cash flows using a risk-free interest rate. Management determines bad debts by regularly evaluating individual balances and considering current financial and economic conditions. Receivables are written off when deemed uncollectible. Recoveries of receivables previously written off are recorded when received.

At December 31, 2016 and 2015, management did not identify any receivables they believe to be uncollectible. No allowance for uncollectible accounts has been recorded.

**Revenue recognition:** Memberships and program fees are recognized as revenue over the period to which the membership or fees relate. Revenue from grants is recognized according to the terms of the agreements. All contributions and promises to give are recognized at the time the Organization has the unconditional right to receive them and are reported at fair value as unrestricted unless specifically restricted by the donor. Conditional contributions are recognized when the condition has been substantially met. Amounts recognized that are restricted for future periods or specific purposes are reported as increases in temporarily restricted or permanently restricted net assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities and changes in net assets as net assets released from restrictions. If the restriction is met in the period the related revenue is recognized, the amounts are reported only within the unrestricted activity.

Many individuals have contributed a significant amount of time to activities of the Organization. The Organization does not recognize these contributed services as revenues unless the services received (1) create or enhance existing facilities, or (2) require specialized skills and are provided by individuals possessing those skills. The Organization recognized approximately \$4,325 and \$59,924 in contributed services during the years ended December 31, 2016 and 2015, respectively.

Donated goods and equipment are reflected as contributions in the accompanying financial statements at their estimated fair value at the date of receipt. Facility improvements from the City of Rochester were approximately \$6,000 for the years ended December 31, 2016 and 2015, (see Note 5) are included in the total donated goods and equipment recognized by the Organization of approximately \$14,280 and \$28,320 during the years ended December 31, 2016 and 2015, respectively.

## Rochester Art Center

### Notes to Financial Statements

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#### Note 1. Summary of Significant Accounting Policies (Continued)

**Functional expense allocation:** The cost of providing various programs and other activities has been summarized on a functional basis in the statements of activities and changes in net assets. Accordingly, certain costs have been allocated among the corresponding functional classifications, such as major classes of program services and supporting activities that benefit from such costs.

**Works of art:** The Organization recognizes works of art as assets. Donations of works of art are recorded at fair value at the date of the gift based on independent appraisals or valuations. Purchases of works of art are recorded at cost. Long-lived assets, such as works of art, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. No indicators of potential impairment were present as of December 31, 2016 and 2015; therefore, no impairment analysis was performed on these dates.

**Inventory:** Gallery shop inventory is valued at the lower of cost (first-in, first-out) or market.

**Furniture and equipment:** Furniture and equipment are stated at cost, if purchased, or at fair value on the date received, if donated, less accumulated depreciation. Depreciation is provided on the straight-line basis over the estimated useful life of the various assets (five to 10 years for the furniture and equipment). At December 31, 2016 and 2015, accumulated depreciation was \$603,737 and \$596,953, respectively. Depreciation expense for the years ended December 31, 2016 and 2015, was \$6,784 and \$6,871, respectively.

**Leasehold interest in facility:** The leasehold interest in the Rochester Art Center facility is stated at cost less amortization. Amortization is provided on the straight-line basis over the remaining term of the lease (see Note 5).

**Net assets:** Unrestricted net assets are those funds presently available for use by or on behalf of the Organization, including amounts available for general and administrative expenses. Temporarily restricted net assets are contributions that have donor-imposed stipulations that can be fulfilled by certain actions of the Organization. These are primarily contributions that are restricted for special programs, events and leasehold interest in facility. Permanently restricted net assets are contributions that have donor-imposed restrictions, whereby the amount of the gift is to be held in perpetuity.

**Income taxes:** The Organization is generally exempt from federal income taxes as a public charity under section 501(c)(3) of the Internal Revenue Code. The Organization files federal exempt income tax returns. As of December 31, 2016, generally, the federal and Minnesota tax returns for the Organization are open for examination by taxing authorities for the years 2014 to 2016. There was no material unrelated business income for the years ended December 31, 2016 and 2015.

As of December 31, 2016, management evaluated the Organization's tax positions and concluded that the Organization had taken no uncertain tax provisions that require adjustment to the financial statements to comply with the provisions of the Income Taxes Topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification.

**Pension plan:** The Organization maintains a noncontributory pension plan for all qualified employees. Contributions to the plan are at the discretion of the Board of Directors. Pension expense was approximately \$2,100 and \$4,000 for the years ended December 31, 2016 and 2015, respectively.

**Note 1. Summary of Significant Accounting Policies (Continued)**

**Recent accounting pronouncements:** In May 2014, the FASB issued Accounting Standards Updated (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, requiring an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The updated standard will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective and permits the use of either a full retrospective or retrospective with cumulative effect transition method. The updated standard becomes effective for the Organization for the year beginning January 1, 2019. Management has not yet selected a transition method and is currently evaluating the effect that the updated standard will have on the financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. While both lessees and lessors are affected by the new guidance, the effects on lessees are much more significant. The most significant change for lessees is the requirement under the new guidance to recognize right-of-use assets and lease liabilities for all leases not considered short-term leases. For short-term leases, lessees may elect an accounting policy by class of underlying asset under which right-of-use assets and lease liabilities are not recognized and lease payments are generally recognized as expense over the lease term on a straightline basis. This change will result in lessees recognizing right-of-use assets and lease liabilities for most leases currently accounted for as operating leases under the legacy lease accounting guidance. For many entities, this could significantly affect the financial ratios they use for external reporting and other purposes, such as debt covenant compliance. The ASU is effective for the Organization for the year beginning January 1, 2020. Management is currently evaluating the effect that the standard will have on its financial statements.

In August 2016, the FASB issued accounting standard update (ASU) No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, to improve the current net asset classification requirements and the information presented in the financial statements and notes about a not-for-profit entity's liquidity, financial performance, and cash flows. ASU 2016-14 will be effective for the Organization for fiscal years beginning after December 15, 2017.

In September 2016, the FASB issued accounting standard update (ASU) No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force)*, which addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. ASU 2016-15 will be effective for the Organization for fiscal years beginning after December 15, 2018.

**Subsequent events:** In preparing these financial statements, the Organization has evaluated events and transactions for potential recognition or disclosure through November 3, 2017, the date the financial statements were available to be issued.

**Note 2. Pledges Receivable**

As of December 31, 2016 and 2015, pledges receivable are approximately \$63,300 and \$25,000, respectively, and are all expected to be collected in the next year. Accordingly, an allowance for uncollectible pledges receivable has not been established.

## Rochester Art Center

### Notes to Financial Statements

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#### Note 3. Net Assets

Permanently restricted net assets, with the earnings available to support donor purposes, as of December 31, 2016 and 2015, consisted of the following:

	2016	2015
Endowment Fund: The fund was established in 2005 to support the long-term financial stability of the Rochester Art Center.	\$ 1,100	\$ 1,100
John Riese Memorial Fund: The fund was established in 1994 to recognize high school students' excellence in art.	7,020	7,020
	<u>\$ 8,120</u>	<u>\$ 8,120</u>

Temporarily restricted net assets as of December 31, 2016 and 2015, consisted of the following:

	2016	2015
Purpose restricted:		
Public exhibitions and admissions	\$ 23,000	\$ 29,683
Art education and scholarships	7,500	33,518
Time restricted:		
Operations	58,530	19,570
Time restricted based on the life of the lease agreement:		
Leasehold interest in facility	6,009,011	6,177,488
	<u>\$ 6,098,041</u>	<u>\$ 6,260,259</u>

#### Note 4. Funds Held by Others

**Rickee Henoch Art Fund:** The Rickee Henoch Art Fund is a donor-designated fund established in 1989 to provide funding for the Rochester Art Center in support of its programs, special events or other special needs relating to arts and education. The principal and investment of the funds are under the control of the Rochester Area Foundation, which has the ability to grant out the income of the fund to the Organization, and are not reflected in the Organization's financial statements. The total funds held by the Rochester Area Foundation as of December 31, 2016 and 2015, were \$22,730 and \$22,095, respectively. The Organization did not receive any distributions from this fund in 2016 or 2015.

**Rochester Art Center Fund:** The Rochester Art Center Fund is an agency endowment fund established by the Organization in 1998 to provide long-term sustainable endowment growth for the Organization. The principal and investment of the funds are under the control of the Rochester Area Foundation, which has the ability to grant out the income of the fund to the Organization, or other similar board-approved organizations, and are not reflected in the Organization's financial statements. The total funds held by the Rochester Area Foundation as of December 31, 2016 and 2015, were \$12,565 and \$12,190, respectively. The Organization did not receive any distributions from this fund in 2016 and 2015, respectively.

## Rochester Art Center

### Notes to Financial Statements

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#### **Note 5. Leasehold Interest in Facility and Concentration**

The Organization completed a capital campaign to fund the construction of the current facility, which was completed in 2004 and constructed on land owned by the City of Rochester (the City). The Organization exchanged the facility with the City for a 50-year lease. The lease terms are a \$1 annual fee through December 2052. This agreement results in a contribution reported on the accompanying statements of financial position as a leasehold interest in facility. The Organization recognized a release from restriction and amortization of leasehold interest of \$168,477 in each year ended December 31, 2016 and 2015. The Organization is responsible for routine maintenance, and the City is responsible for major capital improvements.

The Organization receives a significant amount of support from the City in the form of other unrestricted contributions for operating activities and grants for minor facility improvements. For the years ended December 31, 2016 and 2015, the Organization recognized approximately \$443,000 and \$337,000, respectively, in grant revenues and approximately \$6,000, in facility repairs. This support from the City represents approximately 43 percent and 37 percent of total revenues for the years ended December 31, 2016 and 2015, respectively.

#### **Note 6. Going Concern and Management's Plans**

The accompanying financial statements for the year ended December 31, 2016, have been prepared assuming the Organization will continue as a going concern. Management has assessed its ability to continue as a going concern and has determined that due to the liquidity position and recurring losses from operations, substantial doubt about its ability to continue as a going concern one year after the financial statements were available to be issued, on November 3, 2017, exists. The following are management's observations, comments and plans to mitigate the going concern matter.

There were improvements in operating performance during 2016, which management believes demonstrate the Organization's ability to function as a going concern. Specifically, the Organization reduced its net operating loss by more than 16 percent compared to 2015, which was achieved through increases in general contributions, grants and expense reductions which began at the end of the year.

In 2017, the Organization initiated a multistage restructuring plan that is being implemented in 2017 and 2018, led by a new interim executive director. The plan includes reducing the existing net asset deficiency and creating a reserve fund for future operational reliability by:

- Increasing general attendance and contributions by leveraging connectivity with the Rochester and greater Minnesota community (general attendance increased 2,900 individuals the first 3 months of 2017 compared to 2016).
- Decreasing expenses for staffing, operations, and programming that are not vital to support the revenue producing activities of the Organization. In 2016, salaries, related benefits expense and contract labor expense was approximately \$624,000. As of September 2017, salaries, related benefits expense and contract labor expense was approximately \$342,000
- Implementing project based budgeting with internal measurements and controls for all projects.
- The Organization does not anticipate any significant reductions in current funding sources as identified at September 30, 2017. A loss of any significant funding sources could further increase the risk of continued existence to the Organization.



## **Rochester Art Center**

### **Notes to Financial Statements**

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#### **Note 6. Going Concern and Management's Plans (Continued)**

Based on these efforts, management projects that there will be improvements to the liquidity position for 2017 and 2018. As of September 2017, these efforts have resulted in the growth of cash by approximately \$31,500 and a reduction of current liabilities of approximately \$121,000. Additionally, through September 2017, the Organization continues to be on-track to achieve revenues exceeding expenses before depreciation and amortization for the year ending December 31, 2017. The 2018 Budget, prepared as a result of the restructuring, also projects revenues exceeding expenses before depreciation and amortization.

These financial statements do not include adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Organization be unable to continue as a going concern.