

Financial Statements
Years Ended
December 31, 2013 and 2012



The Mariners' Museum

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Independent Auditors' Report

Board of Trustees
The Mariners' Museum

We have audited the accompanying financial statements of *The Mariners' Museum*, which comprise the statements of financial position as of December 31, 2013 and 2012, 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of *The Mariners' Museum* as of December 31, 2013 and 2012, 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.

Dixon Hughes Goodman LLP

Newport News, Virginia
May 23, 2014

The Mariners' Museum

Statements of Financial Position

December 31,	2013	2012
Assets		
Current assets		
Cash and cash equivalents		
Unrestricted	\$ 2,796,308	\$ 2,762,972
Restricted (Note 3)	1,395,788	1,508,582
Certificates of deposit	1,389,228	1,385,069
Accounts receivable	4,308	12,424
Current portion of pledges receivable (Note 4)	855,928	1,273,920
Inventories	217,262	214,717
Other current assets	342,743	63,659
Total current assets	7,001,565	7,221,343
Property and equipment - net (Note 6)	31,915,881	33,357,246
Other assets		
Investments		
Investments (Note 5)	15,986,743	14,636,058
Beneficial interest in trusts (Note 7)	89,131,722	83,240,976
Pledges receivable - less current portion (Note 4)	1,213,017	1,661,020
Total other assets	106,331,482	99,538,054
	\$ 145,248,928	\$ 140,116,643
Liabilities and Net Assets		
Current liabilities		
Accounts payable	\$ 118,782	\$ 68,558
Accrued expenses	427,791	373,567
Total current liabilities	546,573	442,125
Long-term liabilities		
Charitable gift annuities (Note 9)	85,685	100,041
Bond payable (Note 11)	9,600,000	9,600,000
Deferred revenue (Note 10)	5,875,394	5,760,442
Total liabilities	16,107,652	15,902,608
Net assets		
Unrestricted	36,640,730	37,837,404
Temporarily restricted (Note 12)	2,783,835	2,600,644
Permanently restricted (Note 12)	89,716,711	83,775,987
Total net assets	129,141,276	124,214,035
	\$ 145,248,928	\$ 140,116,643

The accompanying notes are an integral part of these financial statements.

The Mariners' Museum

Statement of Activities

Year Ended December 31, 2013	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue, gains and support				
Realized and unrealized gains (losses) on investments - net	\$ 1,217,364	\$ (15,921)	\$ 5,942,958	\$ 7,144,401
Grants	184,498	-	-	184,498
Contributions	790,256	352,750	1,100	1,144,106
Income from funds held in trust by others	4,099,260	-	-	4,099,260
Dividend and interest income - net	275,470	75,434	8,686	359,590
Museum shop	166,581	-	-	166,581
Admission fees	355,555	-	-	355,555
Miscellaneous	205,694	14,107	-	219,801
Lease	161,289	-	-	161,289
Education program fees	89,983	-	-	89,983
Photography	45,281	-	-	45,281
Facility rental	138,506	-	-	138,506
Chris Craft	31,214	-	-	31,214
Publications	1,683	-	-	1,683
Boat house	5,745	-	-	5,745
Deaccession	5,835	-	-	5,835
Change in valuation of charitable gift annuities	-	-	(12,020)	(12,020)
Net assets released from restrictions	243,179	(243,179)	-	-
Total revenue, gains and support	8,017,393	183,191	5,940,724	14,141,308
Program expenses				
Education	265,445	-	-	265,445
Collection management	192,384	-	-	192,384
Marketing and special events	777,309	-	-	777,309
Curatorial and conservation	606,796	-	-	606,796
Park and Noland Trail	94,428	-	-	94,428
Facilities management	87,948	-	-	87,948
Library and archives	322,402	-	-	322,402
Exhibit design and production	211,696	-	-	211,696
Photography	145,180	-	-	145,180
Admissions	211,362	-	-	211,362
Museum shop	147,097	-	-	147,097
Publications and graphic design	548	-	-	548
Chris Craft	20,971	-	-	20,971
Total program expenses	3,083,566	-	-	3,083,566
Supporting expenses				
General administration	3,501,568	-	-	3,501,568
Development and membership	495,478	-	-	495,478
Facilities management	2,113,396	-	-	2,113,396
Museum shop	20,059	-	-	20,059
Total supporting expenses	6,130,501	-	-	6,130,501
Total expenses	9,214,067	-	-	9,214,067
Change in net assets	(1,196,674)	183,191	5,940,724	4,927,241
Net assets - beginning of year	37,837,404	2,600,644	83,775,987	124,214,035
Net assets - end of year	\$ 36,640,730	\$ 2,783,835	\$ 89,716,711	\$ 129,141,276

The accompanying notes are an integral part of these financial statements.

The Mariners' Museum

Statement of Activities

Year Ended December 31, 2012	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue, gains and support				
Realized and unrealized gains (losses) on investments - net	\$ 781,487	\$ (22,821)	\$ 3,836,931	\$ 4,595,597
Grants	-	112,887	-	112,887
Contributions	593,463	422,500	100	1,016,063
Income from funds held in trust by others	3,948,855	-	-	3,948,855
Dividend and interest income - net	385,443	67,393	10,172	463,008
Museum shop	154,487	-	-	154,487
Admission fees	307,380	-	-	307,380
Miscellaneous	366,037	11,702	-	377,739
Lease	167,513	-	-	167,513
Education program fees	102,304	-	-	102,304
Photography	41,827	-	-	41,827
Facility rental	111,605	-	-	111,605
Chris Craft	36,492	-	-	36,492
Publications	7,034	-	-	7,034
Boat house	6,714	-	-	6,714
Deaccession	2,719	-	-	2,719
Café	68,808	-	-	68,808
Change in valuation of charitable gift annuities	-	-	(12,019)	(12,019)
Net assets released from restrictions	262,438	(262,438)	-	-
Total revenue, gains and support	7,344,606	329,223	3,835,184	11,509,013
Program expenses				
Education	273,184	-	-	273,184
Collection management	153,817	-	-	153,817
Marketing and special events	631,694	-	-	631,694
Curatorial and conservation	631,846	-	-	631,846
Park and Noland Trail	96,164	-	-	96,164
Facilities management	34,150	-	-	34,150
Library and archives	305,584	-	-	305,584
Exhibit design and production	235,893	-	-	235,893
Photography	139,795	-	-	139,795
Admissions	80,246	-	-	80,246
Museum shop	174,633	-	-	174,633
Café	100,315	-	-	100,315
Publications and graphic design	5,893	-	-	5,893
Chris Craft	24,637	-	-	24,637
Total program expenses	2,887,851	-	-	2,887,851
Supporting expenses				
General administration	3,527,974	-	-	3,527,974
Development and membership	383,361	-	-	383,361
Facilities management	1,929,873	-	-	1,929,873
Museum shop	13,144	-	-	13,144
Total supporting expenses	5,854,352	-	-	5,854,352
Total expenses	8,742,203	-	-	8,742,203
Change in net assets	(1,397,597)	329,223	3,835,184	2,766,810
Net assets - beginning of year	39,235,001	2,271,421	79,940,803	121,447,225
Net assets - end of year	\$ 37,837,404	\$ 2,600,644	\$ 83,775,987	\$ 124,214,035

The accompanying notes are an integral part of these financial statements.

The Mariners' Museum

Statements of Cash Flows

Years Ended December 31,	2013	2012
Cash flows from operating activities		
Change in net assets	\$ 4,927,241	\$ 2,766,810
Adjustments to reconcile to net cash from operating activities:		
Depreciation and amortization	1,771,714	1,871,915
Change in allowance for uncollectible pledges	124,635	(4,907)
Change in inventory allowance	(180)	2,314
Unrealized gains on investments		
Funds held in trust by others	(5,890,746)	(3,805,513)
Investments	(1,064,698)	(768,603)
Realized gains on investments	(188,957)	(21,481)
Change in valuation of charitable gift annuities	12,020	12,019
Change in:		
Accounts receivable	8,116	568
Pledges receivable	741,360	443,421
Inventories	(2,365)	64,364
Other current assets	(279,084)	37,287
Accounts payable	50,224	(85,448)
Accrued expenses	54,224	(22,527)
Deferred revenue	114,952	389,792
Net cash from operating activities	378,456	880,011
Cash flows from investing activities		
Property and equipment acquisitions	(330,349)	(466,453)
Sales and maturities of investments	952,850	3,114,005
Purchases of investments	(1,049,881)	(4,011,125)
Maturation of certificate of deposit	-	1,359,283
Purchase of certificate of deposit	(4,159)	(1,385,069)
Net cash from investing activities	(431,539)	(1,389,359)
Cash flows from financing activities		
Payments on charitable gift annuities	(26,375)	(26,375)
Proceeds from bond payable	-	86,619
Net cash from financing activities	(26,375)	60,244
Net change in cash and cash equivalents	(79,458)	(449,104)
Cash and cash equivalents - beginning of year	4,271,554	4,720,658
Cash and cash equivalents - end of year	\$ 4,192,096	\$ 4,271,554
Supplemental disclosure of cash flow information		
Cash paid for interest	\$ 262,501	\$ 300,532
Supplemental disclosure of noncash information		
Construction in progress transferred to property and equipment for assets placed in service	\$ 338,705	\$ 279,400

The accompanying notes are an integral part of these financial statements.

The Mariners' Museum

Notes to Financial Statements

December 31, 2013 and 2012

1. Organization and Nature of Activities

The Mariners' Museum (Museum) is a Virginia nonprofit educational and cultural institution which was incorporated in May 1930, and is located in Newport News, Virginia. The stated mission of *The Mariners' Museum* is to make a difference in people' lives, inviting them to discover their relationship to the sea by exploring maritime culture, science and technology. *The Mariners' Museum* uses its art and artifacts to educate local, national and international audiences of all ages about the vital role of the sea in mankind's development.

2. Summary of Significant Accounting Policies

Accounting Method

The financial statements of the Museum have been prepared on the accrual basis in accordance with accounting principles generally accepted in the United States of America; revenue and gains are recognized when earned, and expenses and losses are recognized when incurred. The significant accounting policies are described below to enhance the usefulness of the financial statements to the reader.

Basis of Presentation

The financial statements report amounts separately by classes of net assets.

Unrestricted amounts are those currently available at the discretion of the Museum's Board of Trustees for use in operations and those resources invested in property and equipment.

Temporarily restricted amounts are those which are stipulated by donors for specific operating purposes or for the acquisition of property and equipment. When a donor restriction is satisfied, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities as net assets released from restrictions.

Permanently restricted amounts are those donated with a stipulation that they be invested to provide a permanent source of revenue. Such revenue is expendable in accordance with the conditions of each specific donation.

All contributions are considered available for unrestricted use unless specifically restricted by the donor or subject to other legal restrictions.

Cash and Cash Equivalents

The Museum considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents. Included in cash and cash equivalents balances are amounts restricted, primarily for future property and equipment acquisitions.

Certificates of Deposit

Excess cash is invested in certificates of deposit, which mature at various times and earns interest at various rates. Certificates of deposit are stated at cost plus accrued interest earned.

Inventories

Inventories consist of gift shop items and publications and are stated at the lower of cost (determined using the first-in, first-out method) or market. Inventory related to the Museum Shop was \$174,755 and \$170,589 at December 31, 2013 and 2012, respectively, and publications inventory was \$47,230 and \$49,031 at December 31, 2013 and 2012, respectively. At December 31, 2013 and 2012, a valuation allowance of \$4,723 and \$4,903, respectively, was recorded for slow-moving publications inventory.

Investments

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the statements of financial position. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. See Note 13 for discussion of fair value measurements. Investments in mortgage backed securities are valued at their fair value as determined by the investment company from prices obtained from independent quotation bureaus that use computerized valuation formulas to calculate current value. Investment distribution or loss (including gains and losses on investments, interest and dividends) is included in the statements of activities as increases or decreases in unrestricted net assets unless the income or loss is restricted by donor or law.

Beneficial interest in trusts represent resources neither in the possession nor under the control of the Museum, but held and administered by outside fiscal agents, with the Museum deriving income from such funds. The trusts are stated at fair value. The assets held in trust are classified as permanently restricted. The distribution received from the trusts is classified as increases in unrestricted net assets in the accompanying statements of activities. Unrealized gains or losses of the assets held by the trusts are reflected as a change in permanently restricted net assets on the accompanying statements of activities.

Property and Equipment

Property and equipment are stated at cost on acquisition date or fair value on gift date. Property and equipment, except land and lakes, dams and improvements, are depreciated by the straight-line method over their estimated useful lives as follows:

	<u>Years</u>
Building and improvements	5 - 59
Furniture and equipment	2 - 20
The Noland Trail	20
Land improvements	10 - 20

Maintenance and ordinary repairs are expensed; improvements are capitalized. Gains and losses arising from disposal or retirement of property and equipment are recognized currently in the accompanying statements of activities and the cost and related accumulated depreciation, if applicable, are removed from the accounts. For capital assets purchased with restricted cash or donated capital assets, the Museum does not impose a restriction on the length of time the assets must be held. The Museum's policy is to capitalize all items with a useful life greater than one year.

Collection

The Museum maintains significant collection assets, including models, small crafts, prints, paintings, books, photographs, and navigation instruments. In accordance with industry practice, the value of the collection has been excluded from the statements of financial position. Only current year purchases and proceeds from sale are reflected in the statements of activities. It is the policy of the Museum that proceeds from the sale of any collection items are to be used for the acquisition of objects for the permanent collections or for the conservation or maintenance of items currently owned by the Museum by external conservators.

Pledges Receivable

Pledges receivable are recognized as revenue in the period the promise is made by the donor. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. An allowance for uncollectible pledges receivable is provided based upon management's judgment, including such factors as prior collection history and type of pledge.

The Museum received in-kind contributions of \$158,480 and \$9,458 in 2013 and 2012, respectively. These contributions were primarily related to advertising and artifacts. Additionally, the Museum received volunteer hours of 15,785 and 17,334 in 2013 and 2012, respectively. No amounts have been recognized in the statements of activities for donated services because the criteria for recognition under applicable accounting standards have not been satisfied.

Restricted Contributions

Contributions received by the Museum with donor-imposed temporary restrictions, which are not met within the same reporting period, are reported as temporarily restricted revenues. The revenue is then shown as released from restrictions on the accompanying statements of activities when the restriction has been satisfied.

Use of Estimates

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

Functional Expenses

The Museum allocates its expenses on a functional basis among its various programs and supporting services. Expenses that can be identified with a specific program or supporting service are allocated directly. Other expenses that are common to several functions are allocated by various statistical bases.

Advertising Costs

Advertising costs are expensed as incurred and were \$119,901 and \$140,358 for 2013 and 2012, respectively, excluding donated advertising.

Income Taxes

The Museum is a nonstock corporation which has been determined by the Internal Revenue Service to be exempt from taxes on income derived from activities related to its exempt purpose under Section 501(c)(3) of the Internal Revenue Code. The Museum is subject to income taxes on profits, if any, generated from the sale of items in its gift shop which are unrelated to its exempt purpose. The Internal Revenue Service has also determined that the Museum is not a private foundation under Section 509(a)(1). The Museum has determined that it does not have any material unrecognized tax benefits or obligations as of December 31, 2013 and 2012. Fiscal years ending on or after December 31, 2010, remain subject to examination by federal and state tax authorities.

Credit Risk

Financial instruments that potentially expose the Museum to concentrations of credit risk consist primarily of cash and cash equivalents, certificates of deposit, and investments. Cash and cash equivalents, certificates of deposit and investments are maintained at high quality financial institutions and exposure is limited to any one institution. During 2009, the Museum entered into a sweep to master note agreement where cash and cash equivalents in this account are invested in master note obligations that mature daily. Master note obligations are not bank deposits and; therefore, are not insured or guaranteed by the Federal Deposit Insurance Corporation (FDIC). At December 31, 2013 and 2012, \$3,749,664 and \$3,947,578, respectively, of cash and cash equivalents were held in the sweep account. All other accounts at financial institutions are insured by the FDIC up to the legal limit. The Museum has not experienced any losses on its cash equivalents.

Reclassifications

Certain reclassifications have been made to the 2012 financial statements to correspond to the current year format. Total net assets and change in net assets are unchanged due to these reclassifications.

Subsequent Events

In preparing these financial statements, the Museum has evaluated events and transactions for potential recognition or disclosure through May 23, 2014, the date the financial statements were available to be issued.

3. Restricted Cash

The Museum's restricted cash is held for the following restriction:

	2013	2012
Maritime Galleries and Exhibit Funding	\$ 1,395,788	\$ 1,508,582

4. Pledges Receivable

The Museum records pledges receivable as income in the year the promise is received. Pledges receivable have the following restrictions:

	2013	2012
The Monitor Center campaign	\$ 2,017,134	\$ 2,720,989
General operating and library support	51,811	212,951
Other temporarily restricted contributions	-	1,000
	<u>\$ 2,068,945</u>	<u>\$ 2,934,940</u>

The anticipated cash flows from pledges receivable is as follows:

	2013	2012
Receivable in less than one year	\$ 855,928	\$ 1,273,920
Receivable in one to five years	1,431,928	1,766,191
Total pledges receivable	<u>2,287,856</u>	<u>3,040,111</u>
Less - discounts to net realizable value	(33,911)	(44,806)
Less - allowance for uncollectible pledges	(185,000)	(60,365)
	<u>2,068,945</u>	<u>2,934,940</u>
Less - current portion	(855,928)	(1,273,920)
	<u>\$ 1,213,017</u>	<u>\$ 1,661,020</u>

At December 31, 2013 and 2012, the discount rates used ranged from 0.25% to 4.9%.

5. Investments

Investments are presented at fair value and consist of the following:

	2013	2012
Equity securities	\$ 6,632,980	\$ 5,771,508
Bonds	6,697,134	6,232,690
Real estate securities	563,352	544,907
Money funds	697,489	687,735
Mortgage-backed securities	1,395,788	1,399,218
	<u>\$ 15,986,743</u>	<u>\$ 14,636,058</u>

The investments are under the management of Frank Russell Investment Company, UBS Commercial Services, Inc., and Wells Fargo Advisors, LLC, who also maintain custody of the securities. The Museum's investments are in mutual funds and investment income is reported in the accompanying statements of activities, net of investment management fees.

Fair values and unrealized gains (losses) are summarized as follows:

<u>December 31, 2013</u>	Cost	Fair Value	Unrealized Gain (Loss)
Frank Russell Investment Company	\$ 12,817,477	\$ 14,540,215	\$ 1,722,738
Wells Fargo Advisors, LLC	48,750	50,740	1,990
UBS Commercial Services, Inc.	1,403,151	1,395,788	(7,363)
	<u>\$ 14,269,378</u>	<u>\$ 15,986,743</u>	<u>\$ 1,717,365</u>
<u>December 31, 2012</u>			
Frank Russell Investment Company	\$ 12,482,327	\$ 13,083,461	\$ 601,134
Wells Fargo Advisors, LLC	41,068	44,016	2,948
UBS Commercial Services, Inc.	1,498,477	1,508,581	10,104
	<u>\$ 14,021,872</u>	<u>\$ 14,636,058</u>	<u>\$ 614,186</u>

6. Property and Equipment

Property and equipment consist of the following:

	<u>2013</u>	<u>2012</u>
Building and improvements	\$ 50,766,676	\$ 50,585,292
Furniture and equipment	6,340,823	6,183,502
The Noland Trail	2,219,802	2,219,802
Land improvements	4,656,952	4,656,952
Lakes, dams and improvements	626,901	626,901
	<u>64,611,154</u>	<u>64,272,449</u>
Less - accumulated depreciation	(32,697,226)	(30,925,512)
	<u>31,913,928</u>	<u>33,346,937</u>
Construction in process	1,953	10,309
	<u>\$ 31,915,881</u>	<u>\$ 33,357,246</u>

Depreciation expense for 2013 and 2012 was \$1,771,714 and \$1,871,915, respectively.

7. Beneficial Interest in Trusts

The Museum is the beneficiary of various irrevocable trusts established by the Museum founder, Archer M. Huntington, that are classified as permanently restricted. The Museum receives distributions on the securities held by the trusts. These distributions are reported in the accompanying statements of activities, net of expenses. The Museum paid management fees to JP Morgan Chase Bank of \$212,255 and \$203,533 in 2013 and 2012, respectively.

The value recorded for the beneficial interest in trusts is comprised of the following:

	2013	2012
JP Morgan Chase Bank Trust #03152009	\$ 46,721,577	\$ 47,534,610
JP Morgan Chase Bank Trust #03583005	31,815,694	32,815,822
JP Morgan Chase Bank Trust #98940006	2,740,716	-
JP Morgan Chase Bank Trust #98843002	2,196,980	-
JP Morgan Chase Bank Trust #03152306	1,529,819	-
JP Morgan Chase Bank Trust #03583302	1,020,405	-
SunTrust Bank Trust #13214200	1,925,109	1,747,292
Bank of America (formerly U.S. Trust Co. of New York #239550)	815,873	755,833
Bank of New York #676580	184,480	193,831
Bank of New York #676730	102,249	109,406
Bank of New York #676760	78,820	84,182
	<u>\$ 89,131,722</u>	<u>\$ 83,240,976</u>

During 2013, the funds held in trust in the Museum's JP Morgan Chase Bank Trusts were split into several new trust accounts for portfolio diversification purposes.

The Museum has adopted a total return policy with respect to distributions received from its Huntington Trust at JP Morgan. This total return policy allows the Museum to receive distributions based upon 4.5% of the rolling average market value of the trusts, using the quarter end value for the preceding twelve quarters, ending with September 30 of the current year. For 2013 and 2012, the Board of Trustees approved a temporary increase to the total return policy which allowed the Museum to receive distributions based upon 5% of the preceding twelve quarters rolling average of the fair market value of the trusts. The remaining trusts also pay out 5% of the trust assets on an annual basis.

The Museum is also a co-beneficiary with three other not-for-profit organizations under the trust agreement with Bank of America (formerly U.S. Trust Co., of New York). Therefore, the amount recorded in the accompanying statements of financial position is 25% of the trust's value, which represents the Museum's share under this split-interest agreement.

8. Retirement Plan

The Museum has a 403(b) Tax Deferred Retirement Plan. The Plan is a defined contribution plan covering substantially all employees. Employees may contribute to the Plan subject to the limitations imposed by the Internal Revenue Service. Effective March 1, 2009, the Museum no longer makes contributions to the Plan.

9. Charitable Gift Annuities

The Museum holds charitable gift annuities, recognized at fair value, which earn income that is permanently restricted and added to the annuity until the donor's death. Upon the donor's death, the annuity becomes a part of the Museum's endowment fund, and any subsequent distribution earned is available to support Museum operations. The liability to beneficiaries was \$85,685 and \$100,041, at December 31, 2013 and 2012, respectively. The discount rates used to calculate the fair value ranged from 4.20% to 7.60% for both 2013 and 2012.

10. Deferred Revenue

The Museum's deferred revenue consists primarily of four lease agreements for portions of the Museum's land. In connection with the first agreement, the Museum received an advance rental payment of \$5,000,000, and the lease term extends through 2061. The Museum has deferred the recognition of the amount received, and is amortizing the revenue on a straight-line basis over the lease term at an annual amount of \$69,204. The amount deferred is \$3,321,798 and \$3,391,002 at December 31, 2013 and 2012, respectively.

The second lease agreement provides for 20 annual installment payments of \$270,811. The lessee has the option to purchase the land anytime during the lease term, which expires July 5, 2017. The payments include principal and interest at 6% and the Museum recognized lease income of \$64,425 and \$76,415 in 2013 and 2012, respectively. The Museum deferred the principal payments, which will be recognized at the end of the lease term. These deferred amounts are \$2,189,066 and \$1,982,680 at December 31, 2013 and 2012, respectively.

The third lease agreement commenced on December 1, 2010, and was for an initial term of 20 years. The rent for the initial term was \$65,000, paid upon the commencement of the lease. The lessee had two options to renew the lease for 20 and 30 years, respectively, by making payments upon exercise of those options in the amount of \$25,000 and \$20,000, respectively. The lessee has chosen to exercise both options by making the payments with respect to those options. The term of the lease now ends on November 30, 2080. The Museum has deferred recognition of the amount received, and is amortizing the revenue over the lease term at the following rates, \$3,250 annually over the first 20 years, through 2030, \$1,250 annually for the next 20 years, 2030 - 2050, and \$667 annually for the final 30 years, 2050 - 2080. The deferred amounts are \$99,979 and \$103,229 at December 31, 2013 and 2012, respectively.

During 2012, the Museum entered into a fourth lease agreement, similar to the above. The lease commenced on May 1, 2012, and was for an initial term of 18.5 years. The rent for the initial term was \$143,780, paid upon the commencement of the lease. The lessee had two options to renew the lease for 20 and 30 years, respectively, by making payments upon exercise of those options in the amount of \$65,492 and \$42,650, respectively. The lessee has chosen to exercise both options by making the payments with respect to those options. The term of the lease now ends on November 30, 2080. The Museum has deferred recognition of the amount received, and is amortizing the revenue over the lease term at the following rates, \$7,772 annually over the first 18.5 years, through 2030, \$3,275 annually for the next 20 years, 2030 - 2050, and \$1,422 annually for the final 30 years, 2050 - 2080. The deferred amounts are \$238,969 and \$246,741 at December 31, 2013 and 2012, respectively. Additionally, the Museum had various deferred amounts of \$25,582 and \$36,790 at December 31, 2013 and 2012, respectively.

11. Bond Payable

On October 1, 2005, the Museum entered into an agreement with the Industrial Development Authority of Mathews County, Virginia under which it issued a \$10,000,000 fixed rate bank qualified tax-exempt bond, which was unsecured. The bond provided for a maximum borrowing of \$10,000,000, bore interest at a fixed rate of 4.03% and interest only was payable monthly beginning January 1, 2006, through November 1, 2015, at which time the entire outstanding principal balance was to be due along with any accrued interest.

The Museum has used the proceeds from the bond to finance the 65,000 square foot expansion of the Museum called the USS *Monitor* Center.

On February 1, 2012, the Museum refinanced the bond arrangement. Under the new agreement with the Economic Development Authority of Lancaster County, Virginia, the Museum was issued a \$9,600,000 fixed rate bank qualified tax-exempt bond, which is unsecured. This new bond issue retired the existing debt. The bond bears interest at a fixed rate of 2.7% and accrued interest on the unpaid principal balance is due monthly through April 1, 2027. On April 1, 2018, the Museum will begin annual principal payments of \$960,000 through April 1, 2027, when the bond is due and payable in full. Interest expense related to these bonds was \$262,800 and \$288,703 for 2013 and 2012, respectively.

12. Net Asset Restrictions

Temporarily restricted net assets are available for the following purposes:

	2013	2012
Program restrictions	\$ 2,783,835	\$ 2,600,644

Permanently restricted net assets are invested to:

	2013	2012
Beneficial interest in trusts, a portion of the spending rate which is available to support operations	\$ 89,131,722	\$ 83,240,976
Endowment funds	584,989	535,011
	\$ 89,716,711	\$ 83,775,987

13. Fair Value Measurements

Accounting standards established a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1: Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Museum has the ability to access.

Level 2: Inputs to the valuation methodology include:

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical assets or liabilities in inactive markets;
- inputs other than quoted prices that are observable for the asset or liability;
- inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

Level 3: Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset or liability's fair value measurement within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at December 31, 2013 and 2012.

Mutual funds: Valued at the closing price reported on the active market on which the mutual funds are traded.

Money funds: Short-term securities purchased within 60 days to maturity are valued at amortized cost, which approximates market value.

Mortgage-backed securities: Prices of asset backed securities are obtained from independent quotation bureaus that use computerized valuation formulas to calculate current values.

Pledges receivable: Pledges receivable are reported at net realizable value if at the time the promise is made payment is expected to be received in one year or less. Pledges receivable that are expected to be collected in more than one year are reported at fair value initially and, in subsequent periods, fair value is calculated as the present value of the expected future pledges to be received using a discount rate.

Beneficial interest in trusts: Valued using the fair value of the underlying assets of the trust as an estimate for the present value of the expected future cash flows.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Museum believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following sets forth by level, within the fair value hierarchy, the Museum's assets at fair value:

Assets at Fair Value as of December 31, 2013				
	Level 1	Level 2	Level 3	Total
Trading securities:				
Mutual funds - bonds / fixed income	\$ 6,697,134	\$ -	\$ -	\$ 6,697,134
Mutual funds - international	1,208,183	-	-	1,208,183
Mutual funds - real estate	563,352	-	-	563,352
Mutual funds - equity - other	5,424,797	-	-	5,424,797
Money funds	697,489	-	-	697,489
Fixed income:				
Residential mortgage-backed securities	-	-	1,395,788	1,395,788
	14,590,955	-	1,395,788	15,986,743
Pledges receivable	-	-	2,068,945	2,068,945
Beneficial interest in trusts	-	-	89,131,722	89,131,722
Total assets at fair value	\$ 14,590,955	\$ -	\$ 92,596,455	\$ 107,187,410

Assets at Fair Value as of December 31, 2012

	Level 1	Level 2	Level 3	Total
Trading securities:				
Mutual funds - bonds/fixed income	\$ 6,232,689	\$ -	\$ -	\$ 6,232,689
Mutual funds - international	1,045,127	-	-	1,045,127
Mutual funds - real estate	544,907	-	-	544,907
Mutual funds - equity - other	4,726,382	-	-	4,726,382
Money funds	687,734	-	-	687,734
Fixed income:				
Residential mortgage-backed securities	-	-	1,399,219	1,399,219
	13,236,839	-	1,399,219	14,636,058
Pledges receivable	-	-	2,934,940	2,934,940
Beneficial interest in trusts	-	-	83,240,976	83,240,976
Total assets at fair value	\$ 13,236,839	\$ -	\$ 87,575,135	\$ 100,811,974

The table below sets forth a summary of changes in the fair value of the Museum's level 3 investment assets:

	Residential Mortgage- backed Securities	Pledges Receivable	Beneficial Interest in Trusts
Balance - December 31, 2012	\$ 1,399,219	\$ 2,934,940	\$ 83,240,976
Total gains and losses included in change in net assets	(64,440)	-	-
Interest and dividends	60,252	-	-
Investment sales	(664,339)	-	-
Investment purchases	777,180	-	-
Withdrawals	(112,084)	-	-
New pledges	-	56,610	-
Pledge collections	-	(808,865)	-
Pledges written off	-	-	-
Adjustment to fair value	-	(113,740)	5,890,746
Balance - December 31, 2013	\$ 1,395,788	\$ 2,068,945	\$ 89,131,722

14. Donor-Designated Endowments (UPMIFA State) After Implementation of FSP FAS 117-1

The Mariners' Museum Endowment (Endowment) was established to support its mission. The Endowment substantially contributes to the growth, financial security and the long-term stability of the Museum.

The Endowment includes two general categories of funds. One category of funds is donor-restricted funds that are restricted for a particular purpose. The second category of funds is composed of receipts from long-term rentals of real estate (primarily described in Note 10) and gifts and bequests to the Museum by donors, which are unrestricted, which the Board of Trustees has designated to function as permanently restricted endowments. With respect to donor-restricted funds, the net assets associated with these endowment funds are classified and reported based on the existence of donor-imposed restrictions. The Board of Trustees of the Museum has interpreted the State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Museum classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. In accordance with SPMIFA, the Museum considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the various funds, (2) the purposes of the donor-restricted endowment funds, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, (6) other resources of the Museum, and (7) the Museum's investment policies.

Board Designated Endowment. With respect to those unrestricted funds designated by the Board of Trustees to function as endowments, the operative resolution allows the Board of Trustees to set a spending policy based on such factors as the Board determines appropriate, including, but not limited to, the general economic conditions, the needs of the Museum, the possible effect of inflation and deflation, the expected total return from income and the appreciation of investments, and other resources available to the Museum.

The Board Designated Endowment may be expended only with the prior approval of at least two-thirds of the members of the Board of Trustees in office; provided, however, that during any period of five consecutive years, no more than 25% of the principal of the Endowment, measured as of the beginning of that five-year period, may be expended or distributed. The Museum may make loans from the Endowment to the Museum, for its general purpose or for special programs or projects, upon such terms as the Board of Trustees may determine; provided, however, that any loan shall be considered to be a distribution of principal for the purposes of the approval requirement previously stated.

Investment Return Objectives, Risk Parameters and Strategies. The Museum has adopted investment and spending policies, approved by the Board of Trustees, for endowment assets that attempt to provide a predictable stream of distributions to programs supported by its endowment funds while also maintaining the purchasing power of those endowment assets over the long-term. Accordingly, the investment process seeks to maximize the total return of the Endowment to ensure conservation of the principal while providing appreciable yield, to the extent financially prudent and practicable. Endowment assets are invested in a well-diversified asset mix that is intended to result in a consistent inflation-protected rate of return. Generally, total return shall mean for this purpose that (1) assets are invested to achieve the highest overall return (interest, dividends, and realized as well as unrealized appreciation), consistent with the safety and preservation of the assets and (2) the Board of Trustees, or its designee, may annually determine the amount of the total return that will be treated as distributions available for current use. Investment risk is measured in terms of the total endowment fund; investment assets and allocation between asset classes and strategies are managed to not expose the fund to unacceptable levels of risk.

Spending Policy. The Museum Board of Trustees governs the use of the Endowment and identifies the mission related programs and services for which the funds will be used.

Composition of and changes in endowment net assets at December 31, 2013, are presented below.

Donor-designated endowment net asset composition is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Donor restricted endowment funds	\$ -	\$ -	\$ 584,989	\$ 584,989

Changes in endowment net assets were as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Endowment net assets - beginning of year	\$ -	\$ -	\$ 535,011	\$ 535,011
Contributions	-	-	1,100	1,100
Investment income	-	-	8,686	8,686
Net appreciation	-	-	40,192	40,192
Endowment net assets - end of year	\$ -	\$ -	\$ 584,989	\$ 584,989

Composition of and changes in endowment net assets at December 31, 2012, are presented below.

Endowment net asset composition and type of fund is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Donor restricted endowment funds	\$ -	\$ -	\$ 535,011	\$ 535,011

Donor-designated endowment net asset composition is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total Net Endowment Assets
Endowment net assets - beginning of year	\$ -	\$ -	\$ 505,340	\$ 505,340
Contributions	-	-	100	100
Investment income	-	-	10,172	10,172
Net depreciation	-	-	19,399	19,399
Endowment net assets - end of year	\$ -	\$ -	\$ 535,011	\$ 535,011

15. Leasing Arrangements

The Museum leases a 5,400 square foot building to National Oceanic and Atmospheric Administration (NOAA) under a noncancelable lease that expires in February 2025. The lease agreement provides for annual rental payments of \$2,500 per year plus reimbursement of operating expenses incurred by the Museum for the upkeep and maintenance of the building as a shared expense. The operating expenses are estimated by the Museum at the beginning of each year and split into twelve equal installments to be paid by NOAA. Within 120 days after the end of each year the Museum adjusts the rent charged for the actual operating expenses incurred to NOAA and either credits their future rent or requires additional payment, as necessary. The following is a summary of future minimum rental income under the noncancelable operating lease:

Future minimum payments on the above long-term lease are as follows:

2014	\$	2,500
2015		2,500
2016		2,500
2017		2,500
2018		2,500
Thereafter		15,000
		<hr/>
	\$	27,500

The Museum also has other lease agreements for portions of the Museum's land. The significant agreements are described in Note 10.

16. Commitment

The Museum entered into an agreement with Christopher Newport University (CNU) whereby CNU agreed to update its library to house a portion of the Museum's library collection. Under the terms of this agreement, the Museum agreed to reimburse CNU for a portion of the interest expense incurred to fund the library renovations. During 2013 and 2012, the Museum did not make any payments under this portion of the agreement. During 2009, the Museum also agreed to begin reimbursing CNU each month for a portion of the CNU Library Director's salary and benefits. Total reimbursements were \$39,901 and \$39,360 for 2013 and 2012, respectively.

During 2013, the Museum entered into a contract for theater upgrades. The total commitment is \$425,000 and, at December 31, 2013, \$235,250 has been expended under the contract. The remaining \$189,750 is expected to be paid in 2014.

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