Smithsonian Institution
Office of the Inspector General

Memo

Date: January 24, 2020

To: Audit and Review Committee, Board of Regents
Lonnie G. Bunch III, Secretary

Cc: Mike McCarthy, Acting Chief Operating Officer and Under Secretary for Finance and Administration
Martha Newton, Acting Director, Office of Finance and Accounting
Porter Wilkinson, Chief of Staff to the Board of Regents
Greg Bettwy, Chief of Staff, Office of the Secretary

From: Cathy L. Helm, Inspector General Cathy L. Helm

Subject: *Independent Auditor's Report on the Smithsonian Institution's Fiscal Year 2019 Financial Statements* (OIG-A-20-02)

This memorandum transmits the fiscal year 2019 financial statement audits of the Smithsonian Institution (Smithsonian) performed by the independent public accounting firm of KPMG LLP (KPMG). On January 24, 2020, KPMG issued its independent auditor's report on the statement of the Smithsonian Institution's financial position as of September 30, 2019, and the related statements of financial activity and cash flows. KPMG expressed an unmodified opinion that concluded the financial statements were presented fairly, in all material respects, in accordance with the applicable financial reporting standards.

As part of our oversight activities, we reviewed KPMG's audit documentation and interviewed its representatives. Our review of KPMG's fiscal year 2019 audit procedures disclosed no instances where KPMG did not comply, in all material respects, with the applicable auditing standards.

Our oversight of KPMG's audit was not intended to enable us to express, and we do not express, an opinion about the Smithsonian's financial statements, internal controls over financial reporting, or compliance with laws and regulations. KPMG is responsible for its audit report and the conclusions therein.

If you have any questions, please do not hesitate to contact me or Joan T. Mockeridge, Assistant Inspector General for Audits, at (202) 633-7050.

Attachment

KPMG

SMITHSONIAN INSTITUTION

Financial Statements

September 30, 2019

KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report

The Office of the Inspector General, Audit and Review Committee
of the Board of Regents, and Secretary Bunch
Smithsonian Institution:

We have audited the accompanying financial statements of Smithsonian Institution (Smithsonian), which comprise the statement of financial position as of September 30, 2019, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Smithsonian Institution as of September 30, 2019, and the changes in its net assets and its cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.

Emphasis of Matters

As discussed in Note 2(t) to the financial statements, in fiscal year 2019, Smithsonian Institution adopted Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, as amended, and ASU No. 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. Our opinion is not modified with respect to these matters.

Report on Summarized Comparative Information

We have previously audited Smithsonian's 2018 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated January 8, 2019. In our opinion, the summarized comparative information presented herein as of and for the year ended September 30, 2018 is consistent, in all material respects, with the audited financial statements from which it has been derived before the adjustments to adopt ASU 2016-14. As part of our audit of the 2019 financial statements, we also audited the adjustments described in Note 2(t) that were applied to adopt ASU 2016-14 retrospectively in the 2018 financial statements. In our opinion, such adjustments are appropriate and have been properly applied.

Other Matter

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplemental schedule of federal appropriated activities is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

KPMG LLP

Washington, District of Columbia
January 24, 2020

SMITHSONIAN INSTITUTION

Statement of Financial Position

September 30, 2019
(with summarized financial information as of September 30, 2018)
(Dollars in millions)

		2019	2018
Assets:			
Cash, cash equivalents, and U.S. Treasury balances	$	785.2	634.0
Accounts receivable and other assets, net		80.5	102.6
Pledges receivable, net		167.9	212.2
Investments		1,946.2	1,880.6
Property and equipment, net		2,440.9	2,347.1
Collections		—	—
Total assets	$	5,420.7	5,176.5
Liabilities:			
Accounts payable and accrued expenses	$	338.1	289.2
Deferred revenue		60.1	67.4
Unexpended federal appropriations		530.5	461.1
Environmental remediation obligation		61.4	49.8
Long-term debt		96.4	148.0
Total liabilities		1,086.5	1,015.5
Net assets:			
Without donor restriction:			
Board designated		717.4	707.7
Undesignated		1,881.8	1,883.3
Net assets without donor restriction		2,599.2	2,591.0
With donor restriction:			
Purpose and time restrictions		1,159.1	1,023.8
Endowments at historical cost		575.9	546.2
Net assets with donor restriction		1,735.0	1,570.0
Total net assets		4,334.2	4,161.0
Commitments and contingencies			
Total liabilities and net assets	$	5,420.7	5,176.5

See accompanying notes to financial statements.

SMITHSONIAN INSTITUTION

Statement of Financial Activities

Year ended September 30, 2019
(with summarized financial information for year ended September 30, 2018)

(Dollars in millions)

		Without Donor Restriction	With Donor Restriction	Total 2019	Total 2018
Operating:					
Support and revenue:					
Appropriations for salaries and expenses	$	734.2	—	734.2	733.8
Contributions and grants		126.0	145.7	271.7	272.3
Business activities		167.3	—	167.3	183.2
Endowment payout		40.4	35.5	75.9	76.5
Imputed benefit revenue		86.3	—	86.3	71.3
Short-term investment income and other revenue		39.8	0.5	40.3	36.5
Total operation revenues		1,194.0	181.7	1,375.7	1,373.6
Net assets released from restrictions		192.6	(192.6)	—	—
Total support and revenue		1,386.6	(10.9)	1,375.7	1,373.6
Expenses:					
Program activities:					
Research		350.7	—	350.7	342.4
Collections management		314.0	—	314.0	291.9
Education, public programs, and exhibitions		428.8	—	428.8	410.9
Business activities		127.8	—	127.8	141.7
Total program activities		1,221.3	—	1,221.3	1,186.9
Supporting activities:					
Administration		230.4	—	230.4	221.5
Development		68.2	—	68.2	70.3
Total supporting activities		298.6	—	298.6	291.8
Total expenses		1,519.9	—	1,519.9	1,478.7
Change in net assets from operating activities		(133.3)	(10.9)	(144.2)	(105.1)
Nonoperating activities:					
Appropriations for repair, restoration, and construction		—	239.1	239.1	136.6
Contributions for endowments		—	29.2	29.2	18.8
Contributions for construction		—	17.6	17.6	30.6
Investment return, net of endowment payout		10.6	26.1	36.7	93.3
Gain on sale of Smithsonian Network		9.9	—	9.9	12.4
Other, net		4.1	—	4.1	6.8
Collection items purchased, not capitalized		(12.4)	—	(12.4)	(16.4)
Net assets released from restrictions		136.1	(136.1)	—	—
Change in net assets from nonoperating activities		148.3	175.9	324.2	282.1
Increase in net assets		15.0	165.0	180.0	177.0
Net assets, beginning of year		2,591.0	1,570.0	4,161.0	3,984.0
Cumulative effect of accounting change		(6.8)	—	(6.8)	—
Net assets, end of year	$	2,599.2	1,735.0	4,334.2	4,161.0

See accompanying notes to financial statements.

SMITHSONIAN INSTITUTION

Statement of Cash Flows

Year ended September 30, 2019
(with summarized financial information for year ended September 30, 2018)

(Dollars in millions)

		2019	2018
Cash flows from operating activities:			
Change in net assets	$	180.0	177.0
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:			
Depreciation and amortization		176.8	162.1
Net investment gains		(105.4)	(155.2)
Gain on sale of Smithsonian Network		(9.9)	(12.4)
Present value discount and accretion		(0.5)	0.8
Gain/loss on disposition of assets		0.2	(0.2)
Collection items purchased		12.4	16.4
Appropriations for repair, restoration, and construction		(239.1)	(136.6)
Contributions for endowments		(29.2)	(18.8)
Contributions for construction		(17.6)	(7.1)
Decrease (increase) in assets:			
Accounts receivable and other assets, net		1.1	(2.3)
Pledges receivable, net		47.8	(14.1)
Increase (decrease) in liabilities:			
Accounts payable and accrued expenses		(6.4)	(10.7)
Deferred revenue		(7.3)	(3.8)
Unexpended federal appropriations		4.9	(3.8)
Net cash provided by (used in) operating activities		7.8	(8.7)
Cash flows from investing activities:			
Purchases of property and equipment		(204.9)	(164.7)
Purchases of investment securities		(557.7)	(586.3)
Proceeds from sales/maturities of investment securities		597.5	613.9
Proceeds from sale of Smithsonian Network		25.5	24.2
Collection items purchased		(12.4)	(16.4)
Proceeds from loan receivable		—	2.7
Net cash used in investing activities		(152.0)	(126.6)
Cash flows from financing activities:			
Appropriations for repair, restoration, and construction		303.6	312.5
Contributions for endowments		28.8	24.2
Contributions for construction		14.4	43.9
Principal payments on long-term debt		(51.4)	(51.5)
Net cash provided by financing activities		295.4	329.1
Net change in cash and cash equivalents		151.2	193.8
Cash, cash equivalents, and U.S. Treasury balances:			
Beginning of year		634.0	440.2
End of year	$	785.2	634.0
Noncash investing activities:			
Construction cost accruals	$	71.5	16.2
Cash paid for interest	$	2.9	4.2

See accompanying notes to financial statements.

(1) Organization

The Smithsonian Institution (Smithsonian) was created by an act of Congress in 1846 in accordance with the terms of the will of James Smithson of England, who, in 1826, bequeathed property to the United States of America "to found at Washington, under the name of the Smithsonian Institution, an establishment for the increase and diffusion of knowledge among men." Congress established the Smithsonian as a trust of the United States of America and vested responsibility for its administration in the Smithsonian Board of Regents (Board).

The Smithsonian is a museum and an education and research complex consisting of 17 museums and the National Zoological Park in Washington, DC, and two museums in New York City. Additional facilities and programs are operated in five states and Panama. Research is carried out at nine research centers, in the museums and other facilities throughout the world. During fiscal year 2019, 23.2 million individuals visited Smithsonian museums and other facilities.

As of September 30, 2019, the Smithsonian's extensive collection contained approximately 155.5 million objects: 0.4 million works of arts, 8.8 million historical artifacts, and 146.3 million natural and physical science specimens (living and nonliving). The Smithsonian also maintained 164,593 cubic feet and 0.7 million items of archival materials and 2.3 million library volumes. During fiscal year 2019, 123,301 collection items were acquired and 3,788 items were deaccessioned.

A substantial portion of the Smithsonian's operations is funded by annual federal appropriations. The Smithsonian also receives federal appropriations for the construction or repair and restoration of its facilities. Certain facilities have been constructed entirely by federal appropriations, while others have constructed with a combination of federal and private funds.

In addition to federal appropriations, the Smithsonian receives private support in the form of contributions, grants, and contracts, and also earns income from investments and various business activities. Business activities include Smithsonian magazines, other publications, online catalogs, and retail operations located in its museums and centers.

(2) Summary of Significant Accounting Policies

(a) General

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

These financial statements do not include the accounts of the National Gallery of Art, the John F. Kennedy Center for the Performing Arts, or the Woodrow Wilson International Center for Scholars, which were established by Congress within the Smithsonian, but are governed by independent boards of trustees and not controlled by the Smithsonian.

The Smithsonian receives annual federal appropriations to cover its core programs and renovation of its facilities as part of the budget approved annually by Congress and signed by the President. This is supplemented with income generated by business activities and endowment income designated for current operating expenditures as well as gifts and grants designated by donors for other specific expenditures. All monies, related activities, and balances from federal appropriations are referred to herein as “federal.” While all other monies, related activities, and balances are referred to as “trust.”

(b) Measure of Operations

The Smithsonian includes in its measure of operations federal and trust support and revenue and expenses that are integral to its core programs services: research; collections management; education, public programs, and exhibitions; and business activities. The measure of operations excludes certain nonoperating activities, including grants and contributions (federal capital appropriations, gifts for capital projects, and endowment gifts), investment return in excess of amounts designated for operations, collection proceeds and acquisitions, and other nonrecurring items.

The Board appropriates a portion of the Smithsonian’s cumulative investment return for support of current operations. The remainder is retained to support operations in future years and to offset potential market declines. The amount appropriated is computed under the Smithsonian’s spending policy and is appropriated for use based on the underlying donor-imposed restrictions (see notes 11, 12 and 13). The annual appropriation is referred to as the “endowment payout.”

(c) Summarized Financial Information

The financial statements include certain summarized prior-year information in total only. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. GAAP. Accordingly, such information should be read in conjunction with the Smithsonian’s financial statements as of and for the year ended September 30, 2018, from which the summarized information was derived, before the adjustments to adopt Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statements of Not-For-Profit Entities*.

(d) Net Assets

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

Without donor restrictions – Net assets without donor restrictions consist of the Smithsonian’s net investment in completed property and equipment less any unfunded liabilities and all other sources which are not subject to donor-imposed restrictions or other legal stipulations. At the discretion of the Smithsonian’s Board of Regents, trust funds which are not expended for operating activities may be set aside for designated purposes.

With donor restrictions – Net assets with donor restrictions carry specific donor-imposed stipulations on the use of the contributed funds, including federal appropriations received for specific capital projects. Donor-imposed restrictions may expire by the passage of time or as a result of fulfillment of the donor’s stipulations. Unconditional contributions restricted to the acquisition or construction of long-lived assets are recorded as non-operating revenue with donor restrictions in the period received. Donor restrictions are generally considered met and the net assets released from restriction when the related long-lived asset is placed in service.

Other net assets with donor restrictions include net assets with stipulations that require the corpus of the gift be maintained with only the income to be used to support operations or other specified purpose.

(e) Cash, Cash Equivalents and U.S. Treasury Balances

Cash, cash equivalents, and U.S. Treasury balances include interest-bearing demand deposits and appropriated amounts yet to be disbursed remaining on deposit with the U.S. Department of Treasury (U.S. Treasury). The Smithsonian considers all highly liquid investments with an original maturity of three months or less at the date of purchase to be cash equivalents, except where such cash is held as part of a long-term investment strategy (see note 6).

U.S. Treasury balances of $645.3 at September 30, 2019 consist of appropriated funds that are available to pay current liabilities and finance authorized purchase commitments of the Smithsonian. U.S. Treasury balances are carried forward until such time as goods or services are received and payments made, or until the funds are returned to the U.S. Treasury.

(f) Contracts with Customers and Accounts Receivable

Business activities, including advertising, subscriptions, licensing, and other revenues are generally recognized as the services are provided over the period of performance. Revenues from magazines and long-term contracts are deferred and recognized ratably over the period of the underlying agreement. Concessions and retail sales are recognized when goods or services are sold at a point in time.

Customer receivables are invoiced based upon contractual terms. The Smithsonian maintains allowances for doubtful accounts to reflect management’s best estimate of probable losses inherent in receivable balances. Management determines the allowances for doubtful accounts based on known troubled accounts, historical experience, and other currently available evidence.

(g) Contributions, including Government Grants and Contracts, and Pledges Receivable

Contributions, including unconditional promises to give, are recognized as revenue in the period received. Unconditional promises to give are recognized initially at fair value giving consideration to anticipated future cash receipts and discounting such amounts at a risk-adjusted rate. Amortization of the discount is included in contributions revenue. Conditional promises to give are not recognized until they become unconditional, that is, when the barriers on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value.

Allowance is made, if necessary, for uncollectible contributions receivable based upon management’s judgment and analysis of the creditworthiness of the donors, past collection experience, and other relevant factors.

The Smithsonian conducts sponsored program activity with various sponsors, including agencies and departments of the federal government, local government entities, and foundations. Such grants and contracts revenue are recognized as the related qualifying expenses are incurred.

(h) Investments and Trusts Held by Others

Smithsonian employs an investment strategy that is designed to achieve returns that support Smithsonian's mission and fulfill its fiduciary responsibility to its donors and constituents.

Investments are generally reported at fair value. Publicly traded fixed income, global equities, natural resources and cash and cash equivalents, including gift annuity program investments are reported and valued using readily determinable market prices. Nearly all of the valuations reported by marketable alternative investments and public equities held in commingled funds rely upon third party administrators to objectively value positions and calculate net asset value (NAV) as a practical expedient. Investments in private equity structured funds (private equity, venture capital, real estate, natural resources) (collectively, nonmarketable investments) are valued at estimated fair value based on the funds' net asset values or their equivalents, as a practical expedient, unless it is probable that all or a portion of the investment will be sold for an amount different from NAV. As of September 30, 2019, the Smithsonian had no plans or intentions to sell investments at amounts different from NAV. These estimated fair values may differ from the values that would have been used had a ready market existed for these investments, and the differences could be significant.

Purchases and sales of investments are reflected on the trade-date basis using average historical cost. Dividend and interest income is recorded when earned on an accrual basis. In accordance with the policy of stating investments at fair value, the net change in unrealized appreciation or depreciation for the year is reflected in the statement of activities (see note 6).

The Smithsonian is also party to various split interest agreements with donors consisting primarily of irrevocable charitable remainder trusts and gift annuities.

Charitable remainder trusts held by others – Assets are reflected in pledges receivable and other assets with contribution revenues recognized at the date the trust is established based on the net present value of the estimated future payments to be made to the donors and/or other beneficiaries. Income distributions from these trusts are recorded as investment income and changes in the fair value of these trusts are recorded as unrealized gains or losses in the statement of activities.

Charitable gift annuities – Assets are included in investments and recognized at fair value at the date of the annuity agreement. An annuity liability is also recognized for the present value of future cash flows expected to be paid to the donor. Contribution revenue recognized is equal to the difference between the assets and the annuity liability. The annuity liabilities are adjusted during the term of the annuity for payments to donors, accretion of discounts, and changes in the life expectancies of the donors.

(i) Property and Equipment

Certain land occupied by Smithsonian buildings, located primarily in the District of Columbia, Maryland, and Virginia, were appropriated and reserved by Congress for the Smithsonian's use. The Smithsonian serves as trustee of the land for as long as they are used to carry out its mission. The land are titled in the name of the U.S. government and no value has been assigned in the accompanying financial statements.

Property and equipment purchased with federal or trust funds are recorded at cost. Property and equipment acquired through transfers from government agencies are recorded at net book value or fair value at the date of transfer, whichever is more readily determinable. Property and equipment acquired through donation are recorded at estimated fair value at the date of the gift.

Property and equipment assets are depreciated on a straight-line basis over their estimated useful lives as follows:

Buildings	30 years
Major renovations	15 years
Equipment and software	3 – 7 years
Exhibit costs	10 years

Leasehold improvements are amortized over the shorter of the lease term or their useful lives.

Rent expense under operating leases that provide for scheduled rent increases over their terms is recognized on a straight-line basis.

(j) Collections – Stewardship Assets

The Smithsonian acquires its collections by purchase or by donation. Collections are held for public exhibition, education, or research. The Smithsonian’s collections management policy includes guidance on the preservation, care, and maintenance of the collections and procedures relating to the accession/deaccession of collection items.

In conformity with the practice generally followed by museums, no value is assigned to the collections in the statement of financial position. Purchases of collection items are recognized as reductions in the appropriate net asset class in the period of acquisition. Proceeds from deaccessions or insurance recoveries for lost or destroyed collection items are recognized as increases in net assets without donor restrictions and designated for future collection acquisitions.

Noncash deaccessions of collection items result from the exchange, donation, or destruction due to deterioration, a lack of mission relation, or duplicate other objects. During the fiscal year, noncash deaccessions included works of art, animals, historical objects, and natural specimens.

Items that are acquired with the intent to sell, exchange, or otherwise be used for financial gain are not considered collection items and are recorded as other assets at their fair value at the date of acquisition. Contributed items held for sale, amounting to $0.9, are included in other assets.

(k) Federal Appropriations and Funds

Federal appropriations are provided by the U.S. Federal Government to support the general operations of the Smithsonian and the construction, repair and restoration of its facilities. Funds are to be spent in accordance with applicable law and revenue is recognized ratably over the fiscal year as the qualifying expenses are incurred and funds are expended. Unexpended appropriation balances are classified as a liability on the statement of financial position.

Federal appropriations for general operations are recognized as operating revenue without donor restrictions, as qualifying expenses are incurred, and generally available for two years. The portion of these appropriations which are not obligated or expended are retained by the Smithsonian in accordance with federal guidelines and returned to the U.S. Department of Treasury five years after the expiration of the obligation period. During the fiscal year, $0.9 related to the fiscal 2013 appropriation was returned.

Amounts appropriated for construction or repair and restoration of facilities are recognized as non-operating revenues with donor restrictions as capital is expended and generally available for obligation until expended. Such amounts remain purpose restricted until the capital project is completed and placed in service, at which time the net assets are released from restrictions.

Net assets of federal funds without donor restrictions consist primarily of cash held at U.S. Treasury and net investment in property and equipment acquired or constructed with federal funds less unfunded liabilities for environmental remediation obligations, annual leave, and estimated Federal Employees Compensation Act liabilities for workers compensation claims. Net assets of federal funds with donor restrictions consist of U.S. Treasury cash balances and construction in progress.

(l) Annual Leave

Annual leave is accrued as it is earned by employees and is included in personnel compensation and benefit costs. The liability for unused annual leave totaling $45.9 as of September 30, 2019 is included in accounts payable and accrued expenses.

(m) Employee Benefit Plans

The Smithsonian offers its employees a comprehensive set of benefits including pension, health and life insurance, and workers compensation for injuries sustained on the job. The Smithsonian's current year contributions to the retirement, health, and life insurance plans described below are recognized in the statement of activities.

Federal funded pension, health and life insurance benefits, including imputed benefits:

Federal employees hired subsequent to January 1, 1984, participate in the Federal Employees' Retirement System (FERS). Federal employees hired prior to January 1, 1984, had the option of remaining under the Civil Service Retirement System (CSRS) or electing FERS. The terms of both these plans are defined in federal regulations. Under both systems, a specified percentage is withheld from each federal employee's salary. The Smithsonian also contributes specified percentages of employees' salaries. Additional costs associated with these plans are borne by the U.S. government. The Smithsonian recognizes its share of these additional costs as imputed benefits revenue and expense in the financial statements. Imputed benefits totaled $86.3 in fiscal 2019. Smithsonian's direct expense for these plans amounted to $40.8 for fiscal 2019.

(Continued)

The Smithsonian's current year contributions to the pension plans are recognized in the statement of activities using rates established by the Office of Personnel Management (OPM), the agency with U.S. government-wide responsibility for the oversight and administration of the plans. Consistent with reporting under multi-employer pension plans, the Smithsonian does not report CFRS and FERS assets, accumulated plan benefits, or future liabilities, if any, applicable to its covered employees. This data is reported for plan participants by OPM.

Federal employees covered by CSRS or FERS are eligible to contribute to the Thrift Savings Plan (TSP), a defined contribution plan similar to a 401(k). The TSP is administered by the Federal Retirement Thrift Investment Board, an independent agency of the U.S. government. For FERS-covered employees, the Smithsonian is required to match contributions of specified percentages of base pay. No matching contributions are made for CSRS-covered employees.

Most federal employees are also eligible to participate in the Federal Employees Group Life Insurance (FEGLI) Program. Participating employees can obtain basic term life insurance, with the employee paying two-thirds of the cost and the Smithsonian paying one-third. Additional coverage is optional, to be paid fully by the employee. The basic life coverage may be continued into retirement if certain requirements are met. OPM administers this program and is responsible for the reporting of liabilities.

Most federal employees are eligible to enroll in the Federal Employees Health Benefit (FEHB) Program, which provides post-retirement health benefits if certain conditions are met. OPM administers this plan and Smithsonian is not obligated under this plan.

<u>Trust funded pension, health and life insurance benefits:</u>

Substantially all trust fund employees are eligible to participate in defined contribution retirement plan under which the Smithsonian contributes specified percentages of employees' salaries. Such contributions are used to purchase individual annuities, the rights to which are immediately vested with the employees. Employees may also make voluntary contributions, subject to certain limitations. The Smithsonian's expense for this plan was $21.0 for fiscal 2019.

In addition to the retirement plans, certain health care and life insurance benefits are made available to active and retired trust fund employees. The plan is contributory for retirees and requires payment of premiums and deductibles. Retiree contributions for premiums are established by an insurance carrier based on the average per capita cost of benefit coverage for all participants. At September 30, 2019, the accrued benefit obligation under this plan was $16.1 and is included in accounts payable and accrued expenses in the statement of financial position.

<u>Workers compensation;</u>

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

FECA expense is recognized based on amounts invoiced or expected to be invoiced by DOL and changes in the actuarially determined value of expected future benefits. The actuarially determined FECA liability represents the liability for expected future benefits for death, disability, medical, and miscellaneous costs for approved cases. The actuarial liability is determined by DOL and evaluated by Smithsonian management annually, as of September 30, using a method utilizing historical benefit patterns related to specific incurred period, wage inflation factors, medical inflation factors and other variables. This liability constitutes an extended future estimate of cost which will not be obligated against budgetary resources until the fiscal year in which DOL bills the cost to the Smithsonian. The payment associated with this liability cannot be met by the Smithsonian without continued annual federal appropriation.

(n) Contributed Services and Donated Assets

Volunteers make significant contributions of time to the Smithsonian, enhancing its activities and programs. During fiscal 2019, about 6,900 volunteers contributed around 508,700 hours of service and another 13,600 digital volunteers transcribed about 91,300 pages during fiscal year 2019. The services provided do not meet the criteria for recognition of contributed services, and accordingly, are not reflected in the statement of financial activities.

Donated assets, other than donations of cash or collection items, are recorded at estimated fair value at the date of gift.

In kind contributions such as donated space, equipment, services, and various other items totaled $11.6 in fiscal year 2019 and recognized as program support revenues (within other revenues) and program activity expenses in the statement of activities.

(o) Functional Allocation of Expenses

The cost of providing various programs and other activities summarized on a functional and natural basis is shown in note 16.

- Included in research are personnel, travel, and other costs associated with the Smithsonian's world-wide research programs.
- Collections management includes the care, storage, transportation, digitization, and other costs.
- Education, public programs and exhibits includes the cost of providing a wide array of programing and outreach to academia and the general public as well as costs to display, manage, and transport exhibits.
- Business activities includes the cost of goods sold and related expenses.
- General and administrative expenses include costs for executive management, financial administration, human resources, and legal services.
- Development expenses include those costs associated with individual and corporate gifts and grants, annual appeals and other fund-raising efforts.

Costs that benefit more than one program, such as security, facilities, and depreciation, are allocated across programs based on relative square footage, or direct costs as a percentage of total costs, before allocations.

(p) Related Organizations

The Smithsonian recognizes its interest in the net assets of organizations that are financially interrelated and the changes in its interest as other non-operating activities. Such organizations included the Smithsonian Network and Friends of the National Zoo. During fiscal year 2019, the Smithsonian sold its remaining interest in the Smithsonian Network recognizing a nonoperating gain of $9.9.

(q) Income Taxes

The Smithsonian is a tax-exempt organization as described in Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the Code). As such, the Smithsonian is generally exempt from Federal income taxes to the extent provided under Section 501 of the Code, except for unrelated business income, principally advertising sales.

The Tax Cuts and Jobs Act (the Act) was enacted in December 2017. Among other things, the Act imposes new taxes and establishes new rules for calculating unrelated business taxable income. The Smithsonian has reflected an estimate in its statements for unrelated trade or business income tax using the current proposed regulatory guidance and will continue to evaluate the impact of the Act on current and future tax positions.

The Smithsonian accounts for uncertain tax positions, when applicable. The tax years that remain subject to examination by the major tax jurisdictions under the statute are from the year 2015 and forward.

(r) Use of Estimates

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

(s) Risks and Uncertainties

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

(t) Recently Adopted Accounting Pronouncements

Not-for-Profit Financial Statement Presentation

During 2019 the Smithsonian retroactively adopted ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements for Not-for-Profit Entities*. ASU 2016-14 reduces the number of net asset categories to two: net assets without donor restrictions, previously reported as unrestricted net assets, and net assets with donor restrictions, previously reported as temporarily restricted net assets and permanently restricted net assets. The ASU also requires that net assets with donor restrictions associated with capital projects (including capital appropriations) be released upon placing the related capital asset into service. Previously the Smithsonian accounted for its federal capital appropriations as unrestricted. Accordingly, the Smithsonian reclassified $251.2 of net assets from previously reported unrestricted net assets to net assets with donor restrictions as of the beginning of fiscal 2019. The guidance also requires enhanced disclosures for board designated amounts, composition of net assets without donor restrictions (note 11), liquidity (note 3), and the presentation of expenses by both their natural and functional classification (note 16).

Revenue Recognition

In May 2014, FASB ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606),* which, along with related amendments, replaces existing revenue recognition requirements. The core principle of Topic 606 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration it expects to be entitled in exchange. In addition, Topic 606 requires disclosures about the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers.

In June 2018, FASB issued ASU No. 2018-08, *Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made*. The FASB issued this ASU to reduce diversity in reporting by clarifying (1) whether transactions should be accounted for as contributions or as exchange transactions subject to other guidance and (2) whether a contribution is conditional.

The Smithsonian implemented ASU 2014-09, as amended, and ASU 2018-08 (Standards) effective October 1, 2018, on a modified retrospective basis. As a result of the application of the new standards, the Smithsonian elected to combine government grants and contracts with contributions on its statement of financial activities in fiscal year 2019 and conformed fiscal year 2018 presentation. Other revenue reclassifications required by the Standards were not significant.

The Standards also require that costs associated with the preparation of long-lived materials, such as catalogs and campaigns to secure new subscribers be expensed at the date such materials are first issued. Previously, the Smithsonian amortized such costs over the estimated useful life of such items. This resulted in a cumulative effect adjustment to reduce beginning net assets without donor restrictions by $6.8.

(Dollars in millions)

Summary impact

The following summarizes the impact on beginning net assets of adopting ASU 2016-14 and the Standards.

	As Previously Presented	Without Donor Restriction	With Donor Restriction	Total
Net assets:				
Unrestricted	$ 2,842.2	$ 2,842.2	—	2,842.2
Temporarily restricted	772.6	—	772.6	772.6
Permanently restricted	546.2	—	546.2	546.2
Total net assets	$ 4,161.0	2,842.2	1,318.8	4,161.0
Federal capital appropriations, ASU 2018-08		(251.2)	251.2	—
Net assets as of September 30, 2018 under ASU 2016-14		2,591.0	1,570.0	4,161.0
Cumulative effect of Topic 606		(6.8)	—	(6.8)
Net assets as of October 1, 2018, as presented		$ 2,584.2	1,570.0	4,154.2

(u) *Recent Accounting Pronouncements*

In February 2016, the Financial Accounting Standards Board (FASB) issued ASU No. 2016-02, *Leases* (Topic 842). ASU 2016-02 requires the recognition of right-of-use assets and lease liabilities by lessees for those leases classified as operating leases under the Accounting Standards Codification (ASC) Topic 840 – Leases. The accounting applied by the lessor under ASU 2016-02 is largely unchanged from that applied under ASC Topic 840. ASU 2016-02 is effective for the Smithsonian in fiscal year 2020.

In March 2019, the FASB issued ASU No. 2019-03, *Updating the Definition of Collections, Not-For-Profit Entities* (Topic 958). This ASU modifies the term “Collections” which in turn may change collection recognition policies and add certain disclosure requirements. ASU 2019-03 is effective for the Smithsonian in fiscal year 2021.

(3) Financial Assets and Liquidity Resources

Federal appropriations provide a significant funding for the Smithsonian’s various programs and general operating costs, in addition to capital support for the repair, renovation and construction of its facilities. At the date of appropriation, an equal amount of cash is deposited and held by the U.S. Treasury on Smithsonian’s behalf until expended. As of September 30, 2019, the U.S. Treasury held cash of $645.3 which represents the balance of the operating and capital appropriations not yet expended.

(Dollars in millions)

Private donor gifts and grants, government grants and contracts, and other revenue sources, such as business activities and rentals, provide funding for non-appropriated program and operating activities as well as for the repair, renovation, and construction of facilities not funded through appropriation.

To meet immediate and longer term cash needs, the Smithsonian has a working capital investment policy. The policy requires excess funds be invested in short term, high quality instruments allowing for required liquidity and providing a maximum return within defined risk constraints. As of September 30, 2019, the working capital investment fund totals $260.3 and is comprised of cash equivalents of $50.5 and short-term investments of $209.8.

The Smithsonian also has available a $50.0 line of credit available to provide additional resources if necessary. Borrowings under the line bear annual interest at LIBOR (London Interbank Offered Rate) Daily Floating Rate plus 0.55%. Beginning in fiscal year 2020, an annual availability fee of 0.04% on the unused balance is required. The line is due to expire October 31, 2020.

The following reconciles total financial assets at September 30, 2019 to financial assets available to meet cash needs for general expenditures (operating expenses, capital, and debt service) with one year.

	Trust	Federal	Total
Financial assets:			
Cash, cash equivalents, and U.S. Treasury balances	$ 139.9	645.3	785.2
Accounts receivable and other assets	77.3	3.2	80.5
Pledges receivable, net	167.9	—	167.9
Investments	1,946.2	—	1,946.2
Total financial assets at year end	2,331.3	648.5	2,979.8
Plus endowment payout appropriated for fiscal year 2020	69.6	—	69.6
Less financial assets unavailable for general expenditures within one year:			
Endowment investments	(1,713.2)	—	(1,713.2)
Pledges due beyond one year	(59.7)	—	(59.7)
Charitable remainder trusts	(17.9)	—	(17.9)
Gift annuity assets	(23.2)	—	(23.2)
Inventory	(13.1)	—	(13.1)
Deferred expenses	(8.6)	—	(8.6)
Other assets	(18.1)	—	(18.1)
	$ 547.1	648.5	1,195.6

(Dollars in millions)

Quasi endowment assets include funds without donor restrictions designated by the Board to function as endowment funds supporting the Smithsonian's programs and operations, including the directors of certain museums and centers and various operating costs. Although the Smithsonian does not intend to spend from its board designated endowment funds, other than amounts appropriated, these funds could be made available, if necessary (see note 12).

(4) Accounts Receivable and Other Assets

Accounts receivable and other assets consist of the following:

Grants and contracts	$	20.6
Trade accounts, net of $0.3 allowance		18.0
Inventory		13.1
Deferred expenses		8.6
Accrued interest and dividend receivable		2.1
Other assets		18.1
Total receivables and other assets	$	80.5

(5) Pledges Receivable

Pledges receivable consist of the following:

Due within:		
Less than 1 year	$	90.3
1 to 5 years		66.9
5 years or beyond		0.3
		157.5
Less:		
Allowance for uncollectible contributions		(3.4)
Unamortized discount (at rates ranging from 1.1% to 2.9%)		(4.1)
Contributions receivable, net		150.0
Charitable remainder trust		17.9
Pledges receivable, net	$	167.9

(6) Investments and Fair Value Measurements

Investments are comprised of the following:

Endowment investments, including Board designated funds	$	1,713.2
Working capital short-term investments		209.8
Charitable gift annuity investments		23.2
Total investments	$	1,946.2

The three levels of the fair value hierarchy for recurring fair value measurements are prioritized based on the inputs to valuation techniques used to measure fair value and are as follows:

- Level 1 – Quoted or published prices in active markets for identical assets or liabilities, as of the reporting date.
- Level 2 – Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

(Dollars in millions)

The following summarizes Smithsonian's investments at fair value which are determined primarily based on quoted market prices as of September 30, 2019:

	Total	Level 1	Level 3	NAV [1]
Endowment investments:				
Global equities:				
Global markets	$ 313.7	54.8	—	258.9
Emerging markets	114.4	2.9	—	111.5
Marketable alternatives	273.9	—	—	273.9
Private equity:				
Private equity	159.1	—	—	159.1
Venture capital	420.7	2.9	—	417.8
Real assets:				
Energy and natural resources	110.8	9.8	—	101.0
Real estate funds	134.8	—	—	134.8
Fixed income	82.7	53.9	—	28.8
Cash and equivalents	102.1	102.1	—	—
Pooled investments	1,712.2	226.4	—	1,485.8
U.S. Treasury deposits	1.0	1.0	—	—
Total endowment	1,713.2	227.4	—	1,485.8
Fixed income (working capital fund)	209.8	209.8	—	—
Gift annuities, primarily equities	23.2	23.2	—	—
Total investments	1,946.2	460.4	—	1,485.8
Charitable trusts	17.9	—	17.9	—
	$ 1,964.1	460.4	17.9	1,485.8

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

The following table summarizes the changes in Level 3 assets, Charitable trusts held by other, measured at fair value on a recurring basis:

Fair value of Level 3 assets, beginning of the year	$ 19.3
Unrealized losses	(1.1)
Proceeds from distributions	(0.3)
Fair value of Level 3 assets, end of the year	$ 17.9

(Dollars in millions)

The following summarizes information relating to the investments, which are stated at NAV as practical expedient for fair value and includes information about the nature, strategies, and risks of these major classes of nonmarketable investments:

		NAV	Unfunded Commitments	Redemption terms	Days of notices
Global equity:	(a)				
Developed markets		$ 258.9	-	Weekly to annually	6 - 91
Emerging markets		111.5	2.0	Monthly to semi-annually	14 - 90
Marketable alternatives:	(b)	273.9	39.9	Monthly to at maturity	30 - N/A
Private equity:	(c)				
Private equity		159.1	85.2	N/A	N/A
Venture capital		417.8	76.5	N/A	N/A
Real assets:	(d)				
Energy and natural resources		101.0	36.6	N/A	N/A
Real estate funds		134.8	108.9	Quarterly to at maturity	60 - N/A
Fixed income	(e)	28.8	-	Quarterly to at maturity	90 - N/A
		$ 1,485.8	349.1		

(a) Global equity is comprised of investments in funds and strategies invested in publicly listed equity securities in the global developed and emerging markets. Some of the funds are subject to lock-ups.

(b) Marketable alternatives consist of investments in a broad array of securities and strategies aimed to reduce volatility and enhance returns. Smithsonian's marketable alternatives managers may follow certain investment strategies including, but not limited to, such as long/short equity, credit and distressed, multi-strategy, and global macro funds. Some of the funds are subject to soft and hard lock-ups and other funds are not eligible for redemption.

(c) Private equity consists of limited partnerships that are organized to invest primarily in shares of operating companies that are not listed on a publicly traded stock exchange. Private equity strategies include investments in leveraged buyouts, growth capital and distressed investments. Venture capital strategies invest in start-ups and small businesses with perceived long-term growth potential. Distributions to limited partners are made as soon as feasible and, in accordance with the limited partnership agreement, when realizations (sales of portfolio companies) are made, or when interest payments, dividends, or recapitalizations are generated.

(d) Real assets include real estate and energy and natural resources investments that are made mostly in private limited partnerships as well as publicly traded securities funds. Distributions to limited partners are made as soon as feasible and, in accordance with the limited partnership agreement, when realizations (sales of portfolio companies) are made, or when interest payments, dividends, or recapitalizations are generated.

(Dollars in millions)

(e) Fixed income includes funds that invest in U.S. government, agency and municipal bonds, and other interest bearing products.

The Smithsonian is obligated under the terms of certain limited partnership agreements to remit additional funding periodically as capital calls are exercised. As of September 30, 2019, the Smithsonian had uncalled commitments totaling approximately $349.1. Such commitments are callable over the fund investment period, generally the first five years of the funds. The standard life of Smithsonian's investments in these private partnerships are between 8 and 10 years with possible one to two one-year extension periods and/or other termination clauses.

The following summarizes the investment return, net of expenses, and its classification in the statement of activities:

Dividend and interest, net of expenses	$	15.1
Net realized and unrealized gains		105.4
Total investment return		120.5
Endowment payout appropriated for operations		(75.9)
Short term investment income		(7.9)
Nonoperating investment return	$	36.7

(7) Property and Equipment

Property and equipment consists of the following:

Land	$	12.6
Construction in progress		414.1
Buildings and capital improvements		3,906.1
Equipment and software		442.0
Leasehold improvements		143.4
		4,918.2
Accumulated depreciation		(2,477.3)
Total property and equipment	$	2,440.9
Depreciation expense	$	166.2

(Dollars in millions)

(8) Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consists of the following:

		Trust	Federal	Total
Accounts payable	$	31.8	101.7	133.5
Accrued salaries		12.4	18.7	31.1
Accrued annual leave		15.6	30.3	45.9
Workers' compensation (FECA)		2.7	43.7	46.4
Post retirement benefits		16.1	—	16.1
Other accrued personnel benefits		0.3	6.7	7.0
Deferred rent		14.3	—	14.3
Charitable gift annuity liabilities		13.4	—	13.4
Other accrued liabilities		17.0	13.4	30.4
Total accounts payable and accrued expenses	$	123.6	214.5	338.1

Accrued federal accrued annual leave, FECA, and other accrued liabilities are unfunded and cannot be met by the Smithsonian without continued annual federal appropriation.

(9) Environmental Remediation Obligations

The Smithsonian has an unfunded environmental remediation obligation that is estimated based on third party studies, contractor bids and internal estimates derived from recently completed remediation projects for similar facilities and other information for similar projects. The present value of the obligation is calculated using an inflation rate of 1.9% and a discount rate of 2.3%. Each period the obligation is accreted to its present value. Because the related properties are fully depreciated, changes in the estimated obligation are expensed. Any difference between the estimated obligation and the actual cost of remediation is also expensed.

Fiscal year 2019 activity in the unfunded environmental remediation obligation follows:

Balance, beginning of the year	$	49.8
Accretion		1.0
Change in estimate		10.6
Balance, end of the year	$	61.4

(Dollars in millions)

(10) Long-term Debt

The Smithsonian's long-term debt are unsecured obligations and funded solely through trust funds without donor restrictions. Long-term debt is comprised of the following:

Series 2010 Revenue Bonds, serial, principal amounts ranging from $1.6 to $1.7, interest rates 5.00% to 5.25%, due February 1, 2020 through 2021	$	3.3
Series 2010 Revenue Bonds, term, principal amounts ranging from $1.8 to $2.4, interest rate 5.25%, due February 1, 2022 through 2028		14.7
Series 2003 Revenue Bonds, variable interest rate, due December 1, 2033:		
Series A		52.5
Series B		25.0
		95.5
Plus unamortized bond premium		0.9
Total long-term debt	$	96.4

Series 2010 Revenue Bonds

The tax-exempt Series 2010 Revenue Bonds were issued by the District of Columbia on behalf of the Smithsonian to finance capital and other projects. Interest is payable semiannually on August 1 and February 1.

The serial bonds mature annually through February 1, 2021, with principal repayments ranging from $1.6 to $1.7 per year. The term bonds maturing on February 1, 2028 are subject to mandatory redemption by sinking fund installments, which begin on February 1, 2022 and range from $1.8 to $2.4 per year through the maturity date.

Series 2003 Revenue Bonds

The tax-exempt Series 2003 Revenue Bonds were issued by the Fairfax County Economic Development Authority (Virginia) on behalf of the Smithsonian to finance a portion of the Steven F. Udvar-Hazy Center, an extension of the National Air and Space Museum. The bonds are subject to early redemption at the option of the Smithsonian. Interest is payable monthly at a variable interest rate determined in accordance with the Indenture. Interest rates for Series A and Series B were 1.5%, at September 30, 2019.

The bonds are supported by a standby bond purchase agreement for both the Series A and Series B (collectively, the 2003 Liquidity Facility) with Wells Fargo (Trustee) and Northern Trust Company (Liquidity Facility provider). The 2003 Liquidity Facility provides liquidity support when the bonds are bearing interest at a daily or weekly rate and expires September 8, 2020.

On October 25, 2018, the Smithsonian redeemed the remaining of its outstanding Series 2013 Taxable Bonds, Series A for $50.8, including accrued interest of $0.3.

Interest expense was $2.6 in fiscal year 2019.

(Dollars in millions)

Future annual maturities of long-term debt are as follows:

2020	$	1.6
2021		1.7
2022		1.8
2023		1.9
2024		2.0
Thereafter		86.5
	$	95.5

(11) Net Assets

Net assets consist of the following:

		Without Donor Restrictions	With Donor Restrictions	Total
Endowment investment fund	$	—	1,002.2	1,002.2
Board designated quasi endowment funds		717.4	—	717.4
Total net assets subject to payout spending policy		717.4	1,002.2	1,719.6
Net assets with donor restrictions available for:				
Programs and operations		—	191.9	191.9
Capital repairs, renovation, and construction		—	114.2	114.2
Endowment contributions receivable and other		—	28.9	28.9
Net investment in property and equipment		1,954.6	389.9	2,344.5
Unfunded federal liabilities		(148.8)	—	(148.8)
Undesignated, including time restrictions		76.0	7.9	83.9
	$	2,599.2	1,735.0	4,334.2

Donor restricted endowment funds include accumulated appreciation of $416.0. Future-funded federal liabilities include environmental remediation obligations and accrued annual leave, workers compensation, and litigation liabilities.

(Dollars in millions)

Net assets with donor restrictions are available for the following purposes:

		Endowments at historical cost	Subject to purpose restriction and time	Total
Museums and general support	$	146.1	219.2	365.3
Education, public programs and exhibitions		276.6	231.4	508.0
Research		93.9	114.0	207.9
Acquisitions and collections		57.7	88.6	146.3
Facilities and capital		1.6	505.9	507.5
	$	575.9	1,159.1	1,735.0

(12) Endowment Funds

The Smithsonian endowment consists of over 660 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the Board to function as endowments supporting the Smithsonian's programs and operations. Net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law

Management has resolved to be guided by the standards of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) in the management, investment, and expenditure of endowment funds although it is not required to do so as a matter of law. Management has interpreted UPMIFA, as allowing the Smithsonian to appropriate for expenditure or accumulate so much of an endowment fund as it determines to be prudent for the uses, purposes, and durations for which the endowment fund is established, subject to the intent of the donor as expressed in the gift instrument. Unless otherwise stated in the gift instrument, the assets in an endowment fund shall be donor-restricted assets until appropriated for expenditure. The corpus of the Smithsonian's endowment funds consist of (a) the original vale of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) changes to the permanent endowment made in accordance with the direction of the donor gift instrument. Earnings and accumulated appreciation of the endowment fund remain restricted until appropriated for expenditure in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA the following factors are considered when making a determination to appropriate or accumulate donor-restricted funds:

- Duration and preservation of the fund
- Purpose of board designated or donor-restricted fund
- General economic conditions

- Possible impact of inflation and deflation
- Expected return from income and appreciation of investments
- Other available resources
- The Smithsonian's investment policies

The Smithsonian has adopted investment and spending policies for endowment assets that are intended to provide a predictable stream of funding for programs and operations while maintaining the purchasing power of the endowment. Under the investment policy, as approved by the Board, endowment assets are invested in a manner that reduces risk through diversification while obtaining a competitive rate of return. To satisfy its long-term rate-of-return, the Smithsonian relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends), targeting a diversified asset allocation that utilizes fixed income and equity-based investments to achieve its long-term objectives within prudent risk constraints. The Board's Investment Committee reviews the long-term asset allocation for the investment pool.

Substantially all of the assets of individual endowment funds are pooled and invested. Individual funds buying or disposing of units on the basis of the per unit market value at the beginning of the month in which the transaction takes place. Each fund participating in the investment pool receives an annual appropriation based on the number of units owned. The Smithsonian's spending policy is based on an annual endowment spending rate of 5% of the prior five years' average endowment value This spending rate constitutes the Board's annual appropriation for spending endowment earnings to support programs and operations. The Board authorized an additional allocation of up to 0.75% for eligible funds to support the fund-raising campaign.

The following summarizes certain per endowment unit information, in whole dollars.

Market value of fund per unit:		
Beginning of the year	$	974.68
End of the year	$	996.12
Payout per unit		
Program and operations support	$	42.53
Development	$	4.53

(Dollars in millions)

The following table summarizes the change in endowment funds during fiscal year 2019:

		Without donor restrictions	With donor restrictions		Total
Endowment net assets at beginning of the year	$	707.7	937.6		1,645.3
Additional designation of quasi endowment funds*		1.7	5.4		7.1
Contributions received		—	29.2		29.2
Investment return		48.4	65.5		113.9
Appropriation of endowment assts for expenditure		(40.4)	(35.5)		(75.9)
Endowment net assets at end of year	$	717.4	1,002.2		1,719.6
Uninvested cash and receivables					(6.4)
Endowment investments (Note 6)				$	1,713.2

** Includes transfers to quasi endowments with donor restrictions*

Endowment funds with deficiencies

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level required to be maintained in perpetuity or the applicable donor gift document, creating an “underwater” endowment fund. Such deficiencies are generally the result of unfavorable market fluctuations and continuing the appropriations for various programs is generally deemed prudent by the Board. At September 30, 2019 there are no significant underwater endowment funds.

(Dollars in millions)

(13) Net Assets Released From Restriction

Net assets are released from donor restrictions due to the passage of time, assets placed in service, or by incurring expenses satisfying the restricted purpose specified by the donors were as follows for fiscal 2019:

Operating releases:		
Purpose restricted gifts released for:		
Museums and general support	$	34.3
Education, public programs and exhibitions		72.3
Research		48.7
Acquisitions and collections		10.7
Facilities		26.6
Total operating releases		192.6
Non-operating releases:		
Assets placed in service and released from:		
Capital appropriation		100.2
Capital contributons		35.9
Total nonoperating releases		136.1
Total releases	$	328.7

(14) Federal Appropriations

A substantial portion of the Smithsonian is funded primarily by two Congressional appropriations: one appropriation covers salaries, benefits and expenses and the second appropriation provides funding for the repair, restoration, and construction of Smithsonian properties. The appropriation for salaries, benefits, and expenses is a two year appropriation that must be obligated by the end of the second fiscal year. The appropriation for repair, restoration, and construction is available until expended.

(Dollars in millions)

The federal appropriation received in fiscal year 2019 is reconciled to federal appropriation revenue recognized as follows:

		Salaries and expenses	Repair, restoration, and construction	Total
Federal appropriations received	$	740.0	303.5	1,043.5
Unexpended appropriations		(96.3)	(278.1)	(374.4)
Amounts expended from prior years' appropriations		90.5	213.7	304.2
Federal appropriation revenue	$	734.2	239.1	973.3
Without donor restrictions (operating)	$	734.2	—	734.2
With donor restrictions (nonoperating)		—	239.1	239.1
Federal appropriation revenue	$	734.2	239.1	973.3

(15) Business Activities

The following summarizes business activities for fiscal year 2019.

		Revenues	Operating expenses	Net operating gain
Smithsonian Enterprises	$	147.5	114.8	32.7
Unit activities		19.8	13.0	6.8
	$	167.3	127.8	39.5

Revenue is further detailed as follows for fiscal year 2019.

Merchandise sales	$	60.1
Media		38.6
Concessions, licensing, and other		68.6
	$	167.3

(Dollars in millions)

(16) Functional Classification of Expenses

Expenses by functional and natural classification are shown below for the year ended September 30, 2019:

		Program Activities				Supporting Activities		
		Research	Collections management	Education, public programs and exhibitions	Business activities	General and administrative	Development	Total
Compensation	$	195.6	168.4	211.1	57.8	132.1	36.4	801.4
Occupancy		120.6	80.2	143.4	18.8	63.6	27.5	454.1
Cost of sales		—	—	0.4	58.7	0.1	1.6	60.8
Travel and transportation		9.2	2.5	7.5	0.5	1.1	1.8	22.6
Depreciation and amortization		20.2	61.3	64.0	1.8	29.2	0.3	176.8
Other		5.1	1.6	2.4	(9.8)	4.3	0.6	4.2
Total operating expenses	$	350.7	314.0	428.8	127.8	230.4	68.2	1,519.9

Collections items purchased, not capitalized included in nonoperating activities are collections management activities.

(17) Commitments and Contingencies

(a) Leasing Activities

The Smithsonian leases office and warehouse space under long-term operating leases expiring at various dates to 2032. These leases generally provide for rent escalations based on increases in the Consumer Price Index or changes in property taxes or operating expenses attributable to the leased properties. The Smithsonian currently limits leases using federal funds to five years under the five-year contracting authority of the Federal Acquisition Streamlining Act. The Smithsonian still has legacy leases exceeding the current five-year authority.

Annual minimum lease payments due under operating leases in effect as of September 30, 2019 are as follows:

2020	$	50.2
2021		35.5
2022		24.0
2023		22.9
2024		13.4
Thereafter		23.9
	$	169.9

Rent expense under operating leases, including executory costs such as maintenance, insurance, and taxes, totaled $62.3 for fiscal year 2019, which includes $7.6 in office space received in-kind.

(b) Government Awards

The Smithsonian receives significant amounts of federal funding in the form of appropriations, grants, and contracts. These awards are subject to audit by federal agencies. Management is of the opinion that no material disallowances of costs or expenses are likely.

(c) Construction

As of September 30, 2019, the Smithsonian has commitments approximating $420.7 related to construction in process at a number of its locations. The most significant of these relate to projects at the National Air and Space Museum ($301.4) and the National Zoological Park ($18.3).

(d) Litigation

The Smithsonian is a party to various litigation arising out of the normal conduct of its operations. In the opinion of the Smithsonian's general counsel, the ultimate resolution of these matters will not have a significant effect on the Smithsonian's financial position or future results of operations.

(e) Subsequent Events

Subsequent to September 30, 2019, the Smithsonian committed capital of $11.1 to 5 funds. Management has evaluated subsequent events from September 30, 2019 through January 24, 2020, which is the date that the financial statements are available to be issued and determined that there are no adjustments to or other items to disclose.

SMITHSONIAN INSTITUTION

Supplemental Schedule

September 30, 2019

SMITHSONIAN INSTITUTION

Federal Appropriated Activities

(Dollars in millions)

Statement of Financial Position		**September 30, 2019**
Assets:		
Cash and cash equivalents	$	645.3
Accounts receivable and other assets		3.2
Property and equipment, net		1,710.3
Total assets		2,358.8
Less liabilities:		
Accounts payable and accrued liabilities		(214.5)
Unexpended federal appropriations		(530.5)
Environmental remediation obligation		(61.4)
Total liabilities		(806.4)
Net assets		1,552.4

Statement of Financial Activities		**Fiscal Year 2019**
Support and revenue:		
Federal appropriations	$	734.2
Imputed benefits revenue		86.3
Other		10.6
Total operating revenue		831.1
Expenses:		
Research		190.2
Collections management		280.0
Education, public programs, and exhibitions		305.7
Total program actvities		775.9
Administration		190.1
Development		1.1
Total operating expenses		967.1
Change in net assets from operating activities		(136.0)
Nonoperating activities:		
Federal capital appropriations		239.1
Collection items purchased, not capitalized		(3.5)
Other, net		(0.2)
Change in net assets from nonoperating activities		235.4
Increase in net assets		99.4
Net assets at beginning of year		1,453.0
Net assets at end of year	$	1,552.4