

VIRGINIA HISTORICAL SOCIETY

Financial Statements

December 31, 2008 and 2007

VIRGINIA HISTORICAL SOCIETY

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REPORT OF INDEPENDENT ACCOUNTANTS

Board of Trustees
Virginia Historical Society:

We have audited the accompanying statements of financial position of the Virginia Historical Society (the "Society") as of December 31, 2008 and 2007, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Society's management. 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. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Virginia Historical Society as of December 31, 2008 and 2007, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

As discussed in Note 1 to the financial statements, in 2008 the Society adopted FASB Staff Position 117-1, *Endowments for Non-profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures of All Endowment Funds*, and Statement of Financial Accounting Standard Number 157, *Fair Value Measurements*.

Keiter, Stephens, Hurst, Gary & Shreaves, P.C.

May 15, 2009

VIRGINIA HISTORICAL SOCIETY

Statements of Financial Position December 31, 2008 and 2007

<u>Assets</u>	<u>2008</u>	<u>2007</u>
Current assets:		
Cash and cash equivalents	\$ 4,724,397	\$ 8,675,973
Accrued interest and dividends	85,548	101,180
Contributions receivable, current (Note 3)	1,871,149	1,423,615
Grants receivable	280,293	396,645
Other current assets	<u>360,520</u>	<u>297,269</u>
Total current assets	7,321,907	10,894,682
Investments (Note 2)	38,008,060	58,337,514
Contributions receivable (Note 3)	3,135,134	3,367,931
Beneficial interest in a trust	331,906	416,516
Bond issuance costs, net	446,979	474,296
Property and equipment, net (Note 5)	<u>25,976,942</u>	<u>26,974,914</u>
Total assets	<u>\$ 75,220,928</u>	<u>\$ 100,465,853</u>
<u>Liabilities and Net Assets</u>		
Current liabilities:		
Accounts payable	\$ 188,644	\$ 252,099
Accrued expenses and other liabilities	607,316	668,297
Current portion of bonds payable (Note 6)	425,000	725,000
Deferred revenue (Note 10)	<u>169,839</u>	<u>211,683</u>
Total current liabilities	1,390,799	1,857,079
Interest rate swap liability	735,448	203,665
Bonds payable, less current portion (Note 6)	<u>8,865,000</u>	<u>15,490,000</u>
Total liabilities	<u>10,991,247</u>	<u>17,550,744</u>
Net assets:		
Unrestricted	21,440,209	40,839,966
Temporarily restricted (Note 14)	13,651,144	12,835,218
Permanently restricted (Note 15)	<u>29,138,328</u>	<u>29,239,925</u>
Total net assets	<u>64,229,681</u>	<u>82,915,109</u>
Total liabilities and net assets	<u>\$ 75,220,928</u>	<u>\$ 100,465,853</u>

See accompanying notes to financial statements.

VIRGINIA HISTORICAL SOCIETY

Statements of Activities Year Ended December 31, 2008, with Comparative Totals for 2007

	2008				2007
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
Support and revenue (loss):					
Membership dues	\$ 240,290	\$ -	\$ -	\$ 240,290	\$ 234,291
Annual giving	1,100,490	-	-	1,100,490	1,100,095
Investment (loss) return (Note 2)	(9,075,967)	(6,892,170)	-	(15,968,137)	7,340,036
Contributions	342,890	1,681,109	804,028	2,828,027	893,018
Grants	42,860	1,963,197	-	2,006,057	1,656,651
Publications and merchandise sales	381,084	-	-	381,084	377,052
Royalties	2,275	-	-	2,275	2,822
Rental income (Note 10)	288,580	-	-	288,580	282,420
Fees and admissions	201,607	15,174	-	216,781	236,033
Other	1,612	-	-	1,612	3,068
Net assets released from restriction	<u>8,442,211</u>	<u>(8,442,211)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total support and revenue (loss)	<u>1,967,932</u>	<u>(11,674,901)</u>	<u>804,028</u>	<u>(8,902,941)</u>	<u>12,125,486</u>
Expenditures:					
Program services:					
Library	2,409,365	-	-	2,409,365	2,397,937
Publications/education	1,837,480	-	-	1,837,480	1,605,950
Museums/exhibits	2,374,120	-	-	2,374,120	3,212,367
Supporting services:					
General administration	1,576,202	-	-	1,576,202	1,550,924
Fund raising/public relations	<u>1,053,537</u>	<u>-</u>	<u>-</u>	<u>1,053,537</u>	<u>1,353,680</u>
Total expenditures	9,250,704	-	-	9,250,704	10,120,858
Fair value change of interest rate swaps	<u>(531,783)</u>	<u>-</u>	<u>-</u>	<u>(531,783)</u>	<u>(304,047)</u>
Change in net assets	(7,814,555)	(11,674,901)	804,028	(18,685,428)	1,700,581
Net assets, beginning of year, previously stated	40,839,966	12,835,218	29,239,925	82,915,109	81,214,528
Change in accounting principle	<u>(11,585,202)</u>	<u>12,490,827</u>	<u>(905,625)</u>	<u>-</u>	<u>-</u>
Net assets, beginning of year, restated	<u>29,254,764</u>	<u>25,326,045</u>	<u>28,334,300</u>	<u>82,915,109</u>	<u>81,214,528</u>
Net assets, end of year	<u>\$ 21,440,209</u>	<u>\$ 13,651,144</u>	<u>\$ 29,138,328</u>	<u>\$ 64,229,681</u>	<u>\$ 82,915,109</u>

See accompanying notes to financial statements.

VIRGINIA HISTORICAL SOCIETY

Statement of Activities, Continued Year Ended December 31, 2007

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Support and revenue:				
Membership dues	\$ 234,291	\$ -	\$ -	\$ 234,291
Annual giving	1,100,095	-	-	1,100,095
Investment return (Note 2)	6,981,097	358,939	-	7,340,036
Contributions	164,595	600,183	128,240	893,018
Grants	338,556	1,318,095	-	1,656,651
Publications and merchandise sales	377,052	-	-	377,052
Royalties	2,822	-	-	2,822
Rental income (Note 10)	282,420	-	-	282,420
Fees and admissions	225,578	10,455	-	236,033
Other	3,068	-	-	3,068
Net assets released from restriction	2,669,127	(2,669,127)	-	-
Total support and revenue	12,378,701	(381,455)	128,240	12,125,486
Expenditures:				
Program services:				
Library	2,397,937	-	-	2,397,937
Publications/education	1,605,950	-	-	1,605,950
Museums/exhibits	3,212,367	-	-	3,212,367
Supporting services:				
General administration	1,550,924	-	-	1,550,924
Fund raising/public relations	1,353,680	-	-	1,353,680
Total expenditures	10,120,858	-	-	10,120,858
Fair value change of interest rate swaps	(304,047)	-	-	(304,047)
Change in net assets	1,953,796	(381,455)	128,240	1,700,581
Net assets, beginning of year	38,886,170	13,216,673	29,111,685	81,214,528
Net assets, end of year	\$ 40,839,966	\$ 12,835,218	\$ 29,239,925	\$ 82,915,109

See accompanying notes to financial statements.

VIRGINIA HISTORICAL SOCIETY

Statements of Cash Flows Years Ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Cash flows from operating activities:		
Change in net assets	\$ (18,685,428)	\$ 1,700,581
Adjustments to reconcile change in net assets to net cash from operating activities:		
Depreciation and amortization	1,029,873	1,141,492
Permanently restricted contributions, including changes in present value of contributions receivable	(804,028)	(128,240)
Net realized and unrealized loss (gain) on investments	16,968,171	(5,982,940)
Fair value change of interest rate swaps	531,783	304,047
Change in assets and liabilities:		
Accrued interest and dividends	15,632	15,563
Contributions and grants receivable	(98,385)	4,429,045
Other current assets	(63,251)	111,967
Accounts payable	(63,455)	140,411
Deferred revenue	(41,844)	38,293
Accrued expenses and other liabilities	(60,981)	(29,739)
Net cash (used in) provided by operating activities	<u>(1,271,913)</u>	<u>1,740,480</u>
Cash flows from investing activities:		
Purchase of property and equipment	(16,838)	(195,561)
Purchase of investments	(22,452,434)	(16,472,888)
Proceeds from sale of investments	25,910,581	19,820,986
Net cash provided by investing activities	<u>3,441,309</u>	<u>3,152,537</u>
Cash flow from financing activities:		
Payment on 2004/2006 bond series	(6,925,000)	(270,000)
Permanently restricted contributions, including changes in present value of contributions receivable	804,028	128,240
Net cash used in financing activities	<u>(6,120,972)</u>	<u>(141,760)</u>
 (Decrease) increase in cash	 (3,951,576)	 4,751,257
Cash and cash equivalents, beginning of year	<u>8,675,973</u>	<u>3,924,716</u>
Cash and cash equivalents, end of year	<u>\$ 4,724,397</u>	<u>\$ 8,675,973</u>
 Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	<u>\$ 495,734</u>	<u>\$ 638,189</u>

See accompanying notes to financial statements.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements

1. Summary of Significant Accounting Policies:

Organization: The Virginia Historical Society (the "Society") was founded in 1831 and chartered in 1834. The purpose of the Society is to collect, preserve, and interpret Virginia's past for the education and enjoyment of present and future generations. The Society currently serves the entire Commonwealth of Virginia through its museum and library, as well as through a variety of educational programs.

Basis of Accounting: The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States ("GAAP").

Basis of Presentation: Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Society and changes therein are classified and reported as follows:

Unrestricted funds include funds that impose no restrictions on the Society as to their use or purpose. Such funds are expended for charitable purposes as deemed appropriate by the Board of Trustees and for operating purposes.

Temporarily restricted net assets are subject to donor-imposed stipulations that will be met either by actions of the Society and/or the passage of time. These net assets represent contributions and other income, which must be spent for the purpose designated by the donors. Expirations of temporary restrictions on net assets (i.e., donor-stipulated purpose has been fulfilled and/or stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets. Temporary restrictions on contributions to acquire long-lived assets are considered met in the period in which the assets are acquired or placed into service.

Permanently restricted net assets are subject to donor-imposed stipulations that require the principal be invested and the income be used either for a designated purpose or for general operations of the Society. Generally, the donors of these assets permit the Society to use all of, or part of, the income earned on related investments for general or specific purposes.

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Gains and losses in the present value of contributions receivable are included as contributions revenue or loss. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as net assets released from restrictions.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

1. Summary of Significant Accounting Policies, Continued:

Cash and Cash Equivalents: For purposes of the statements of cash flows, the Society considers all highly liquid securities not included in the investment portfolio that were purchased with a maturity of three months or less to be cash equivalents.

Credit Risk: Financial instruments that potentially subject the Society to concentrations of credit risk consist principally of cash and cash equivalents. The Society maintains its cash and cash equivalents in a financial institution with balances that periodically exceed federally insured limits.

Contributions and Grants Receivable: Contributions are recorded as receivables and contributions revenue in the year made. Contributions received for support of future operations and museum acquisitions are recorded as increases to temporarily restricted net assets. Contributions receivable are solicited from entities and individuals primarily throughout Virginia.

Investments and Investment Income: The Society accounts for long-term investments at fair value. Certain less marketable securities are generally carried at values determined by the respective investment managers. Investments are exposed to various risks, such as interest rate, market, and credit. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in the risks in the near term could materially affect amounts reported on the financial statements.

Bond Issuance Costs: Bond issuance costs are amortized over the period the obligation is outstanding using the straight-line method, which approximates the interest method.

Property and Equipment: Property and equipment are stated at cost, less accumulated depreciation. Major repairs and betterments are capitalized and normal maintenance and repairs are charged to expense as incurred. Depreciation is computed by the straight-line method over the estimated useful lives of the related assets, ranging from 3 to 40 years. Upon retirement or sale of an asset, the cost and accumulated depreciation are removed from the accounts and any gain or loss is reflected in operations.

Collection Objects: In conformity with the practice followed by most museums, the Society's financial statements exclude the value of the collection objects and library holdings, and no determination has been made as to the aggregate value of such items. Purchases of collection items are recorded as decreases in unrestricted net assets or temporarily restricted net assets if the assets used to purchase collection items are restricted by the donor. See Note 4 for a description of the collection objects and library holdings.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

1. Summary of Significant Accounting Policies, Continued:

Deferred Revenue: Deferred revenue consists of advance payments related to rental income and state appropriations.

Functional Allocation of Expenses: The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Income Taxes: The Society received a favorable determination letter from the Internal Revenue Service dated May 16, 1961, stating that it is exempt from income taxes under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3).

Contributed Services: The Society receives services from volunteers for support of the Society's activities. The value of these services is not clearly measurable and is not recorded in the financial statements.

Use of Estimates: Management of the Society has made a number of estimates and assumptions relating to the reporting of assets, liabilities, revenues and expense and disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting principles generally accepted in the United States. Actual results could differ from those estimates.

Adoption of New Accounting Principles: During 2008, the Society adopted FASB Staff Position 117-1, *Endowments of Non-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures of All Endowment Funds* ("FSP"). The Society adopted the FSP on January 1, 2008, and it resulted in a reclassification of approximately \$905,625 from permanently restricted net assets to temporarily restricted net assets, and \$11,585,202 from unrestricted net assets to temporarily restricted net assets. Additionally, the FSP requires expanded disclosures for all endowment funds (see Note 8). The Society also adopted for 2008 certain provisions of Statement of Financial Accounting Standard No. 157, *Fair Value Measurements* ("SFAS 157"), related to disclosures for financial assets and liabilities and any other assets and liabilities that are carried at fair value on a recurring basis in the financial statements (see Note 9).

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

1. Summary of Significant Accounting Policies, Continued:

Pending Accounting Pronouncement: In June 2006, the Financial Account Standards Board issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* ("FIN 48"), an interpretation of FASB Statement No. 109. This interpretation clarifies the accounting for uncertainty in income taxes and details how entities should recognize, measure, present and disclose uncertain tax positions that have been or are expected to be taken. As such, financial statements will reflect or disclose expected future tax consequences of uncertain tax positions presuming the taxing authorities' full knowledge of the position and relevant facts. The Society has elected to defer the adoption of FIN 48 until its fiscal year ending December 31, 2009, pending additional clarification on FIN 48's applicability to not-for-profit entities such as the Society. In instances where the Society has taken or expects to take a tax position in its tax returns and the Society believes that it is more than likely than not that such tax position will be upheld by the relevant tax authorities, the Society has not disclosed such tax position in the financial statements. Management has evaluated the impact of FIN 48 and does not expect it to have a material impact on the Society's financial condition, change in net assets or income tax disclosure practices.

Reclassifications: Certain prior year balances have been reclassified to conform with the current year presentation.

2. Investments:

Investments at December 31, 2008 and 2007 are comprised of the following:

	2008		2007	
	Market	Cost	Market	Cost
Cash equivalents	\$ 975,586	\$ 975,586	\$ 827,481	\$ 825,663
U. S. government obligations	3,012,720	2,892,695	3,492,313	3,464,152
Marketable equity securities	2,409,358	2,778,411	6,546,305	5,236,127
Mutual funds	24,832,846	29,833,512	41,319,740	31,196,978
Real estate funds	2,581,735	2,581,735	1,276,480	1,276,480
Corporate obligations	4,195,815	4,533,863	4,875,195	4,918,185
	<u>\$ 38,008,060</u>	<u>\$ 43,595,802</u>	<u>\$ 58,337,514</u>	<u>\$ 46,917,585</u>

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

2. Investments, Continued:

Investment return for 2008 and 2007 is as follows:

	2008	2007
Interest and dividends	\$ 1,000,034	\$ 1,357,096
Unrealized gains, net	(17,007,673)	3,636,531
Realized gains, net	39,502	2,346,409
Total	\$ (15,968,137)	\$ 7,340,036

3. Contributions Receivable:

As of December 31, 2008 and 2007, contributors to the Society have made unconditional written and oral promises to give that relate to the following purposes:

	2008	2007
Unrestricted - split interest agreements	\$ 533,669	\$ 962,392
Temporarily restricted:		
New wing	2,026,525	2,784,126
Exhibitions	196,938	270,406
Education	440,219	282,062
Split interest agreements	1,369,667	458,588
Total temporarily restricted	4,033,349	3,795,182
Permanently restricted	439,265	33,972
Total contributions receivable	\$ 5,006,283	\$ 4,791,546

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

3. Contributions Receivable, Continued:

The Society projects that contributors will remit these contributions as follows:

	2008	2007
Year ending December 31:		
Less than one year	\$ 1,871,149	\$ 1,423,615
One year to five years	1,336,051	1,966,218
Thereafter	2,071,914	3,009,086
Gross contributions receivable	5,279,114	6,398,919
Less discount to present value, discount rate 1.186% for 2008 and ranging from 5.15% to 7.2% in 2007	272,831	1,607,373
	\$ 5,006,283	\$ 4,791,546

At December 31, 2008, the Society had received conditional promises to give and indications of intention to give of approximately \$13,980,000. In accordance with accounting principles generally accepted in the United States these conditional promises to give are not recorded in these financial statements. These potential contributions consist primarily of bequests and charitable remainder trusts. If received, approximately \$9,820,000 would be included as permanently restricted net assets, approximately \$635,000 would be included as temporarily restricted net assets, and approximately \$3,525,000 would be included as unrestricted net assets.

4. Collections:

The Society collects manuscripts, books, maps, newspapers, photographs, portraits, and other works of art, as well as museum artifacts that are related to Virginia and American history. The Society's collections are maintained for research, education, and public exhibition in furtherance of public service rather than for financial gain. Collections are the most valuable assets of the Society and are protected, kept unencumbered, cared for, and preserved. As steward for many treasures relating to the state's and the nation's history, the Society maintains meticulous records and is nationally noted for the depth and detail of its descriptive cataloging for its library holdings.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

4. Collections, Continued:

Intellectual as well as physical control of all collections is maintained by an extensive paper trail including provenance of origin; accession date; terms of gift or purchase price, whichever is applicable; physical description and condition report; location; and conservation record. To more efficiently manage its extensive record keeping, the Society is embarking upon an automation project, which will convert its records to a computer format.

In conformity with the American Association of Museum guidelines, collections are deaccessioned rarely and in close adherence to specific steps, culminating in approval from either the Society's director or board of trustees. Proceeds derived from the sale of any deaccessioned collections are applied to resources restricted to the purchase of library or museum collections.

The Society does not include either the cost or the value of its collections in the statements of financial position, nor does it recognize gifts of collection items as revenues in the statements of activities. Because items acquired for collections by purchase are not capitalized, the cost of those acquisitions is reported as a decrease in net assets in the statement of activities.

5. Property and Equipment:

A summary of property and equipment at December 31, 2008 and 2007 is as follows:

	<u>2008</u>	<u>2007</u>
Land	\$ 436,301	\$ 436,301
Buildings and improvements	29,336,374	29,336,191
Equipment and furnishings	<u>8,042,522</u>	<u>8,025,867</u>
Total	37,815,197	37,798,359
Less accumulated depreciation	<u>11,838,255</u>	<u>10,823,445</u>
Property and equipment, net	<u>\$ 25,976,942</u>	<u>\$ 26,974,914</u>

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

6. Bonds Payable:

In 1996, the Society issued \$8,045,000 of Museum Facilities Revenues Refunding Bonds, Series 1996 ("Series 1996"), issued by the Industrial Development Authority of the City of Richmond, Virginia to refund all outstanding Museum Facilities Revenue Bonds, Series 1990 ("Series 1990") bonds which were issued to finance certain costs of renovating, expanding, and equipping Battle Abbey, the principal facility of the Society. Upon the issuance of the Series 1996 bonds, the Series 1990 bonds were in-substance defeased but remained outstanding, secured exclusively by escrowed U.S. Treasury securities and not by any obligation of the Society.

The Series 1996 bonds were defeased in 2006, by issuance of the Series 2006 bonds.

Series 2006

In 2006, the Society entered into an agreement with SunTrust Capital Markets and the Virginia Small Business Financing Authority to issue \$6,625,000 of Variable Rate Revenue Refunding Bonds, Series 2006 ("Series 2006"). The bonds are secured by an irrevocable 10-year Letter of Credit Facility which is scheduled to expire on August 1, 2016. The bonds were issued to defease the remaining 1996 bonds outstanding as of September 2006.

The Society entered into a forward interest rate swap agreement in March 2005, which included a declining notional amount (originally \$6,615,000). Under this swap agreement expiring September 2019, the Society pays SunTrust a fixed rate of 3.529% and SunTrust pays the Society the variable interest rate of 67% of the 1 month LIBOR. The change in the fair value of the interest rate swap is recognized as a yield adjustment. For the years ended December 31, 2008 and 2007, \$478,968 and \$159,296, respectively, are included for the loss in the fair value of the interest rate swap in the accompanying statements of activities. At December 31, 2008 and 2007, \$673,900 and \$194,932, respectively, are included in interest rate swap liability in the accompanying statements of financial position to reflect the fair value of the interest rate swap.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

6. Bonds Payable, Continued:

The amortization schedule for the Series 2006, with total outstanding of \$5,900,000, is as follows:

<u>Year</u>	<u>Principal</u>
2009	\$ 425,000
2010	445,000
2011	465,000
2012	485,000
2013	510,000
2014	535,000
2015	555,000
2016	580,000
2017	605,000
2018	635,000
2019	660,000

Total interest expense for the Series 2006 bonds was \$166,996 for 2008 and \$279,797 for 2007.

Series 2004

In 2004, the Society entered into an agreement with SunTrust Capital Markets and the Industrial Development Authority of the City of Richmond, Virginia to issue \$14,165,000 of Variable Rate Revenue Bonds, Series 2004 ("Series 2004"). The bonds are secured by an irrevocable 10-year Letter of Credit Facility which is scheduled to expire on July 15, 2014. The bonds were issued for the construction of a new wing at Battle Abbey, the Society's principal facility. The Society entered into a loan agreement with the Industrial Development Authority of the City of Richmond, Virginia whereby the Society became obligated under the above described Series 2004 Bonds. The trust indenture places further restrictions on future borrowings and the disposition of certain assets.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

6. Bonds Payable, Continued:

The final bond maturity is on July 1, 2034 with the first principal payment due on July 1, 2006 and the final principal payment on July 1, 2034. The amortization schedule for the 2004 series, with total outstanding of \$3,390,000, is as follows:

<u>Year</u>	<u>Principal</u>
2030	\$ 450,000
2031	695,000
2032	720,000
2033	750,000
2034	775,000

Total interest expense for the Series 2004 Bonds was \$207,249 for 2008 and \$421,872 for 2007.

The Society entered into a variable-to-fixed interest rate swap transaction on August 2, 2004. The Society's interest rate swap agreement includes a notional amount of \$3,390,000 that effectively converted a portion of the Society's variable rate financing instrument to a fixed rate. Under this swap agreement, expiring in 2010, the Society pays SunTrust a fixed interest rate of 2.69% and SunTrust pays the Society a variable interest rate equal to 67% of the 1-month LIBOR. The change in the fair value of the interest rate swap is recognized as a yield adjustment of the hedged debt obligation in the same period in which the related interest affects earnings. For the years ended December 31, 2008 and 2007, \$52,815 and \$144,751, respectively, are included for the loss in the fair value of the interest rate swap in the accompanying statements of activities. At December 31, 2008 and 2007, \$61,548 and \$8,733, respectively, is included in interest rate swap liability in the accompanying statement of financial position to reflect the fair value of the interest rate swap.

7. Line of Credit:

As of December 31, 2008 and 2007, the Society has a line of credit with a bank with a maximum available amount of \$1,000,000. The line carries interest at the 30-day LIBOR rate plus 75 basis points (1.19% at December 31, 2008). There were no amounts outstanding under the line of credit as of December 31, 2008 and 2007, nor were there any draw-downs during 2008 and 2007. Any borrowings under the line of credit are secured by the Society's cash accounts at the bank.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

8. Endowment Funds:

There are 53 endowment funds at the Society. These endowment funds were established for a variety of purposes. The endowment funds include both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law: The Board of Trustees of the Society has interpreted the State Prudent Management of Institutional Funds Act ("SPMIFA") as requiring the preservation of the fair value of the original gift of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Society 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. The remaining portion of the donor restricted endowment funds that are not classified as permanently restricted net assets are classified as temporarily restricted net assets until those amounts appropriated for expenditure are disbursed in accordance with the donor restrictions in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, the Society considers the following factors in making a determination to appropriate or accumulate funds in the endowment funds designated by the Board of Trustees:

- The duration and preservation of the fund
- The purposes of the organization and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the organization
- The investment policies of the organization

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

8. Endowment Funds, Continued:

Funds with Deficits: From time to time, the fair value of assets associated with individual endowment funds may fall below the level that the donor or the SPIMFA requires the Society to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$7,890,373 as of December 31, 2008. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that was deemed prudent by the Board of Trustees.

Return Objectives and Risk Parameters: The Society has adopted investment and spending policies for endowment funds that attempt to provide a predictable stream of funding to programs supported by its endowment, while seeking to maintain the purchasing power of the endowment assets. Endowment assets include assets of donor-restricted funds that the organization must hold in perpetuity or for a donor-specified period(s) as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the S&P 500 index while assuming a moderate level of investment risk. The Society expects its endowment funds over time to provide an average rate of return of approximately 9 percent annually. Actual returns in any given year may vary from this amount.

Strategies Employed for Achieving Objectives: To satisfy its long-term rate-of-return objectives, the Society 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). The Society targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy: The Society annually targets for distribution six percent of its endowment funds' fair market average over the 36 month period immediately preceding the fiscal year in which the distribution is intended. In establishing this policy, the Society considered the long-term expected return on its endowment and expects over the long term, that this spending policy will allow its endowment to increase at an average annual rate of 3 percent. This policy is consistent with the objectives of maintaining the purchasing power of the endowment assets held either in perpetuity or for a specific term, which also should experience additional real growth through gifts, bequests and other new capital infusions.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

8. Endowment Funds, Continued:

Endowment net asset composition by type of fund was as follows as of December 31, 2008:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ (7,890,373)	\$ 4,871,446	\$ 29,138,328	\$ 26,119,401
Board-designated funds	<u>319,021</u>	<u>-</u>	<u>-</u>	<u>319,021</u>
Total funds	<u>\$ (7,571,352)</u>	<u>\$ 4,871,446</u>	<u>\$ 29,138,328</u>	<u>\$ 26,438,422</u>

Changes in endowment net assets were as follows for the year ended December 31, 2008:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Net assets, beginning of year	<u>\$ 435,927</u>	<u>\$ 11,879,127</u>	<u>\$ 28,334,300</u>	<u>\$ 40,649,354</u>
Investment loss	(8,007,279)	(4,218,929)	-	(12,226,208)
New gifts	-	-	804,028	804,028
Appropriation of endowment assets for expenditure	<u>-</u>	<u>(2,788,752)</u>	<u>-</u>	<u>(2,788,752)</u>
Net assets (deficit), end of year	<u>\$ (7,571,352)</u>	<u>\$ 4,871,446</u>	<u>\$ 29,138,328</u>	<u>\$ 26,438,422</u>

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

9. Fair Value Measurements:

The Society adopted for 2008 certain provisions of Statement of Financial Accounting Standard No. 157, *Fair Value Measurements* ("SFAS 157"), related to financial assets and liabilities and any other assets and liabilities that are carried at fair value on a recurring basis in the financial statements. The provisions of SFAS 157 related to nonrecurring fair value measurements of nonfinancial assets and nonfinancial liabilities, has been deferred to 2009. SFAS 157 provides a framework for measuring fair value under GAAP and defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. SFAS 157 requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs. SFAS 157 also establishes a fair value hierarchy which prioritizes the valuation inputs into three broad levels. Based on the underlying inputs, each fair value measurement in its entirety is reported in one of three levels:

Level 1 – Unadjusted quoted prices that are available in active markets for the identical assets or liabilities at the measurement date.

Level 2 – Other observable inputs available at the measurement date, other than quoted prices included in Level 1, either directly or indirectly, including:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets in non-active markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by other observable market data.

Level 3 – Unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

9. Fair Value Measurements, Continued:

Assets and liabilities measured at fair value on a recurring basis at December 31, 2008, include the following:

	Fair Value Using			Asset/Liabilities at Fair Value
	Level 1	Level 2	Level 3	
Assets:				
Contributions receivable, net	\$ -	\$ 5,006,283	\$ -	\$ 5,006,283
Investments	20,537,779	14,888,546	-	35,426,325
Beneficial interest	331,906	-	-	331,906
Total assets	<u>\$ 20,869,685</u>	<u>\$ 19,894,829</u>	<u>\$ -</u>	<u>\$ 40,764,514</u>
Liabilities:				
Interest rate swap	\$ -	\$ 735,448	\$ -	\$ 735,448
Annuity obligations	-	353,789	-	353,789
Total liabilities	<u>\$ -</u>	<u>\$ 1,089,237</u>	<u>\$ -</u>	<u>\$ 1,089,237</u>

10. Rental Income:

During 1996, the Society agreed to the terms of an operating lease covering certain space with the Department of Historic Resources of the Commonwealth of Virginia. The commencement date of the lease was March 1, 1998. Rent is to be paid annually on July 1 for the lease term of 20 years. Thus, deferred revenue equal to six months of the annual payment will be recorded on the statement of financial position at each December 31. Annual payments will escalate at a rate of 50% of the previous year's increase in the Consumer Price Index. Rental income was \$288,580 for 2008 and \$282,420 for 2007.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

11. Defined Contribution 401(k) Retirement Plan:

The Society began a 401(k) retirement plan in 1997. Under the plan, employees who have attained the age of 21 and have six months of service may elect to contribute up to 100% of their compensation to the Plan. An employee's contribution is also limited by Internal Revenue Service regulations. The Society matches 100% of an employee's contribution, up to 6% of compensation. Employees are vested in employer contributions as follows:

<u>Years of service</u>	<u>Vesting percentage</u>
1	33%
2	66%
3 or more	100%

Employees are allowed to borrow from their accounts subject to the provisions of the plan document. The total expense for the Plan was \$187,842 for 2008 and \$153,079 for 2007.

12. Executive Retirement Plan – 457(f):

The Society began a 457(f) Nonqualified Executive Retirement Plan (the "Plan") effective December 1, 2003. Under the Plan, administrative staff and other highly compensated employees may participate upon approval of the Board-designated Administrative Committee, which has discretionary authority to make determinations as to eligibility and benefits under the Plan. There is no cap on participant deferrals. The participants' accrued benefits shall be fully vested providing they remain in continuous service with the Society until they leave under a qualifying event. If participants terminate under a nonqualifying event they forfeit all accrued benefits. The Society matches 100% of an employee's contributions up to 6% of compensation. Employees are vested in employer contributions as follows:

<u>Years of service</u>	<u>Vesting percentage</u>
1	33%
2	66%
3 or more	100%

On July 31, 2007 the Plan was frozen and contributions were discontinued for all participants. The accounts in the Plan were distributed to the participants and the Plan was terminated on December 30, 2008. The total expense for the Plan was \$2,115 for 2008 and \$2,262 for 2007.

VIRGINIA HISTORICAL SOCIETY

Notes to Financial Statements, Continued

13. Executive Retirement Plan – 457(b):

The Society began a 457(b) Nonqualified Executive Retirement Plan (the “Plan”) effective August 1, 2007. Under the Plan, administrative staff and other highly compensated employees may participate upon approval of the Board-designated Administrative Committee, which has discretionary authority to make determinations as to eligibility and benefits under the Plan. Employee contribution is also limited by Internal Revenue Service regulations. The Society matches 100% of the employee contribution up to 6% of compensation. Employees are vested in employer contributions as follows:

Years of service	Vesting percentage
1	33%
2	66%
3 or more	100%

The total expense for the Plan was \$8,003 for 2008 and \$16,229 for 2007.

14. Temporarily Restricted Net Assets:

Temporarily restricted net assets available were \$13,651,144 at December 31, 2008 and \$12,835,218 at December 31, 2007, including:

	2008	2007
Time restricted	\$ 2,996,045	\$ 1,558,085
Campaign funds	5,783,653	11,034,682
Unapproved or unspent appreciation	4,871,446	-
Program services	-	242,451
Total temporarily restricted net assets	\$ 13,651,144	\$ 12,835,218

15. Permanently Restricted Net Assets:

Permanently restricted net assets were \$29,138,328 at December 31, 2008 and \$29,239,925 at December 31, 2007. These net assets are restricted to investment in perpetuity, the income from which is expendable to support general or specific purposes as stipulated by the donor.