



PACIFIC NORTHWEST BALLET

**Report of Independent Auditors and
Consolidated Financial Statements
with Supplemental Information**

**June 30, 2011,
with Comparative Totals for 2010**

MOSS ADAMS_{LLP}

Certified Public Accountants | Business Consultants

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CONTENTS

	PAGE
REPORT OF INDEPENDENT AUDITORS	1
CONSOLIDATED FINANCIAL STATEMENTS	
Balance sheet	2
Statement of activities	3
Statement of cash flows	4
Notes to financial statements	5-19
SUPPLEMENTAL INFORMATION	
Consolidated schedule of direct expenses	20

REPORT OF INDEPENDENT AUDITORS

To the Audit Committee
Pacific Northwest Ballet

We have audited the accompanying consolidated balance sheet of Pacific Northwest Ballet Association and Pacific Northwest Ballet Foundation (collectively, "Pacific Northwest Ballet" or the "Company") as of June 30, 2011, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The prior-year summarized comparative information has been derived from the Company's 2010 consolidated financial statements and, in our report dated September 16, 2010, we expressed an unqualified opinion on those consolidated financial statements.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Pacific Northwest Ballet as of June 30, 2011, and the consolidated results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The supplemental information listed in the table of contents is presented for the purpose of additional analysis and is not a required part of the basic consolidated financial statements. The supplemental information is the responsibility of the Pacific Northwest Ballet's management. Such information has been subjected to the auditing procedures applied in our audit of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects when considered in relation to the basic consolidated financial statements taken as a whole.

Moss Adams LLP

Seattle, Washington
October 26, 2011

PACIFIC NORTHWEST BALLET
CONSOLIDATED BALANCE SHEET
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

	2011	2010
ASSETS		
PNB Association assets		
Current assets		
Cash and cash equivalents	\$ 843,978	\$ 192,622
Accounts receivable	68,745	765,603
Contributions receivable, net	1,341,509	904,189
Inventory	203,210	232,460
Prepaid expenses	548,144	433,754
Total current assets	3,005,586	2,528,628
Long-term contributions receivable	462,458	155,792
Investments	443,205	713,872
Gift annuity reserves	215,535	249,967
Other assets	99,415	83,943
Property and equipment, net	5,085,362	5,815,717
Total PNB Association assets	9,311,561	9,547,919
PNB Foundation assets		
Investments	12,564,140	10,171,489
Contributions receivable, net of allowance for doubtful accounts	708,337	1,032,511
Charitable remainder unitrust receivable	1,365,790	1,324,462
Total PNB Foundation assets	14,638,267	12,528,462
 TOTAL ASSETS	 \$ 23,949,828	 \$ 22,076,381
LIABILITIES		
Current liabilities		
Accounts payable and accrued expenses	\$ 1,489,584	\$ 1,686,286
Deferred revenue	2,813,253	2,890,694
Line of credit	-	235,010
Notes payable - current portion	11,015	9,873
Gift annuities payable - current portion	18,546	20,686
Total current liabilities	4,332,398	4,842,549
Notes payable	51,016	62,030
Gift annuities payable	134,571	160,081
TOTAL LIABILITIES	4,517,985	5,064,660
 NET ASSETS		
Unrestricted	5,275,337	3,729,820
Temporarily restricted	2,389,395	1,941,986
Permanently restricted	11,767,111	11,339,915
TOTAL NET ASSETS	19,431,843	17,011,721
	\$ 23,949,828	\$ 22,076,381

PACIFIC NORTHWEST BALLET
CONSOLIDATED STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

	Unrestricted Operating	Unrestricted Plant	Board Designated	Temporarily Restricted	Permanently Restricted	2011 Total	2010 Total
EARNED REVENUE							
Ticket sales	\$ 10,760,281	\$ -	\$ -	\$ -	\$ -	\$ 10,760,281	\$ 10,380,634
Ballet school and outreach	3,063,661	-	-	-	-	3,063,661	2,803,696
Boutique (net)	115,472	-	-	-	-	115,472	99,127
Other earned income	314,184	-	-	-	-	314,184	286,162
Investment return - Association	33,262	-	-	544	-	33,806	20,977
Investment return - Foundation	-	-	2,454,889	-	-	2,454,889	1,122,440
	<u>14,286,860</u>	<u>-</u>	<u>2,454,889</u>	<u>544</u>	<u>-</u>	<u>16,742,293</u>	<u>14,713,036</u>
EXPENSES							
Artistic and production	10,413,004	-	-	-	-	10,413,004	10,331,712
Ballet school and outreach	2,931,231	-	-	-	-	2,931,231	3,006,808
Marketing	3,623,175	-	-	-	-	3,623,175	3,545,134
Administration	1,699,913	-	-	-	-	1,699,913	1,649,688
Development	998,998	-	-	-	-	998,998	980,989
Investment expense - Foundation	-	-	72,439	-	-	72,439	58,691
Contributed services	559,361	-	-	-	-	559,361	506,539
	<u>20,225,682</u>	<u>-</u>	<u>72,439</u>	<u>-</u>	<u>-</u>	<u>20,298,121</u>	<u>20,079,561</u>
Income (loss) from operations	<u>(5,938,822)</u>	<u>-</u>	<u>2,382,450</u>	<u>544</u>	<u>-</u>	<u>(3,555,828)</u>	<u>(5,366,525)</u>
CONTRIBUTIONS							
Contributions to Association	4,103,888	-	330	1,476,033	-	5,580,251	4,882,647
Contributions to Foundation	-	-	54,089	-	444,696	498,785	111,617
Contributions from affiliated groups	35,305	-	-	-	-	35,305	42,826
Special events (net expenses of \$96,303 and \$44,049)	79,665	-	-	-	-	79,665	112,357
Contributed services	559,361	-	-	-	-	559,361	506,539
Loss on uncollectible pledges	(41,336)	-	-	-	(17,500)	(58,836)	(17,299)
	<u>4,736,883</u>	<u>-</u>	<u>54,419</u>	<u>1,476,033</u>	<u>427,196</u>	<u>6,694,531</u>	<u>5,638,687</u>
RELEASES AND TRANSFERS							
PNB Foundation support	758,000	-	(758,000)	-	-	-	-
Releases of restricted funds	916,639	-	-	(916,639)	-	-	-
Funds designated by board for endowment	(37,027)	-	37,027	-	-	-	-
Funds designated by board for Stabilization Fund	(420,000)	-	420,000	-	-	-	-
	<u>1,217,612</u>	<u>-</u>	<u>(300,973)</u>	<u>(916,639)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Change in net assets before depreciation and amortization	<u>15,673</u>	<u>-</u>	<u>2,135,896</u>	<u>559,938</u>	<u>427,196</u>	<u>3,138,703</u>	<u>272,162</u>
DEPRECIATION AND AMORTIZATION							
Depreciation and amortization expense	(230,178)	(488,403)	-	-	-	(718,581)	(733,311)
Releases of funds for depreciation expense	112,529	-	-	(112,529)	-	-	-
	<u>(117,649)</u>	<u>(488,403)</u>	<u>-</u>	<u>(112,529)</u>	<u>-</u>	<u>(718,581)</u>	<u>(733,311)</u>
CHANGE IN NET ASSETS	(101,976)	(488,403)	2,135,896	447,409	427,196	2,420,122	(461,149)
NET ASSETS							
Beginning of year	<u>(2,435,718)</u>	<u>4,826,988</u>	<u>1,338,550</u>	<u>1,941,986</u>	<u>11,339,915</u>	<u>17,011,721</u>	<u>17,472,870</u>
End of year	<u>\$ (2,537,694)</u>	<u>\$ 4,338,585</u>	<u>\$ 3,474,446</u>	<u>\$ 2,389,395</u>	<u>\$ 11,767,111</u>	<u>\$ 19,431,843</u>	<u>\$ 17,011,721</u>

See accompanying notes.

PACIFIC NORTHWEST BALLET
CONSOLIDATED STATEMENT OF CASH FLOWS
YEAR ENDED JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

	<u>2011</u>	<u>2010</u>
OPERATING ACTIVITIES		
Change in net assets	\$ 2,420,122	\$ (461,149)
Adjustments to reconcile change in net assets to cash from operating activities		
Depreciation and amortization	718,581	733,311
Net gain on investments	(2,306,903)	(1,036,742)
Contributions restricted for long-term investments	(481,285)	83,932
Provision for doubtful accounts	41,336	17,299
Cash from changes in operating assets and liabilities		
Accounts receivable	343,039	(243,851)
Contributions receivable	(785,322)	208,007
Inventory and prepaid expenses	(85,140)	193,752
Other assets	(15,472)	22,066
Accounts payable and accrued expenses	(196,702)	(59,684)
Deferred revenue	(77,441)	127,071
Net change in cash from operating activities	<u>(425,187)</u>	<u>(415,988)</u>
INVESTING ACTIVITIES		
Payments for property and equipment	(12,612)	(601,261)
Receipts from disposal of property and equipment	24,386	-
Payments to life tenants of gift annuity	(19,081)	(20,091)
Change in gift annuity actuary valuation	37,026	-
Purchases of investments	(6,487,259)	(5,644,838)
Proceeds from sale of investments	7,014,834	5,643,695
Net change in cash from investing activities	<u>557,294</u>	<u>(622,495)</u>
FINANCING ACTIVITIES		
Net receipts (payments) on line of credit	(235,010)	235,010
Payments on note payable	(9,872)	(8,850)
Contributions restricted for long-term investments	764,131	820,285
Net change in cash from financing activities	<u>519,249</u>	<u>1,046,445</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	651,356	7,962
CASH AND CASH EQUIVALENTS		
Beginning of year	<u>192,622</u>	<u>184,660</u>
End of year	<u>\$ 843,978</u>	<u>\$ 192,622</u>

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 1 - Description of Organization and Summary of Significant Accounting Policies

Organization - The Pacific Northwest Ballet Association (the “Association” or “PNB Association”) and the Pacific Northwest Ballet Foundation (the “Foundation” or “PNB Foundation”) (collectively, the “Organization” or “PNB”) are not-for-profit corporations organized in 1972 and 1996, respectively. The Association stages several major ballets each year, operates a ballet school, and promotes public interest in the art of ballet. The mission of the Association is to enrich lives in the Pacific Northwest by:

- Setting new standards for artistic excellence, innovation, and creativity;
- Attracting the most talented dancers, choreographers, musicians, staff, and volunteers;
- Educating and developing dance artists as well as enthusiasts;
- Captivating a devoted, supportive, continually growing, and diverse audience; and
- Strengthening the Organization’s financial foundation.

The Foundation was formed to conduct and support activities exclusively for the benefit of the Association. The Foundation receives and holds endowment funds for and makes distributions to the Association.

Basis of Presentation - The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) using the accrual basis of accounting. The Organization follows the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 958-205, NPO Entities *Presentation of Financial Statements*. The Organization reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

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

- Unrestricted net assets: Net assets that are not subject to donor-imposed restrictions and consist of operating, plant, and board-designated assets. Temporarily restricted support received during the fiscal period for which the restriction expires or the purpose is accomplished during the same period is reported as unrestricted support.
- Temporarily restricted net assets: Net assets subject to donor-imposed restrictions that may or will be met either by actions of the Organization or the passage of time.
- Permanently restricted net assets: The Organization has interpreted Washington State’s Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA) as requiring the following to be classified as permanently restricted assets:
 - ❖ The original value of gifts designated by donors for the endowment.
 - ❖ The original value of matching gifts related to donor-designated endowment gifts.
 - ❖ If required by the donor gift instrument, accumulations to those donor-designated endowment funds.

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 1 - Description of Organization and Summary of Significant Accounting Policies (Continued)

Changes in Net Assets - 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 and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets are reported as releases from restrictions. Temporarily restricted contributions received and expended in the same accounting period are recorded as unrestricted net asset activity when satisfaction of the restriction is met within the same fiscal year.

Basis of Consolidation - The consolidated financial statements include the financial position and the results of activities, changes in net assets, and cash flows of the Association and the Foundation. All significant intercompany transactions have been eliminated in the consolidated financial statements.

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

Cash and Cash Equivalents - The Organization considers all temporary investments with an original maturity of three months or less to be cash equivalents. The Organization maintains its cash and cash equivalents in depository institution accounts that, at times, may exceed federally insured limits. The Organization has not experienced any losses in such accounts.

Accounts Receivable - Accounts receivable consist of amounts due for student tuition, credit card sales, and for costume and set rentals or co-productions. All account balances are due in less than one year. No allowance for uncollectible balances has been deemed necessary based upon historical experience.

Contributions Receivable - Contributions, which include unconditional promises to give (pledges), are recognized as revenues in the period received. The Organization records an allowance for doubtful accounts on pledges based on review of individual past due balances, historical write-off experience, and economic data. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using the discount rate adjustment technique, in which the rate is based upon the rate a market participant would demand (see Note 3).

Inventory - Inventory consists of ballet shoes for use by PNB dancers in future performances, and leotards for purchase by PNB School students. Such inventory items are recorded at lower of cost or market.

Investments - The Organization's investments are recorded at fair value in the consolidated balance sheet, and the realized and unrealized gains and losses on investments are reported in the consolidated statement of activities as part of investment return. A portion of the Organization's investments are held in private investment partnerships, which are considered alternative investments. The board engages investment consultants to investigate and monitor these investments. See Note 5 for further consideration of the fair market value of investments.

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 1 - Description of Organization and Summary of Significant Accounting Policies (Continued)

Gift Annuities - The Organization periodically enters into gift annuity agreements in connection with contributions for which it is obligated to make periodic payments to designated beneficiaries. Assets contributed are recorded at fair value when received, and a liability is recorded at the present value of future cash flows to annuitants. Funds equal to at least 110% of the present value of payments due to beneficiaries are maintained in a reserve account as required by statute. Investment earnings on the annuity reserves are recognized when earned, and actuarial adjustments are made to the liability annually. The annuity reserve consists of mutual funds that are invested in domestic and international equity securities, fixed income, and money market accounts.

Charitable Remainder Unitrust Receivable - The Foundation is the beneficiary of a trust administered by a donor. The trust invests in temporary cash investments, mutual funds, and contracts receivable. The Foundation's beneficiary interest receivable is recorded at its estimated fair value based on the use of present value techniques and the trust administrator's annual estimated fair value based on unobservable inputs. See Note 5 for further consideration of inputs.

Property and Equipment - Property and equipment is stated at cost. Sets and costumes with a minimum original cost of \$250,000, equipment with a minimum cost of \$5,000, and leasehold improvements with an original cost of \$50,000 are capitalized. Long-lived assets that are acquired with restricted gifts maintain a time restriction that expires over the useful life of the asset. Leasehold improvements represent capitalized costs of constructing the Organization's rehearsal, school, and administrative facilities in its leased Seattle Center and Bellevue locations. Gains or losses on the disposition of capital assets are included in the statement of activities at the time of disposal (Note 6).

Depreciation and amortization of property and equipment are provided as follows:

Sets and costumes	Straight-line basis	3-10 years
Office, studio, and stage equipment	Straight-line basis	3-5 years
Leasehold improvements	Straight-line basis	Lesser of lease term or estimated useful life

Deferred Revenue - Deferred revenue consists primarily of ticket sales for the upcoming season and tuition for ballet school classes held in the summer, subsequent to the corresponding consolidated balance sheet date.

Advertising Expense - Advertising costs are recognized as expense in the period in which the performance occurs. Advertising expense was \$1,818,032 and \$1,714,393 for the years ended June 30, 2011 and 2010, respectively.

Income Tax - The Organization is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code except to the extent of unrelated business income from a partnership with Seattle Opera to operate the Amusements gift shop in McCaw Hall. Income tax expense was approximately \$3,000 for the years ended June 30, 2011 and 2010. As of June 30, 2011 and 2010, the Organization had no uncertain tax positions requiring accrual.

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 1 - Description of Organization and Summary of Significant Accounting Policies (Continued)

Contributed Services - Contributed goods are recorded at fair value when received by the Organization. Contributed professional services are reflected in the consolidated financial statements, inasmuch as an objective basis is available to measure the value of such services. However, a substantial number of volunteers have donated their time to the program services and fund-raising campaigns of the Organization, which is not reflected in the consolidated financial statements because no objective basis is available to measure the value of such services.

Reclassifications - Certain reclassifications have been made in the prior-year consolidated financial statements to conform to the current year presentation. The reclassifications have no effect on the results of consolidated operations or equity.

Subsequent Events - Subsequent events are events that occur after the balance sheet date but before consolidated financial statements are issued. The Organization recognizes in the consolidated financial statements the effects of all subsequent events that provide additional evidence about conditions that existed at the date of the consolidated balance sheet, including the estimates inherent in the process of preparing the consolidated financial statements. The Organization has evaluated subsequent events through October 26, 2011. This is the date that the consolidated financial statements were available to be issued, and the Organization has recognized the effects of those subsequent events, if any, as required by GAAP.

Note 2 - Contributions and Grants

Contributions and grants consisted of the following for the years ended June 30:

	2011			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Individual and affiliated groups	\$ 3,185,832	\$ 1,036,288	\$ 444,696	\$ 4,666,816
Corporate	328,860	348,385	-	677,245
Foundation	331,935	27,360	-	359,295
Government	346,985	64,000	-	410,985
	<u>\$ 4,193,612</u>	<u>\$ 1,476,033</u>	<u>\$ 444,696</u>	<u>\$ 6,114,341</u>
	2010			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Individual and affiliated groups	\$ 2,978,243	\$ 638,850	\$ 63,226	\$ 3,680,319
Corporate	285,720	340,185	-	625,905
Foundation	348,638	34,500	-	383,138
Government	341,728	6,000	-	347,728
	<u>\$ 3,954,329</u>	<u>\$ 1,019,535</u>	<u>\$ 63,226</u>	<u>\$ 5,037,090</u>

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 3 - Contributions Receivable

Contributions receivable consisted of the following at June 30:

	2011		Total	2010 Total
	PNB Association	PNB Foundation		
Current (less than one year)				
Individuals and affiliated groups	\$ 940,711	\$ 195,002	\$ 1,135,713	\$ 1,107,668
Corporate	104,303	-	104,303	135,453
Foundation	-	-	-	-
Government	400,495	-	400,495	224,750
Allowance for doubtful accounts	(104,000)	(50,000)	(154,000)	(164,000)
Current contributions receivable, net	<u>\$ 1,341,509</u>	<u>\$ 145,002</u>	<u>\$ 1,486,511</u>	<u>\$ 1,303,871</u>
Long-term (one to eight years)				
Individuals and affiliated groups	\$ 428,003	\$ 619,300	\$ 1,047,303	\$ 735,704
Corporate	-	-	-	-
Foundation	62,000	-	62,000	162,401
Government	-	-	-	-
Present value discount	(27,545)	(55,965)	(83,510)	(109,484)
Long-term contributions receivable, net	<u>\$ 462,458</u>	<u>\$ 563,335</u>	<u>\$ 1,025,793</u>	<u>\$ 788,621</u>

Note 4 - Net Assets

Unrestricted net assets consisted of the following at June 30:

	2011	2010
Unrestricted net assets		
<u>Pacific Northwest Ballet Association</u>		
Operating funds	\$ (2,537,694)	\$ (2,435,716)
Plant	4,338,585	4,826,987
	<u>1,800,891</u>	<u>2,391,271</u>
Unrestricted - board-designated net assets		
<u>Pacific Northwest Ballet Association</u>		
Stabilization fund	570,330	150,000
<u>Pacific Northwest Ballet Foundation</u>		
General Endowment Fund	1,952,133	1,939,371
Artistic Directors' Fund	981,685	981,685
Outreach Fund	37,026	-
General Endowment unitrust receivable	1,365,790	1,324,462
Undistributed net earnings	(1,432,518)	(3,056,969)
	<u>2,904,116</u>	<u>1,188,549</u>
Total unrestricted	<u>\$ 5,275,337</u>	<u>\$ 3,729,820</u>

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 4 - Net Assets (Continued)

Temporarily restricted net assets consisted of the following at June 30:

	2011	2010
Temporarily restricted net assets		
<u>Pacific Northwest Ballet Association</u>		
Dancer Transition Fund	\$ 164,308	\$ 158,418
Donor-restricted funds	2,225,087	1,783,568
Total temporarily restricted	\$ 2,389,395	\$ 1,941,986

Permanently restricted net assets consisted of the following at June 30:

	2011	2010
Permanently restricted net assets		
<u>Pacific Northwest Ballet Foundation</u>		
General Endowment Fund	\$ 3,562,532	\$ 3,563,032
School and Outreach Funds	4,005,709	3,620,124
Artistic and Creative Funds	3,210,980	3,207,455
Artistic Directors' Fund	1,093,855	1,093,855
Present value discount and allowance for doubtful accounts	(105,965)	(144,551)
Total permanently restricted net assets	\$11,767,111	\$ 11,339,915

Note 5 - Investments

The Organization applies the provisions of ASC 820, *Fair Value Measurements and Disclosures*, which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements.

The ASC describes three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities.
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active 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.

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 5 - Investments (Continued)

Level 2 assets consist of hedge fund investments measured at fair value on a recurring basis using net asset value per share (or its equivalent, such as member units or an ownership in partner's capital to which a proportionate share of net assets is attributed). The hedge fund investments allow capital withdrawals at the end of each quarter with written notice 45 to 90 days prior to quarter end. The funds seek appreciation by allocating their assets among a select group of private investment funds that utilize a variety of alternative investment strategies.

Level 3 assets consist of a charitable remainder unitrust receivable, administered by an outside trustee, which is valued at the present value of the estimated expected future remainder interest to be received when the trust assets are distributed. Adjustments to the remainder interest reflect changes in the fair value, life expectancy, and discount rate and are included as investment returns in the consolidated statement of activities. The discount rates used at June 30, 2011 and 2010, were 2.8% and 3.2%, respectively.

Investment securities are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities and investment contracts, and the level of uncertainty related to changes in the value of the investment securities, it is at least reasonably possible that changes in risks in the near term could materially affect account balances and the amounts reported in the consolidated balance sheet and the consolidated statement of activities.

Investments consisted of the following at June 30:

	2011	
	PNB Association	PNB Foundation
Money market	\$ 378,304	\$ 230,754
Debt securities	64,901	2,464,850
Equity securities	-	7,930,168
Hedge funds	-	1,938,368
	<u>\$ 443,205</u>	<u>\$12,564,140</u>
	2010	
	PNB Association	PNB Foundation
Money market	\$ 649,003	\$ 342,906
Debt securities	64,869	2,298,170
Equity securities	-	5,749,722
Hedge funds	-	1,780,691
	<u>\$ 713,872</u>	<u>\$10,171,489</u>

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 5 - Investments (Continued)

Net investment return consisted of the following for the years ended June 30:

	<u>2011</u>	<u>2010</u>
Interest and dividend income	\$ 181,792	\$ 157,994
Realized and unrealized gain on investments	<u>2,306,903</u>	<u>985,423</u>
	<u>\$ 2,488,695</u>	<u>\$ 1,143,417</u>

The following table discloses the summary of changes in the fair value of Level 3 investment assets:

	<u>2011</u>	<u>2010</u>
Beginning balance	\$ 1,324,462	\$ 3,196,104
Net unrealized gains (losses) *	41,328	(90,951)
Reclassification to Level 2	<u>-</u>	<u>(1,780,691)</u>
Ending balance	<u>\$ 1,365,790</u>	<u>\$ 1,324,462</u>
Earnings attributable to unrealized gains (losses)	<u>\$ 41,328</u>	<u>\$ (90,951)</u>

* Included within the accompanying consolidated statement of activities as investment return (loss) representing earnings for assets held as of June 30, 2011 and 2010.

During the year ended June 30, 2010, the Organization reclassified hedge fund investments from Level 3 to Level 2 based upon authoritative guidance that permits such classification as Level 2. The Organization recognizes transfers in and transfers out as the actual date of the event or change in circumstances that caused the transfer.

Note 6 - Property and Equipment

Property and equipment consisted of the following at June 30:

	<u>2011</u>		
	<u>Cost</u>	<u>Accumulated Depreciation/ Amortization</u>	<u>Net</u>
Leasehold improvements	\$ 10,538,861	\$ 6,200,277	\$ 4,338,584
Sets and costumes	5,188,176	4,454,685	733,491
Office, studio, and stage equipment	<u>990,975</u>	<u>977,688</u>	<u>13,287</u>
	<u>\$ 16,718,012</u>	<u>\$ 11,632,650</u>	<u>\$ 5,085,362</u>
	<u>2010</u>		
	<u>Cost</u>	<u>Accumulated Depreciation/ Amortization</u>	<u>Net</u>
Leasehold improvements	\$ 10,538,861	\$ 5,711,874	\$ 4,826,987
Sets and costumes	5,212,562	4,243,180	969,382
Office, studio, and stage equipment	<u>978,363</u>	<u>959,015</u>	<u>19,348</u>
	<u>\$ 16,729,786</u>	<u>\$ 10,914,069</u>	<u>\$ 5,815,717</u>

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 7 - Benefit Plans

The Organization has a contract with dancers employed under an American Guild of Musical Artists contract. The contract provides that the Organization shall contribute to the Pacific Northwest Ballet Association Employee Benefit Plan, a 401(k) plan, an amount that is 5% of each dancer's gross compensation, plus up to an additional 5% of matching contributions. Pension expense for dancers was approximately \$222,000 and \$190,000 for the years ended June 30, 2011 and 2010, respectively.

The Organization has a contract with musicians employed under an International Guild of Symphony, Opera and Ballet Musicians contract. The contract provides that the Organization shall contribute to the Pacific Northwest Ballet Association Employee Benefit Plan, a 401(k) plan, an amount that is 7% of each musician's wages, plus up to an additional 2% of matching contributions for years ended June 30, 2011 and 2010. Pension expense for musicians was approximately \$80,000 and \$74,000 for the years ended June 30, 2011 and 2010, respectively.

The Organization has a contract with stagehands employed under an International Alliance of Theatrical Stage Employees (IATSE) contract. The contract provides for 401(k) benefits under a union retirement plan, and requires that the Organization contribute 6% of gross pay to the IATSE plan. Pension expense for stagehands was approximately \$38,000 and \$52,000 for the years ended June 30, 2011 and 2010, respectively. Additionally, the contract provides for health and welfare benefits and requires that the Organization contribute 10% of gross wages to the union plan. The health and welfare benefits expense for stagehands was approximately \$65,000 and \$84,000 for the years ended June 30, 2011 and 2010, respectively.

The Organization has a contract with dressers employed under a Theatrical Wardrobe Union contract. The contract provides for 401(k) benefits under a union retirement plan, and requires that the Organization contribute 6% of gross wages. Pension expense for dressers was approximately \$10,000 and \$11,000 for the years ended June 30, 2011 and 2010. Additionally, the contract provides for health and welfare benefits and requires that the Organization contribute 11% and 10% of gross wages to the union plan for the years ended June 30, 2011 and 2010, respectively. The health and welfare benefits expense for dressers was approximately \$15,000 and \$18,000 for the years ended June 30, 2011 and 2010, respectively.

Salary expense for employees covered under collective bargaining agreements was approximately \$4,690,000 and \$4,494,000, representing 49% and 47% of salary expense for the years ended June 30, 2011 and 2010, respectively.

The Organization has a defined contribution plan to provide retirement benefits for all employees not covered by a collective bargaining agreement. Under the terms of the plan, it is optional for the Organization to match up to 4% of an eligible employee's annual gross wages. The Organization did not make any matching contribution for the years ended June 30, 2011 and 2010.

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 8 - Line of Credit

The Organization has a \$2,000,000 revolving credit facility, payable on demand, bearing interest at 1.75% plus the one-month LIBOR (1.94% at June 30, 2011) with a December 1, 2011, maturity. The facility is secured by the Organization's contribution receivables, costumes, and sets. Interest expense under the line of credit was approximately \$8,000 and \$5,000 for the years ended June 30, 2011 and 2010, respectively.

Note 9 - Notes Payable

Current notes payable consisted of the following at June 30:

	2011	2010
Music Acceptance Corp.	\$ 11,015	\$ 9,873

Long-term notes payable consisted of the following at June 30:

	2011	2010
Music Acceptance Corp.	\$ 51,016	\$ 62,030

Interest is paid at a rate of 10.99% annually. Interest paid on these notes was approximately \$7,400 and \$8,400 during 2011 and 2010, respectively. Principal and interest are paid monthly and the note matures in January 2016.

Note 10 - Rent Commitments

The Organization rents office, studio, schools, warehouses, and office equipment under noncancelable operating leases expiring through 2018. Several of these leases contain renewal options. Aggregate minimum rental commitments under these leases approximate the following as of June 30:

2012	\$ 382,104
2013	374,810
2014	373,332
2015	380,028
2016	386,916
Thereafter	1,434,420
	\$ 3,331,610

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 10 - Rent Commitments (Continued)

Fees for rental of the performance hall are paid when the performances are scheduled. Rental expense consists of the following for the years ended June 30:

	2011	2010
Office, studios, schools and warehouses	\$ 459,253	\$ 472,880
McCaw Hall	523,470	480,695
	\$ 982,723	\$ 953,575

Note 11 - Related Party Transactions

Contributions, including both gifts and pledges to give, from members of the Organization's board of trustees were approximately \$1,395,000 and \$1,128,000 for the years ended June 30, 2011 and 2010, respectively. Contributions receivable of approximately \$1,344,000 and \$1,482,000 as of June 30, 2011 and 2010, respectively, were due from members of the Organization's board of trustees.

Note 12 - Intellectual Property Agreement

On July 2, 2002, the Organization entered into an agreement to continue the Organization's interest in certain intellectual property and restaging of ballets. The agreement also requires that certain consulting services be provided throughout the lifetimes of the parties. Future amounts due under this agreement approximate the following as of June 30:

2012	\$ 122,000
2013	123,000
2014	124,000
2015	125,000
2016	126,000
Thereafter	795,000
	\$ 1,415,000

Note 13 - McCaw Hall Facility Use Fee

The Organization is party to an agreement dated November 1, 2005, with the Seattle Opera and Seattle Center regarding the McCaw Hall Facility Use Fee, whereby the three parties have shared responsibility for payment of the debt service for the outstanding balance of capital funding for McCaw Hall. Under a new agreement dated March 23, 2009, the three parties also share the responsibility for capital maintenance of McCaw Hall. The Organization is including a \$2 Facility Use Fee on each ticket sold for \$25 or more to cover its share of the debt service payment and the capital renewal costs of McCaw Hall. The Organization's share of the debt service is expected to be approximately \$35,000 for each year through 2023. The Organization's share of the capital renewal payment was \$100,000 in fiscal year 2011 and 2010, and is expected to be \$100,000 for fiscal year 2012, increasing to \$125,000 for years 2013 and 2014, and then increasing annually by 3% thereafter.

PACIFIC NORTHWEST BALLET
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

Note 14 - Endowment Policies

Investment earnings on permanently restricted net assets, including realized and unrealized capital gains, are classified as temporarily restricted net assets until they are appropriated for distribution to the Association in a manner consistent with the standard of prudence prescribed by the Washington State Uniform Prudent Management of Institutional Funds Act (UPMIFA).

Endowment net assets consist of the following as of June 30:

	<u>2011</u>	<u>2010</u>
Unrestricted net assets	\$ 2,904,116	\$ 1,188,549
Permanently restricted net assets	<u>11,767,111</u>	<u>11,339,915</u>
Total net assets	<u><u>\$ 14,671,227</u></u>	<u><u>\$ 12,528,464</u></u>

Change in endowment net assets for the year ended June 30, 2011:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Net assets, July 1, 2010	\$ 1,188,549	\$ -	\$ 11,339,915	\$ 12,528,464
Investment return	2,454,889	-	-	2,454,889
Distributions	(758,000)	-	-	(758,000)
Other expenses	(72,439)	-	-	(72,439)
Board-designated additions	37,027	-	-	37,027
Contributions	54,089	-	427,196	481,285
Total net assets, June 30, 2011	<u><u>\$ 2,904,115</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 11,767,111</u></u>	<u><u>\$ 14,671,226</u></u>

Change in endowment net assets for the year ended June 30, 2010:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Net assets, July 1, 2009	\$ 866,408	\$ -	\$ 11,276,689	\$ 12,143,097
Investment return	1,122,440	-	-	1,122,440
Distributions	(790,000)	-	-	(790,000)
Other expenses	(58,691)	-	-	(58,691)
Contributions	48,392	-	63,226	111,618
Total net assets, June 30, 2010	<u><u>\$ 1,188,549</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 11,339,915</u></u>	<u><u>\$ 12,528,464</u></u>

The Organization's policy is to recognize transfers in and transfers out as of the actual date of the event or change in circumstances that caused the transfer.

Investment Policy

- The investment policy of the Foundation is to increase the value of the Endowment portfolio and at the same time provide a dependable, growing source of income that will be used to support various programs of the Association.

Note 14 - Endowment Policies (Continued)

- Endowment assets will be managed on a total return basis while taking into account the level of investment income required. While the Board of the Foundation recognizes the importance of the preservation of capital, they also adhere to the principle that varying degrees of investment risk are generally rewarded with concomitant returns over the long term.
- Endowment assets will be diversified among asset classes, as well as within each asset class including diversification among sectors and industries, quality, market capitalization, and investment style on the premise that portfolio diversification and equity style diversification provide protection against a single security or class of securities having a disproportionate impact on aggregate performance.

Investment Objectives

- Risk - The Endowment's risk capacity enables it to serve its mission in perpetuity and to focus its investment horizon primarily over the long term. Consequently, it has the ability to take on a moderately higher degree of volatility and illiquidity than most operating entities. To that consideration, the board of the Foundation believes that a reasonable risk target for the investment portfolio is in the range of 12% to 14%, as measured by the per annum standard deviation of returns. The board of the Foundation believes that achieving that risk target can best be accomplished through a diversified set of investment assets.

With the Foundation's payout needs in mind, the following liquidity constraints will apply:

- ❖ Lock-ups - The Foundation may hold no more than 25% of the portfolio in assets with liquidity of one-quarter of a year or more, and no more than 10% of its portfolio in assets with liquidity of one year or more.
- ❖ Concentrations - The Foundation may not hold more than 5% of its portfolio in any single security that is not supported by the full faith of the U.S. Government.
- Return - Results will be measured through a total return approach, which is the sum of both market value changes (realized and unrealized) and the current yield (interest and dividends). The Endowment should seek to achieve the largest return that is possible, while still being consistent with its risk and liquidity targets. It recognizes that the magnitude of the potential return will vary substantially from one environment to the next. Accordingly, from time to time, it may be appropriate for the Foundation to adjust its return expectation to reflect the lack or plethora of opportunities in the market.

Note 14 - Endowment Policies (Continued)

Distribution Policy

- The overall objective of the distribution policy is to produce distributions to the Association, as well as to preserve the real value of the endowment funds through time by growth of principal. In accordance with UPMIFA, the board of trustees of the Foundation considers the following factors when determining (1) the amounts to be distributed to the Association in accordance with donor intent and (2) the amounts to be accumulated in the endowment funds in accordance with donor intent:
 - ❖ the duration and preservation of the endowment fund;
 - ❖ the purposes of the organization and the endowment fund;
 - ❖ general economic conditions;
 - ❖ the possible effect of inflation or deflation;
 - ❖ the expected total return from income and the appreciation of investments;
 - ❖ other resources of the organization; and
 - ❖ the investment policies of the organization.

- The distribution formula is based on 5% of the average invested assets over the previous 12 quarters ending March 31. The spending policy, as calculated above, is determined on a year-to-year basis by the board. The board has set the following guidelines with respect to any distribution:
 - ❖ Retain discretion to not make a distribution if the Board believes that the distribution would affect the viability of future distributions.

 - ❖ Retain discretion to make a distribution that would cause the fair value of assets to fall below the original value of gifts donated, if the Board believes that to do so would be consistent with UPMIFA and would be a prudent balance between the donors' intent to maintain funds in perpetuity and the donors' intent that the endowment provide support to the Association.

 - ❖ Reserve the right to not pay out in any given year.

- From time to time, the fair value of assets associated with donor-restricted endowment funds may fall below the level to be held in perpetuity. These deficiencies may result from unfavorable market fluctuations and/or from distributions to the Association that were deemed prudent by the board and consistent with the donors' intent. In accordance with generally accepted accounting principles, deficiencies of this nature do not reduce permanently restricted net assets, but are reported in unrestricted net assets. These donor-restricted fund deficiencies were \$0 and \$1,346,046 as of June 30, 2011 and 2010.

Note 15 - Contingencies

The Organization is involved in litigation and contingencies arising in the normal course of business. After consultation with legal counsel, management estimates that any current matters will be resolved without material adverse impact to the Organization's financial position.

SUPPLEMENTAL INFORMATION

PACIFIC NORTHWEST BALLET
CONSOLIDATED SCHEDULE OF DIRECT EXPENSES
YEAR ENDED JUNE 30, 2011, WITH COMPARATIVE TOTALS FOR 2010

	Program Expenses				Support Expenses			Total Expenses	
	Ballet Company and Production	Ballet School and Outreach	Marketing	Total	General Administration	Development	Total	2011	2010
Salaries, benefits, and taxes									
Salaries									
Dancers	\$ 2,509,744	\$ -	\$ -	\$ 2,509,744	\$ -	\$ -	\$ -	\$ 2,509,744	\$ 2,449,382
Musicians	1,362,381	329,020	-	1,691,401	-	-	-	1,691,401	1,777,575
Other artists	623,069	-	-	623,069	-	-	-	623,069	604,841
Technical	1,431,163	21,191	-	1,452,354	-	-	-	1,452,354	1,397,957
Administrative	-	556,473	644,743	1,201,216	932,714	468,237	1,400,951	2,602,167	2,627,616
Teachers	-	710,802	-	710,802	-	-	-	710,802	753,445
	<u>5,926,357</u>	<u>1,617,486</u>	<u>644,743</u>	<u>8,188,586</u>	<u>932,714</u>	<u>468,237</u>	<u>1,400,951</u>	<u>9,589,537</u>	<u>9,610,816</u>
Payroll taxes	757,436	209,698	82,457	1,049,591	89,611	60,717	150,328	1,199,919	1,168,563
Employee benefits	1,219,679	168,143	65,710	1,453,532	51,581	48,693	100,274	1,553,806	1,428,132
Total salaries, benefits, and taxes	<u>7,903,472</u>	<u>1,995,327</u>	<u>792,910</u>	<u>10,691,709</u>	<u>1,073,906</u>	<u>577,647</u>	<u>1,651,553</u>	<u>12,343,262</u>	<u>12,207,511</u>
Scenery and stage	224,905	4,002	-	228,907	-	-	-	228,907	288,635
Costume and toe shoes	242,895	107	-	243,002	-	-	-	243,002	243,915
Choreography and dance	488,559	100	-	488,659	-	-	-	488,659	517,205
Music and instruments	137,433	3,404	-	140,837	-	-	-	140,837	131,241
Performance hall	942,421	26,790	-	969,211	-	-	-	969,211	943,734
Total production expenses	<u>2,036,213</u>	<u>34,403</u>	<u>-</u>	<u>2,070,616</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,070,616</u>	<u>2,124,730</u>
Building occupancy	221,161	576,288	-	797,449	230,516	750	231,266	1,028,715	989,495
Computer and equipment	13,519	29,945	8,951	52,415	97,108	-	97,108	149,523	134,274
Telephone	3,872	7,587	2,362	13,821	57,425	-	57,425	71,246	67,153
Supplies	2,076	4,541	469	7,086	26,793	786	27,579	34,665	42,827
Property and casualty insurance	-	9,000	-	9,000	51,238	-	51,238	60,238	77,865
Student expenses	3,043	96,444	-	99,487	-	-	-	99,487	95,958
Advertising and public relations	-	8,373	1,786,814	1,795,187	200	22,645	22,845	1,818,032	1,714,393
Professional services	50,332	20,864	336,840	408,036	47,402	116,099	163,501	571,537	585,297
Printing and copying	305	5,946	260,404	266,655	8,480	21,551	30,031	296,686	309,334
Postage and delivery	6,932	4,377	179,512	190,821	8,643	11,992	20,635	211,456	183,128
Travel	154,719	67,992	3,766	226,477	2,779	1,099	3,878	230,355	333,451
Hospitality	7,719	1,376	8,383	17,478	17,872	177,367	195,239	212,717	228,117
Dues, fees, and interest	8,082	53,379	239,296	300,757	143,620	43,824	187,444	488,201	447,948
Miscellaneous	1,559	15,389	3,468	20,416	6,370	25,238	31,608	52,024	31,541
Total other expenses	<u>473,319</u>	<u>901,501</u>	<u>2,830,265</u>	<u>4,205,085</u>	<u>698,446</u>	<u>421,351</u>	<u>1,119,797</u>	<u>5,324,882</u>	<u>5,240,781</u>
	<u>\$ 10,413,004</u>	<u>\$ 2,931,231</u>	<u>\$ 3,623,175</u>	<u>\$ 16,967,410</u>	<u>\$ 1,772,352</u>	<u>\$ 998,998</u>	<u>\$ 2,771,350</u>	19,738,760	19,573,022
Contributed services								559,361	506,539
Total operating expenses								<u>\$ 20,298,121</u>	<u>\$ 20,079,561</u>