Houston Symphony Society and Houston Symphony Endowment

Consolidated Financial Statements
and Independent Auditors' Report
for the years ended May 31, 2017 and 2016

Blazek & Vetterling
CERTIFIED PUBLIC ACCOUNTANTS

Independent Auditors' Report

To the Board of Governing Directors of
Houston Symphony Society:

We have audited the accompanying financial statements of Houston Symphony Society and Houston Symphony Endowment (collectively the Symphony), which comprise the consolidated statements of financial position as of May 31, 2017 and 2016 and the related consolidated statements of activities and of cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Symphony as of May 31, 2017 and 2016 and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The financial information by entity for Houston Symphony Society and Houston Symphony Endowment presented on the consolidated statements of financial position as of May 31, 2017 and 2016 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

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financial statements. The information has been subjected to the auditing procedures applied in our audits 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.

Blazek & Vetterling

January 31, 2018

Houston Symphony Society and Houston Symphony Endowment

Consolidated Statements of Financial Position as of May 31, 2017 and 2016

	2017			2016		
	HOUSTON SYMPHONY SOCIETY	HOUSTON SYMPHONY ENDOWMENT	TOTAL	HOUSTON SYMPHONY SOCIETY	HOUSTON SYMPHONY ENDOWMENT	TOTAL
ASSETS						
Cash	$ 571,217		$ 571,217	$ 1,951,856		$ 1,951,856
Other receivables	240,211		240,211	170,461		170,461
Deferred costs and other assets	1,060,603		1,060,603	1,183,957		1,183,957
Pledges receivable, net *(Note 2)*	9,594,414	$ 6,861,307	16,455,721	7,089,698	$ 7,065,468	14,155,166
Property, net *(Note 3)*	1,032,013		1,032,013	1,184,733		1,184,733
Investments *(Notes 4 and 5)*		66,807,253	66,807,253		64,015,872	64,015,872
TOTAL ASSETS	$12,498,458	$73,668,560	$86,167,018	$11,580,705	$71,081,340	$82,662,045
LIABILITIES AND NET ASSETS						
Liabilities:						
Accounts payable	$ 1,600,620		$ 1,600,620	$ 2,173,275		$ 2,173,275
Accrued expenses	1,349,002		1,349,002	1,515,915		1,515,915
Deferred revenue	3,948,698		3,948,698	4,389,275		4,389,275
Due to (from) intercompany	941,955	$ (941,955)		1,559,640	$ (1,559,640)	
Notes payable *(Note 6)*	10,932,854		10,932,854	6,564,448		6,564,448
Accrued pension liability *(Note 11)*	6,905,528		6,905,528	8,201,318		8,201,318
Total liabilities	25,678,657	(941,955)	24,736,702	24,403,871	(1,559,640)	22,844,231
Net assets:						
Unrestricted *(Note 8)*	(18,048,905)	(2,687,697)	(20,736,602)	(17,076,583)	(3,849,233)	(20,925,816)
Temporarily restricted *(Note 9)*	4,868,706		4,868,706	4,253,417		4,253,417
Permanently restricted *(Note 10)*		77,298,212	77,298,212		76,490,213	76,490,213
Total net assets	(13,180,199)	74,610,515	61,430,316	(12,823,166)	72,640,980	59,817,814
TOTAL LIABILITIES AND NET ASSETS	$12,498,458	$73,668,560	$86,167,018	$11,580,705	$71,081,340	$82,662,045

See accompanying notes to consolidated financial statements.

Houston Symphony Society and Houston Symphony Endowment

Consolidated Statement of Activities for the year ended May 31, 2017

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
OPERATING REVENUE:				
Classical and pops series	$ 6,667,722			$ 6,667,722
Other concerts	3,722,260			3,722,260
Other operating income	613,000			613,000
Total operating revenue	11,002,982			11,002,982
OPERATING EXPENSES:				
Orchestra and concert production	20,863,666			20,863,666
Marketing, promotion and ticketing	4,841,697			4,841,697
General and administrative	4,345,517			4,345,517
Total operating expenses	30,050,880			30,050,880
Net deficit before contributed and endowment income	(19,047,898)			(19,047,898)
CONTRIBUTED AND ENDOWMENT INCOME:				
Contributed income:				
Contributions	10,028,347	$ 3,311,595	$ 553,844	13,893,786
Special events	2,341,064			2,341,064
Less cost of direct donor benefits	(1,067,810)			(1,067,810)
Government grants	1,174,771			1,174,771
Release of time and purpose restrictions	2,696,306	(2,696,306)		
Fundraising expenses	(3,701,203)			(3,701,203)
Net contributed income	11,471,475	615,289	553,844	12,640,608
Transfer from endowment for operations	5,109,106			5,109,106
Net contributed and endowment income	16,580,581	615,289	553,844	17,749,714
Changes in net assets from operations	(2,467,317)	615,289	553,844	(1,298,184)
OTHER:				
Investment return, net *(Note 4)*	6,270,642		254,155	6,524,797
Transfer from endowment in excess of accumulated earnings	(5,109,106)			(5,109,106)
Pension liability adjustment *(Note 11)*	1,494,995			1,494,995
CHANGES IN NET ASSETS	189,214	615,289	807,999	1,612,502
Net assets, beginning of year	(20,925,816)	4,253,417	76,490,213	59,817,814
Net assets, end of year	$ (20,736,602)	$ 4,868,706	$ 77,298,212	$ 61,430,316

See accompanying notes to consolidated financial statements.

Houston Symphony Society and Houston Symphony Endowment

Consolidated Statement of Activities for the year ended May 31, 2016

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
OPERATING REVENUE:				
Classical and pops series	$ 7,443,332			$ 7,443,332
Other concerts	2,886,890			2,886,890
Other operating income	279,312			279,312
Total operating revenue	10,609,534			10,609,534
OPERATING EXPENSES:				
Orchestra and concert production	19,909,005			19,909,005
Marketing, promotion and ticketing	4,396,170			4,396,170
General and administrative	3,607,503			3,607,503
Total operating expenses	27,912,678			27,912,678
Net deficit before contributed and endowment income	(17,303,144)			(17,303,144)
CONTRIBUTED AND ENDOWMENT INCOME:				
Contributed income:				
Contributions	9,739,375	$ 1,281,220	$ 669,702	11,690,297
Special events	2,607,668			2,607,668
Less cost of direct donor benefits	(701,379)			(701,379)
Government grants	1,012,775			1,012,775
Release of time and purpose restrictions	4,472,078	(4,472,078)		
Fundraising expenses	(3,805,273)			(3,805,273)
Net contributed income	13,325,244	(3,190,858)	669,702	10,804,088
Transfer from endowment for operations	4,532,433	(4,532,433)		
Net contributed and endowment income	17,857,677	(7,723,291)	669,702	10,804,088
Changes in net assets from operations	554,533	(7,723,291)	669,702	(6,499,056)
OTHER:				
Investment return, net *(Note 4)*	(2,932,811)	721,649	(226,377)	(2,437,539)
Transfer from endowment in excess of accumulated earnings	(916,422)	916,422		
Pension liability adjustment *(Note 11)*	(1,591,293)			(1,591,293)
CHANGES IN NET ASSETS	(4,885,993)	(6,085,220)	443,325	(10,527,888)
Net assets, beginning of year	(16,039,823)	10,338,637	76,046,888	70,345,702
Net assets, end of year	$ (20,925,816)	$ 4,253,417	$ 76,490,213	$ 59,817,814

See accompanying notes to consolidated financial statements.

Houston Symphony Society and Houston Symphony Endowment

Consolidated Statements of Cash Flows for the years ended May 31, 2017 and 2016

	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	$ 1,612,502	$ (10,527,888)
Adjustments to reconcile changes in net assets to net cash used by operating activities:		
Net realized and unrealized (gain) loss on investments	(6,322,548)	3,127,672
Contributions restricted to permanent endowment	(553,844)	(669,702)
Depreciation	219,149	214,552
Changes in operating assets and liabilities:		
Other receivables	(69,750)	201,800
Deferred costs and other assets	123,354	(144,369)
Pledges receivable	(2,504,716)	3,603,102
Account payable and accrued expenses	(739,568)	980,755
Deferred revenue	(440,577)	83,945
Accrued pension liability	(1,295,790)	1,934,926
Net cash used by operating activities	(9,971,788)	(1,195,207)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments	(2,532,979)	(27,031,976)
Proceeds from sales of investments	8,536,164	29,301,437
Net change in money market mutual funds held as investments	(2,472,018)	274,844
Purchases of property	(66,429)	(521,392)
Net cash provided by investing activities	3,464,738	2,022,913
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayments of notes payable	(20,561,857)	(17,708,000)
Proceeds from notes payable	24,930,263	17,698,000
Proceeds from contributions restricted to permanent endowment	758,005	932,172
Net cash provided by financing activities	5,126,411	922,172
NET CHANGE IN CASH	(1,380,639)	1,749,878
Cash, beginning of year	1,951,856	201,978
Cash, end of year	$ 571,217	$ 1,951,856

Supplemental disclosure of cash flow information:

	2017	2016
Cash paid for interest	$164,463	$117,112
Proceeds of donated securities reflected in net cash used by operating activities	$1,106,580	$1,558,915

See accompanying notes to consolidated financial statements.

NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization – Houston Symphony Society (the Society) was incorporated under the laws of the State of Texas in 1936 for charitable and educational purposes related to maintaining a symphony orchestra. The mission of the Society is to inspire and engage a large and diverse audience in greater Houston and beyond through exceptional orchestral and non-orchestral performances, educational programs and community activities.

Houston Symphony Endowment (the Endowment) was originally established as a trust in 1971 under the laws of the State of Texas as a part of and solely to support the operations of the Society. In June 2006, the form of organization of the Endowment was changed to a separate nonprofit corporation organized under the laws of the State of Texas, solely to support the operations of the Society. The nonprofit exemption was approved by the Internal Revenue Service in May 2007. The Endowment holds contributed funds in perpetuity, invests those funds, and makes contributions from time to time to the Society. Such contributions must meet the stated restrictions of donors, as well as the current policies of the Endowment. The Endowment is governed by a Board of Directors who is elected by the officers of the Board of Directors of the Society to serve staggered three-year terms with one-third of the directors elected each year.

Basis of presentation – These financial statements include the assets, liabilities, net assets and activities of the Society and the Endowment (collectively the Symphony). All balances and transactions between the consolidated entities have been eliminated.

Federal income tax status – The Society and the Endowment are exempt from federal income tax under §501(c)(3) of the Internal Revenue Code. The Society is classified as a public charity under §509(a)(2). The Endowment is classified as a Type I supporting organization under §509(a)(3).

Pledges receivable that are expected to be collected within one year are recorded at net realizable value. Pledges receivable that are expected to be collected in future years are discounted to estimate the present value of future cash flows. Discounts are computed using risk-free interest rates applicable to the years in which the promises are received. Amortization of discounts is included in contribution revenue. An allowance for uncollectible pledges is estimated based on management's periodic evaluation of past loss experience, known adverse situations that may affect the donor's ability to pay, and current economic conditions. It is possible that management's estimate regarding the collectability of these balances will change in the near term resulting in a change in the carrying value of the pledges receivable.

Property purchases greater than $1,000 that have a useful life greater than one year are capitalized at original cost if purchased and at estimated fair value at the date of gift if donated. Depreciation is provided on a straight-line basis over estimated useful lives of 3 to 10 years.

Investment valuation and income recognition – Investments in securities are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Society's management determines the valuation policies utilizing information provided by its investment advisers, custodians and fund managers. Contributed land held for investment is reported at historical cost based on the fair market value at the date of donation, which is lower than current market value. Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Net appreciation (depreciation) includes gains and losses on investments bought and sold as well as held during the year. Investment return is reported in the statement of activities as an increase in unrestricted net assets unless the use of the income is limited by donor-imposed restrictions. Investment return whose use is restricted by the donor is reported as an increase in temporarily or permanently restricted net assets.

Net asset classification – Contributions, investment return and the related net assets are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Unrestricted net assets* include those net assets whose use is not restricted by donor-imposed stipulations, even though their use may be limited in other respects, such as by contract or board designation.
- *Temporarily restricted net assets* include contributions and investment return restricted by the donor to use for specific purposes or time periods. When a purpose restriction is accomplished or a time restriction ends, temporarily restricted net assets are released to unrestricted net assets.
- *Permanently restricted net assets* include contributions and investment return that donors have restricted in perpetuity. Investment return that has not been restricted in perpetuity may be used to support the operations of the Symphony.

Revenue from ticket sales is recognized when the related services are provided. Amounts received but unearned are included in the statement of financial position as deferred revenue. Program costs are deferred when incurred and charged to expense when the related revenue is recognized.

Contributions – Contributions, including government grants, are recognized as revenue at fair value when an unconditional commitment is received from the donor. Conditional contributions are recognized in the same manner when the conditions are substantially met. Generally, contributions received with donor restrictions that limit their use are recorded as temporarily or permanently restricted contributions. Restricted contributions whose purpose is met in the same reporting period are reported as unrestricted contributions and increase unrestricted net assets.

Donated materials are recognized at fair value as unrestricted contributions when an unconditional commitment is received from the donor. The related expense is recognized as the item is used. Contributions of services are recognized when services received (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. During 2017, the Symphony received donated services and materials totaling $460,897, which included approximately $460,100 for information technology services, $151,000 for travel vouchers and services used for fundraising events, $80,000 for orchestra conductor fees, and $39,000 for equipment and instruments. During 2016, the Symphony received donated services and materials totaling $217,560, which included approximately $54,000 for donated information technology services and $81,900 for fundraising events.

During the years ended May 31, 2017 and 2016, a substantial number of volunteers contributed significant amounts of time in connection with programs, administration and fundraising for which no amount has been recorded in the financial statements because the services do not meet the criteria for recognition under generally accepted accounting principles.

Advertising costs are expensed as incurred, except for expenditures directly related to future seasons, which are recorded as prepaid expenses. In 2017 and 2016, the Symphony expensed approximately $904,000 and $916,000, respectively, for advertising costs. At May 31, 2017 and 2016, deferred costs include deferred advertising costs of approximately $25,000 and $10,000, respectively.

Changes in net assets from operations – The Symphony includes in its definition of operations all revenue and expenses that are an integral part of its programs and supporting activities. Non-operating investment return and changes in the pension liability are excluded from the changes in net assets from operations.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts reported as revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

Recent financial accounting pronouncements – In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-02, *Leases (Topic 842)*. Under this ASU, a lessee should recognize in the statement of financial position a lease liability and a lease asset representing its right to use the underlying asset for the term of the lease for both finance and operating leases. An entity may make an accounting policy election not to recognize lease assets and lease liabilities for leases with a term of 12 months or less. Recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee have not changed significantly. Qualitative and quantitative disclosures are required by lessees and lessors to enable users of financial statements to assess the amount, timing and uncertainty of cash flows arising from leases. The ASU is effective for fiscal periods beginning after December 15, 2019. Management has not yet determined the impact adoption of this ASU will have on the financial statements.

In August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities.* The amendments in this ASU are the first phase of changes aimed at providing more useful information to users of not-for-profit financial statements. Under this ASU, net assets will be presented in two classes: *net assets with donor restrictions* and *net assets without donor restrictions.* New or enhanced disclosures will be required about the nature and composition of net assets, and the liquidity and availability of resources for general operating expenditures within one year of the balance sheet date. Expenses will be required to be presented by both nature and function and investment return will be presented net of external and direct internal investment expenses. Absent explicit donor stipulations, restrictions on long-lived assets will expire when assets are placed in service. The ASU is effective for fiscal periods beginning after December 15, 2017, but early adoption is permitted. Adoption of this ASU will impact the presentation and disclosures of the financial statements.

NOTE 2 – PLEDGES RECEIVABLE

Pledges receivable at May 31, 2017 consist of the following:

	HOUSTON SYMPHONY SOCIETY	HOUSTON SYMPHONY ENDOWMENT	TOTAL
Pledges receivable are expected to be collected as follows:			
Less than one year	$ 8,454,473	$ 682,600	$ 9,137,073
One to five years	1,631,209	2,288,000	3,919,209
More than five years		4,500,000	4,500,000
Total pledges receivable	10,085,682	7,470,600	17,556,282
Unamortized discount	(36,883)	(591,478)	(628,361)
Allowance for uncollectible pledges receivable	(454,385)	(17,815)	(472,200)
Pledges receivable, net	$ 9,594,414	$ 6,861,307	$ 16,455,721

Pledges receivable at May 31, 2016 consist of the following:

	HOUSTON SYMPHONY SOCIETY	HOUSTON SYMPHONY ENDOWMENT	TOTAL
Total pledges receivable	$ 7,193,967	$ 8,130,830	$ 15,324,797
Unamortized discount	(14,269)	(1,047,547)	(1,061,816)
Allowance for uncollectible pledges receivable	(90,000)	(17,815)	(107,815)
Pledges receivable, net	$ 7,089,698	$ 7,065,468	$ 14,155,166

During 2017, the Society received a two-part challenge grant of $1,000,000. The first payment of $500,000 was conditional upon the Symphony raising matching funds of $4.5 million for the Vision 2025 Implementation Fund. This condition was met and the payment was received and recognized as contribution revenue in 2017. The second payment of $500,000 remains conditional upon the Symphony raising an additional $4.5 million for the Vision 2025 Implementation Fund by March 31, 2018. This amount will be recognized as contribution revenue in 2018, if the Symphony raises the required matching funds.

NOTE 3 – PROPERTY

Property consists of the following:

	2017	2016
Land	$ 16,915	$ 16,915
Computer and information systems	1,100,996	1,151,527
Instruments	1,979,878	1,898,683
Leasehold improvements	284,878	282,774
Furniture and equipment	176,931	176,931
Total property, at cost	3,559,598	3,526,830
Accumulated depreciation	(2,527,585)	(2,342,097)
Property, net	$ 1,032,013	$ 1,184,733

NOTE 4 – INVESTMENTS

Investments consist of the following:

	LIQUIDITY	REDEMPTION NOTICE	2017	2016
Investments, at fair value:				
Limited partnership funds:				
TIFF Keystone Fund, L.P. (a)	(a)	(a)	$ 27,995,654	$ 25,120,342
High Vista II, L.P. (b)	Quarterly	90 days	7,617,068	7,021,682
PMF Fund, L.P. (c)	(c)	(c)	1,776,859	1,987,701
Mutual funds	Daily	None	28,937,672	29,406,147
Total investments, at fair value			66,327,253	63,535,872
Land held for investment, at cost			480,000	480,000
Total investments			$ 66,807,253	$ 64,015,872

The limited partnership funds are invested with external investment managers who can invest in various alternative categories, including real estate, partnerships, long and short equity positions, natural resources, private equity, managed futures, emerging markets, distressed enterprises, and arbitrage positions. These investments are domestic and international in nature, may be illiquid, and may not be realized for a period of several years after the investments are made. In addition to risks associated with other investments, these investments include additional risks, resulting in a greater risk of losing invested capital. Such risks include, but are not limited to, limited liquidity, absence of oversight, dependence upon key individuals, emphasis on speculative investments (both derivatives and non-marketable investments), and nondisclosure of portfolio composition. The investment strategies of each of these funds are as follows:

(a) The TIFF Keystone Fund L.P.'s objective is to maximize annualized returns net of all costs over rolling 10-year periods while adhering to the partnership's risk parameters. In seeking to achieve this objective and in order to manage risk, the general partner intends to deploy the partnership's assets in a manner that seeks to limit to not greater than 10% the probability of a 25% or greater decline in the partnership's inflation-adjusted unit value measured over any time period. There is no assurance that the partnership will achieve this objective. The partnership expects to invest globally in multiple asset classes and in both publicly traded and privately placed securities, properties, and other assets, either directly or through investment funds, including private equity funds, private realty funds, natural resource funds, and hedge funds. There is a two-year lock-up period for redemptions of this investment, which ends in December 2018.

(b) High Vista II, L.P. seeks to maximize risk-adjusted returns over a long-term horizon and may invest in a wide array of investments and strategies. Redemptions can generally be made each calendar quarter, but the fund has the sole discretion to not offer redemptions at any time.

(c) The PMF Fund, L.P. is a closed-end, non-diversified, registered investment company that invests substantially all of its assets in the Endowment PMF Master Fund, L.P. (Master Fund), which also is a closed-end, non-diversified, registered investment company. The investment objective is to manage a portfolio of investment funds and cash to preserve value while prioritizing liquidity to investors over active management, until such time as the Master Fund's portfolio has been liquidated. Distributions will occur quarterly, as available. The process to fully liquidate is expected to take up to ten years.

There are no unfunded commitments as of May 31, 2017 or 2016.

Investment return consists of the following:

	2017	2016
Net realized and unrealized gain (loss)	$ 6,322,548	$ (3,127,672)
Interest and dividends	159,325	578,653
Rents and royalties	74,192	142,996
Custodian fees	(31,268)	(31,516)
Investment return, net	$ 6,524,797	$ (2,437,539)

In addition to the investment custodian fees reflected above, the Society also indirectly incurs management fees and other expenses from the investment funds in which it invests, which are reflected in the change in value of investment funds.

Investments are exposed to various risks such as interest rate, market and credit risks. Because of these risks, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the statement of financial position and statement of activities.

NOTE 5 – FAIR VALUE MEASUREMENTS

Generally accepted accounting principles require that certain assets and liabilities be reported at fair value and establish a hierarchy that prioritizes inputs used to measure fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The three levels of the fair value hierarchy are as follows:

- *Level 1* – Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the reporting date.
- *Level 2* – Inputs are other than quoted prices included in Level 1, which are either directly observable or can be derived from or corroborated by observable market data at the reporting date.
- *Level 3* – Inputs are not observable and are based on the reporting entity's assumptions about the inputs market participants would use in pricing the asset or liability.

Assets measured at fair value at May 31, 2017 are as follows:

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Mutual funds:				
Multi-asset	$ 25,686,712			$ 25,686,712
Money market	2,793,871			2,793,871
Large-cap stock index	457,089			457,089
Total mutual funds	$ 28,937,672	$ 0	$ 0	28,937,672
Investments at net asset value using practical expedient excluded from the fair value hierarchy:				
Limited partnership funds				37,389,581
Total assets at fair value				$ 66,327,253

Assets measured at fair value at May 31, 2016 are as follows:

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Mutual funds:				
Multi-asset	$ 24,291,304			$ 24,291,304
Money market	321,853			321,853
Large-cap stock index	4,792,990			4,792,990
Total mutual funds	$ 29,406,147	$ 0	$ 0	29,406,147
Investments at net asset value using practical expedient excluded from the fair value hierarchy:				
Limited partnership funds				34,129,725
Total assets at fair value				$ 63,535,872

Valuation methods used for assets measured at fair value are as follows:

- *Mutual funds* are valued at the published net asset value.
- *Limited partnership funds* are valued at net asset value as a practical expedient. The net asset value is determined by the fund based on the fair value of the underlying investments held by the fund less any liabilities. If a fund does not provide the fair value on a timely basis, the fair value is estimated based on the most recent value provided, as well as any other relevant information available.

These valuation methods may produce a fair value that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Symphony believes its valuation methods are appropriate, the use of different methods or assumptions could result in a different fair value measurement at the reporting date.

NOTE 6 – NOTES PAYABLE

Notes payable consist of the following:

	2017	2016
Line of credit with a financial institution for $10,500,000; interest payable quarterly at a variable rate equal to 1.30% over LIBOR (2.44761% at May 31, 2017); principal due at maturity on March 30, 2018.	$ 10,258,678	$ 5,564,448
Note payable to a financial institution; variable rate of 1.30% over LIBOR (2.44761% at May 31, 2017); principal and interest payments of $86,008 are due quarterly until maturity on March 30, 2019.	674,176	1,000,000
Total notes payable	$ 10,932,854	$ 6,564,448

Both notes are guaranteed by the Endowment and require the Society to maintain a tangible net worth of $40 million, and a ratio of liabilities to tangible net worth less than 75%. The Endowment is also required to hold a minimum balance of $20 million in marketable assets. Interest expense totaled approximately $163,000 and $117,000 in 2017 and 2016, respectively.

Maturities of notes payable at May 31, 2017 are as follows:

2018	$ 10,595,069
2019	337,785
Total	$ 10,932,854

NOTE 7 – COMMITMENTS

Lease commitments

The Symphony leases certain of its facilities under noncancelable operating lease agreements. Future minimum lease payments under these operating leases as of May 31, 2017 are as follows:

2018	$ 265,953
2019	257,193
2020	261,399
2021	127,491
Total	$ 912,036

Total rent expense for 2017 and 2016 was $1,004,389 and $877,520, respectively, and includes additional month-to-month rentals.

Performance and artist contracts

The Symphony has entered into performance and licensing contracts with various artists for 2018 performances totaling $619,950. As of May 31, 2017, unpaid commitments under these contracts total $572,550. If the Symphony cancels these performances, it may still be liable for all or a portion of these contract amounts.

NOTE 8 – UNRESTRICTED NET ASSETS

Unrestricted net assets consist of the following:

	2017	2016
Accumulated pension liability adjustment	$(10,257,231)	$(11,752,226)
Undesignated	(8,287,621)	(6,085,247)
Aggregate deficiencies of donor-restricted endowments	(2,687,697)	(3,849,233)
Board-designated implementation fund for strategic planning	495,947	760,890
Total unrestricted net assets	$(20,736,602)	$(20,925,816)

NOTE 9 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes:

	2017	2016
Future operations	$ 3,197,543	$ 4,253,417
European tour	1,581,721	
Instrument purchases	87,305	
Cosmos	2,137	
Total temporarily restricted net assets	$ 4,868,706	$ 4,253,417

NOTE 10 – ENDOWMENT

The Endowment was established for the purpose of supporting the Society. It includes only donor-restricted endowment funds. The Endowment Board of Directors has interpreted the Texas Uniform Prudent Management of Institutional Funds Act (TUPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Symphony classifies the original value of gifts donated to the permanent endowment and investment return restricted by the donor in perpetuity as permanently restricted net assets. The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Endowment Board of Directors in a manner consistent with the standard of prudence prescribed by TUPMIFA. In accordance with TUPMIFA, the Endowment Board of Directors considers the following factors in making a determination to appropriate accumulated donor-restricted endowment funds:

- The duration and preservation of the fund
- The purposes of the Symphony 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 Symphony
- The investment policies of the Endowment

Changes in net assets of the endowment funds are as follows:

	UNRESTRICTED	TEMPORARILY RESTRICTED	PERMANENTLY RESTRICTED	TOTAL
Endowment net assets, May 31, 2015	$ 0	$ 2,894,362	$ 76,046,888	$ 78,941,250
Contributions			669,702	669,702
Investment return:				
Interest, dividends, rents and royalties		721,649		721,649
Net realized and unrealized loss	(2,901,295)		(226,377)	(3,127,672)
Custodian fees	(31,516)			(31,516)
Net investment return	(2,932,811)	721,649	(226,377)	(2,437,539)
Distributions	(916,422)	(3,616,011)		(4,532,433)
Endowment net assets, May 31, 2016	(3,849,233)	0	76,490,213	72,640,980
Contributions			553,844	553,844
Investment return:				
Interest, dividends, rents and royalties	233,517			233,517
Net realized and unrealized gain	6,068,393		254,155	6,322,548
Custodian fees	(31,268)			(31,268)
Net investment return	6,270,642		254,155	6,524,797
Distributions	(5,109,106)			(5,109,106)
Endowment net assets, May 31, 2017	$ (2,687,697)	$ 0	$ 77,298,212	$ 74,610,515

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or TUPMIFA requires the Symphony to retain as a fund of perpetual duration. In accordance with generally accepted accounting principles, deficiencies of this nature are reported in unrestricted net assets.

Return Objectives and Risk Parameters

The Endowment has adopted investment and spending policies for endowment assets that have the primary objective of achieving a long-term rate-of-return that will permit the Endowment to assist the Symphony in meeting its operating needs while maintaining its ability to provide for future needs without subjecting the endowment funds to imprudent risks. Endowment assets include those assets of donor-restricted funds that the Symphony must hold in perpetuity or for the donor-specified periods.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the Endowment 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 Endowment 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.

As different asset classes produce different returns during the course of the year, the portfolio's asset allocation changes accordingly. Therefore, rebalancing asset allocations to policy targets is essential for maintaining the risk and return profile that has been adopted. The Endowment reviews the portfolio's actual asset allocation relative to established policy targets and ranges. If deemed necessary, the Endowment will rebalance the portfolio between the various asset classes based on market values.

Spending Policy and How the Investment Objectives Relate to Spending Policy

The Endowment's standing resolution on disbursements has a total return spending rule that allows spending budgets to be funded from interest and dividend income, realized gains, unused portions of prior year spending allowances that have been reinvested, and unrealized appreciation (to use unrealized appreciation units would have to be sold).

Under the standing resolution, expenditures are determined annually based on the Endowment's average market value of the 12 previous quarters as of the March 31 proceeding the Symphony's fiscal year in which the disbursement will be expended. New contributions for each quarter plus the new contributions for all preceding quarters used in the calculations are to be deducted from that quarter's ending fair market value to arrive at an adjusted fair market value. The cumulative new contributions for all quarters are then added to the average adjusted fair market value to form the valuation basis for the draw each year. Subject to restrictions placed by either donors or governing law, disbursements are at the discretion of the Endowment Board of Directors and may be increased or decreased at any time, and the standing policy may be suspended or altered at any time.

During 2017, a 6% distribution based on the Endowment's twelve-quarter rolling average was approved, with 5% distributed to operations in the amount of $3,341,599, and 1% used as forgiveness on the outstanding balance from the Society to the Endowment in the amount of $668,320. In addition, the fiscal year 2018 1% forgiveness was approved as of May 31, 2017 in the amount of $622,321 so that the outstanding loan balance was forgiven in total as of May 31, 2017. Total distributions also include $74,192 in royalty income used for operations and $402,664 distributed to fund capital campaign expenses. During 2016, a 6% distribution based on the Endowment's twelve-quarter rolling average was approved, with 5% distributed to operations in the amount of $3,326,751, and 1% used as forgiveness on the outstanding balance from the Endowment to the Society in the amount of $665,350. Total distributions also include $142,996 in royalty income used for operations and $397,336 distributed to fund capital campaign expenses.

The intercompany receivable balance between the Society and the Endowment at May 31, 2017 represents endowment contributions waiting to be invested and a $500,000 advance on the fiscal year 2018 distribution.

NOTE 11 – PENSION PLAN

Defined benefit retirement plans – Prior to May 31, 2017, the Symphony had two pension plans, the Musicians Retirement Plan (the Musicians Plan) and the Staff Employees' Retirement Plan (the Staff Plan) (collectively the Plans) that cover substantially all of its employees. Retirement benefits primarily are a function of a fixed amount reduced pro-rata for services less than 30 years under the Musicians Plan and the employee's compensation and years of service under the Staff Plan. The Symphony's current policy is to fund accrued pension costs. In 1998, the Symphony agreed to freeze the Musicians Plan and to begin funding the musicians' retirement through the American Federation of Musicians and Employers' Pension Fund, a multiemployer plan. Effective May 31, 2017, the Staff Plan was frozen and merged into the Musician's Plan, which was renamed The Houston Symphony Musicians and Staff Employees' Retirement Plan (the Musicians and Staff Plan). The Symphony uses a May 31 valuation date.

The funded status of each plan at May 31, 2017 and 2016 is as follows:

	MUSICIANS AND STAFF PLAN 2017	MUSICIANS PLAN 2016	STAFF PLAN 2016
Projected benefit obligation	$ 25,347,263	$ 17,763,558	$ 7,922,323
Fair value of plan assets	(18,441,735)	(13,231,761)	(4,252,802)
Unfunded projected benefit obligation	$ 6,905,528	$ 4,531,797	$ 3,669,521
Accumulated benefit obligation	$ 25,347,263	$ 17,763,558	$ 7,922,323

Amounts recognized in the statement of financial position at May 31, 2017 and 2016 are as follows:

	MUSICIANS AND STAFF PLAN 2017	MUSICIANS PLAN 2016	STAFF PLAN 2016
Accrued pension liability	$ 6,905,528	$ 4,531,797	$ 3,669,521

Amounts recognized in unrestricted net assets not yet recognized as periodic pension cost at May 31, 2017 and 2016 are as follows:

	MUSICIANS AND STAFF PLAN 2017	MUSICIANS PLAN 2016	STAFF PLAN 2016
Net loss	$ 10,257,231	$ 8,891,604	$ 2,872,564

Components of net periodic benefit cost at May 31, 2017 and 2016 are as follows:

	MUSICIANS PLAN 2017	STAFF PLAN 2017	MUSICIANS PLAN 2016	STAFF PLAN 2016
Interest cost	$ 642,780	$ 290,975	$ 685,521	$ 290,411
Service cost		257,022		231,933
Expected return on assets	(1,061,325)	(355,856)	(1,089,656)	(349,459)
Amortization of loss	296,991	345,566	256,240	318,637
Total net periodic benefit cost	$ (121,554)	$ 537,707	$ (147,895)	$ 491,522

Other changes in plan assets and benefit obligations recognized in changes in net assets are as follows:

	MUSICIANS PLAN 2017	STAFF PLAN 2017	MUSICIANS PLAN 2016	STAFF PLAN 2016
Net (gain) loss	$ (193,835)	$ (236,986)	$ 1,090,080	$ 1,091,143
Amortization of net gain	(296,991)	(345,566)	(268,709)	(321,221)
Amount recognized due to curtailment		(523,559)		
Total recognized in changes in net assets	$ (490,826)	$ (1,106,111)	$ 821,371	$ 769,922

The estimated actuarial loss from the Musicians and Staff Plan that will be amortized into net periodic benefit cost over the next fiscal year is $284,125. There is no estimated transition asset or prior service credit that will be amortized over the next fiscal year.

Weighted-average assumptions used to determine benefit obligation at year end:

	MUSICIANS PLAN 2017	STAFF PLAN 2017	MUSICIANS PLAN 2016	STAFF PLAN 2016
Discount rate	3.80%	3.80%	3.75%	3.75%

Weighted-average assumptions used to determine net periodic benefit cost:

	MUSICIANS PLAN 2017	STAFF PLAN 2017	MUSICIANS PLAN 2016	STAFF PLAN 2016
Discount rate	3.75%	3.75%	4.00%	4.25%
Expected return on plan assets	8.00%	8.00%	8.00%	8.00%

Additionally, during 2017 mortality assumptions were updated using mortality rates from the Adjusted RP-2014 Mortality Table (baseline mortality table as of 2006 based on experience study data for private pension plans underlying RP-2014) and mortality improvement scale from MP-2016 Table. The inflation rate assumptions increased from 1.75% in 2016 to 2.00% in 2017. These assumption changes, along with the change in the discount rate used, decreased the projected benefit obligation at May 31, 2017 by $578,211.

The expected long-term rate-of-return on assets is established taking into account the intended asset mix and historical rates-of-return on comparable assets.

Plan assets

The Plans were established for the exclusive purpose of providing benefits for employees and beneficiaries. Consistent with this purpose, the primary goal of managing the portfolio assets is to invest the assets so as to preserve the capital and provide an acceptable rate of growth and income. The Plans shall seek the highest possible return while maintaining a prudent regard for legal considerations, fiduciary responsibility, safety of capital and minimum volatility of returns.

The Symphony's targeted pension plan asset allocation by type of asset is as follows:

Equity	50%-75%
Fixed-income	20%-50%
Cash and other	0%-20%

Plan assets measured at fair value on a recurring basis for the Plans at May 31, 2017, by asset category are as follows:

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Equity mutual funds	$ 10,877,198			$ 10,877,198
Fixed-income mutual funds	7,450,381			7,450,381
Fixed-income pooled separate accounts	114,156			114,156
Total	$ 18,441,735	$ 0	$ 0	$ 18,441,735

Plan assets measured at fair value on a recurring basis for the Plans at May 31, 2016, by asset category are as follows:

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Equity mutual funds	$ 9,502,493			$ 9,502,493
Fixed-income mutual funds	7,982,070			7,982,070
Total	$ 17,484,563	$ 0	$ 0	$ 17,484,563

Investments in mutual funds are valued based on the daily published closing price as reported by the fund. Investments in pooled separate accounts are valued at net asset value as a practical expedient based on the fair value of the underlying investments held less liabilities, as determined by the fund manager.

No assets of the Plans are expected to be returned to the Symphony in the next fiscal year.

Cash flows

Contributions to the Plans provide for benefits attributed to service to date, as well as those expected to be earned in the future. The Symphony's contributions to the Plans totaled $115,000 in 2017 and $343,627 in 2016. The Symphony expects to make a contribution to the Plans in 2018 totaling $434,818. Distributions from the Plans during 2017 and 2016 were $1,087,423 and $1,247,267, respectively.

Estimated future benefit payments for the next ten years are as follows:

2018	$1,420,000
2019	$1,470,000
2020	$1,510,000
2021	$1,490,000
2022	$1,540,000
2023 through 2027	$7,640,000

NOTE 12 – MULTIEMPLOYER PENSION PLAN

The Society is a participating employer in a trustee-managed, multiemployer defined benefit pension plan for employees who are covered under the collective bargaining agreement of the Houston Professional Musicians Association (Local Union No. 65-699 of the American Federation of Musicians). The plan generally provides retirement benefits to employees based on years of service to the Society. The multiemployer pension plan is managed by a board of trustees with equal representation from the union and employers. Although the Society is not represented on the board of trustees, other contributing employers are members of the board of trustees. Contributions totaling $533,159 in 2017 and $530,679 in 2016 were charged to pension expense for ongoing participation in the pension plan. The Society's contributions do not represent more than 5% of the pension plan's total contributions. Additionally, there have been no significant changes that affect the comparability of 2017 and 2016 contributions.

The risks of participating in the multiemployer defined benefit pension plan are different from single-employer plans because: (a) assets contributed to the multiemployer plan by one employer may be used to provide benefits to employees of other participating employers, (b) if a participating employer stops contributing to the plan, the unfunded obligations of the plan may be required to be borne by the remaining participating employers, and (c) if the Society chooses to stop participating in the multiemployer plan, it may be required to pay a withdrawal liability to the plan. In connection with ongoing renegotiation of the collective bargaining agreement, the Society may discuss and negotiate for complete or partial withdrawal from the multiemployer pension plan. Depending on the number of employees withdrawn in any future period and the financial condition of the multiemployer plan at the time of withdrawal, the associated withdrawal liabilities could be material to the Society's consolidated change in net assets in the period of the withdrawal. The Society has no plans to withdraw from its multiemployer pension plan.

The following presents information about the Society's multiemployer pension plan as of May 31, 2017 and 2016 and for the years ended May 31, 2017 and 2016:

NAME OF PENSION FUND	EIN AND PLAN NUMBER, IF AVAILABLE	PENSION PROTECTION ACT ZONE STATUS 2017	2016	FIP/RP STATUS	CONTRIBUTIONS FOR THE YEAR ENDED MAY 31, 2017	2016	SURCHARGE IMPOSED	EXPIRATION OF COLLECTIVE BARGAINING AGREEMENT
American Federation of Musicians and Employers' Pension Fund	51-6120204 Plan No. 001	Red 03/31/17	Red 03/31/16	Implemented	$533,159	$530,679	Yes	10/06/18

Due to the plan's "critical" status under the Pension Protection Act of 2006, a rehabilitation plan was implemented by the union in 2010 requiring additional employer contributions. Per the collective bargaining agreement (see Note 13), the Society is required to contribute 6% of scale wages. As part of the rehabilitation program, the Society is now required to contribute 6.54% until the plan is no longer in critical status.

The Society also participates in a multiemployer defined contribution pension plan and a multiemployer defined contribution health and welfare plan for its stagehand employees. Total contributions to these plans were approximately $125,000 and $131,000 in 2017 and 2016, respectively.

NOTE 13 – CONCENTRATION OF RISK

The Symphony's musician employees who perform in the Houston Symphony Orchestra are covered by a collective bargaining agreement between the Society and the Houston Professional Musicians Association (Local Union No. 65-699), which expires in October 2018. The Symphony's stagehand employees are covered by a collective bargaining agreement between the Society and the International Alliance of Theatrical Stagehands (Local Union No. 51), which expires in July 2019.

NOTE 14 – RELATED PARTY TRANSACTIONS

The Symphony has four Governing Directors and three Board of Trustee members that are employed by or are partners of vendors with which the Symphony conducts business. The Symphony has a conflict-of-interest policy whereby all Board of Trustee members with conflicts recuse themselves from voting on any decision which would impact the vendor choices. The Symphony has an agreement with a local law firm to pay for the first $40,000 of legal services and receive the next $60,000 pro-bono each fiscal year. A Governing Director is a partner at this law firm and serves as the Symphony's General Counsel. During 2017 and 2016, the Symphony paid $37,618 and $40,598, respectively, to the law firm.

The Symphony also has an agreement with a local information technology consulting firm, whereby many services are provided as an in-kind contribution. The owner of the firm is a Governing Director. During 2017, the Symphony incurred $393,394 of expenses, of which $190,568 was contributed as in-kind services and $202,826 was paid. During 2016, the Symphony incurred $66,018 of expenses, of which $54,000 was contributed as in-kind services and $12,018 was paid.

Additional expenditures with related party vendors totaled $605,884 in 2017 and $387,620 in 2016 for rent, bank fees, special event, food and supplies.

NOTE 15 – SUBSEQUENT EVENTS

Management has evaluated subsequent events through January 31, 2018, which is the date that the financial statements were available for issuance. As a result of this evaluation, the following events were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.

Hurricane Harvey

On August 25, 2017, Hurricane Harvey hit the Texas Coast. Theatre District Houston, including the Symphony's primary performance, rehearsal and office space, Jones Hall suffered damage, and the Symphony was relocated to temporary office, rehearsal and performance spaces. Flooding in the basement and office spaces below Jones Hall caused significant damage to the Symphony's property, including the losses of the Society's vehicle, organ, podiums, stage equipment, instrument petting zoo, office furniture, paper files, and computer equipment. The Symphony's management has not determined the full-extent of the physical losses caused by Hurricane Harvey; however, the estimate for identified losses is $146,584. Insurance recoveries expected are $5,556 for the vehicle. Additional insurance recoveries may be possible, but the Symphony's management is not able to estimate them.

Additionally, the damages to the facilities caused a significant impact to the performance season; seventeen ticketed performances and the Opening Night Gala fundraising event were cancelled. Alternative venues were secured for seven performances, of which six were provided to the community with free admission. Subsequent to year end, the Symphony incurred the following expenses to mitigate damages, continue operations, pay employees while closed, and hold free concerts in alternative venues:

Staff and orchestra paid during closure and cancelled concerts	$ 1,229,000
Concerts held in alternative venues	378,177
Continued operations	88,509
Labor to mitigate damages	5,995
Disaster expenses, excluding property loses	$ 1,701,681

The Symphony has undertaken an unrestricted fundraising campaign for Hurricane Harvey recovery to mitigate the additional costs that will be incurred and the lost revenue experienced as a result of cancelled concerts and the significant fundraising event.

Line of Credit

In August 2017, the line of credit was increased to $15,000,000. The increased line of credit extended the maturity date to March 30, 2019. To manage the financial burden of Hurricane Harvey, the line of credit was temporarily increased to $17,000,000 until August 31, 2018, at which time it will return to the $15,000,000 limit.

401(k) Plan

On June 1, 2017, the Symphony added a new 401(k) plan for non-musician staff members. The plan is administered by Principal Financial Group and eligible Symphony employees can participate after one year of service. The Symphony will match from 1% to 4% of compensation depending on the employee contribution rate.