

FINANCIAL STATEMENTS TOGETHER WITH
REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

**ART STUDENTS LEAGUE OF NEW YORK AND ITS SUBSIDIARY
THE AMERICAN FINE ARTS SOCIETY, INC.**

For the year ended May 31, 2005
with comparative totals for the year ended May 31, 2004

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To The Trustees of
The Art Students League of New York

We have audited the accompanying statement of financial position of The Art Students League of New York and its subsidiary The American Fine Arts Society, Inc. (the "League") as of May 31, 2005 and the related statements of activities and cash flows for the year then ended. These consolidated financial statements are the responsibility of the League's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the financial statements and supplementary information of the League as of May 31, 2004 and for the year then ended.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America as established by the Auditing Standards Board of the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of the 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 League's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Art Students League of New York and its subsidiary The American Fine Arts Society, Inc. as of May 31, 2005 and the 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 financial statements of the League as of and for the year ended May 31, 2005, taken as a whole.

The supplemental schedules of functional expenses and the art store and cafeteria operations on pages 12 and 13 are presented for the purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Mangli + Company

New York, New York
November 15, 2005

Art Students League of New York and Subsidiary

STATEMENTS OF FINANCIAL POSITION

As of May 31, 2005 and 2004

	<u>ASSETS</u>	
	<u>2005</u>	<u>2004</u>
Current assets:		
Cash and cash equivalents	\$ 288,958	\$ 381,087
Investments	22,173,661	21,630,784
Miscellaneous receivables	26,339	22,167
Accrued interest and dividends	6,932	10,447
Prepaid expenses:		
Catalogue	70,997	69,366
Insurance	30,361	36,593
Others	145,699	1,285
Inventories:		
Art store	138,508	103,103
Cafeteria	3,632	3,208
Print portfolio	14,462	14,462
Total current assets	<u>22,899,549</u>	<u>22,272,502</u>
Property and equipment	9,305,247	9,598,382
Works of art	216,158	213,108
Total assets	<u>\$ 32,420,954</u>	<u>\$ 32,083,992</u>
	<u>LIABILITIES AND NET ASSETS</u>	
Liabilities:		
Accounts payable and accrued expenses	\$ 237,019	\$ 264,864
Deferred revenue	165,580	220,094
Locker deposits	20,690	17,452
Tuition credits	58,614	47,437
Total liabilities	<u>481,903</u>	<u>549,847</u>
Net assets:		
Unrestricted	15,441,504	16,513,644
Temporarily restricted	5,053,572	3,576,526
Permanently restricted	11,443,975	11,443,975
Total net assets	<u>31,939,051</u>	<u>31,534,145</u>
Total liabilities and net assets	<u>\$ 32,420,954</u>	<u>\$ 32,083,992</u>

The accompanying notes are an integral part of these financial statements

Art Students League of New York and Subsidiary

STATEMENT OF ACTIVITIES

For the year ended May 31, 2005 with comparative totals for the year ended May 31, 2004

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2005 Total</u>	<u>2004 Total</u>
Revenues and support:					
Tuition	\$ 2,401,782	-	-	\$ 2,401,782	\$ 1,992,740
Contributions	153,703	255,167	-	408,870	216,948
Fees	235,262	-	-	235,262	194,889
Investment income-net	187,277	415,232	-	602,509	680,854
Unrealized and realized gains and (losses)-net	395,359	877,905	-	1,273,264	1,683,085
Other revenue (net of expenses):					
Art store	82,616	-	-	82,616	48,666
Cafeteria	(9,331)	-	-	(9,331)	8,682
Special events (net of expenses of \$3,692)	28,584	-	-	28,584	11,648
Other income	57,344	-	-	57,344	67,945
	<u>3,532,596</u>	<u>1,548,304</u>	<u>-</u>	<u>5,080,900</u>	<u>4,905,457</u>
Net assets released from restrictions:					
Satisfaction of program restrictions	<u>71,258</u>	<u>(71,258)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total revenues and support	<u>3,603,854</u>	<u>1,477,046</u>	<u>-</u>	<u>5,080,900</u>	<u>4,905,457</u>
Expenses:					
Program services	3,821,943	-	-	3,821,943	3,302,835
Supporting services:					
Management and general	740,102	-	-	740,102	657,453
Fundraising	113,949	-	-	113,949	95,020
Total expenses	<u>4,675,994</u>	<u>-</u>	<u>-</u>	<u>4,675,994</u>	<u>4,055,308</u>
Change in net assets	(1,072,140)	1,477,046	-	404,906	850,149
Net assets, beginning of year	<u>16,513,644</u>	<u>3,576,526</u>	<u>11,443,975</u>	<u>31,534,145</u>	<u>30,383,996</u>
Net assets, end of year	<u>\$ 15,441,504</u>	<u>\$ 5,053,572</u>	<u>\$ 11,443,975</u>	<u>\$ 31,939,051</u>	<u>\$ 31,234,145</u>

Art Students League of New York and its Subsidiary

STATEMENTS OF CASH FLOWS

For the years ended May 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Cash flows from operating activities:		
Changes in net assets	\$ 404,906	\$ 850,149
Adjustments to reconcile changes in net assets to cash provided by:		
operating activities:		
Depreciation expense	399,200	252,533
Unrealized gains on investments	(992,636)	(1,095,055)
Change in operating assets and liabilities:		
(Increase) decrease in miscellaneous receivables	(4,172)	1,585
Decrease (increase) in accrued interest and dividends	3,516	(5,721)
(Increase) decrease in miscellaneous receivables	(139,813)	6,338
(Increase) in inventories	(35,829)	(60,070)
(Increase) in works of art	(3,050)	-
(Decrease) in accounts payable and accrued expenses	(27,845)	(540,973)
(Decrease) increase in deferred revenue	(54,514)	113,807
Increase in other liabilities	14,415	39,315
Net cash (used in) operating activities	<u>(435,822)</u>	<u>(438,092)</u>
Cash flows from investing activities:		
Decrease in investments-net	449,759	4,790,579
Purchase of property and equipment	<u>(106,066)</u>	<u>(6,014,422)</u>
Net cash provided by (used in) investing activities	<u>343,693</u>	<u>(1,223,843)</u>
Net (decrease) in cash and cash equivalents	(92,129)	(1,661,935)
Cash and cash equivalents, beginning of year	<u>381,087</u>	<u>2,043,022</u>
Cash and cash equivalents, end of year	<u>\$ 288,958</u>	<u>\$ 381,087</u>

The Art Students League of New York and its Subsidiary

NOTES TO FINANCIAL STATEMENTS

May 31, 2005 and 2004

NOTE 1 - ORGANIZATION

The Art Students League of New York and its wholly owned subsidiary, The American Fine Arts Society, (the "League") were formed in 1875 to establish and maintain an academic school of art, which gives instruction in painting, drawing, graphics, sculpture, applied art and illustration.

For Federal income tax purposes, both organizations are classified as a 501 (c)(3) organizations and are exempt under Section 501(a) of the Internal Revenue code and a similar provision of the New York State income tax laws.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the League have been prepared on the accrual basis of accounting in accordance with principles generally accepted in the United States of America. The significant accounting policies are described below.

A. Basis of Presentation

The net assets of the League are reported as follows:

Unrestricted

Unrestricted net assets are net assets that are neither permanently restricted nor temporarily restricted by the donor-imposed stipulations and are available for the general operations of the League.

Temporarily Restricted

Temporarily restricted net assets include gifts of cash and other assets received with the donor stipulations that limit the use of the donated assets. When the donor restriction expires or a purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

The Art Students League of New York and its Subsidiary

NOTES TO FINANCIAL STATEMENTS (continued)

May 31, 2005 and 2004

NOTE 2 - (continued)

Permanently Restricted

Permanently restricted net assets include funds that have been restricted by the donor to be held in perpetuity.

B. Principles of Consolidation

The consolidated financial statements include the accounts of The Art Students League of New York and its subsidiary The American Fine Arts Society, Inc. (a not for profit organization). The American Fine Arts Society, Inc. ("AFS") is consolidated with the League since the League owns all the outstanding of shares AFS.

C. Cash and Cash Equivalents

The League considers all highly liquid debt instruments purchased with original maturities of three months or less to be cash equivalents.

D. Investment Policy and Objective

Investments in equity securities, mutual funds, corporate bonds, and other investments are measured at fair value in the accompanying statements of financial position. Realized gains and losses (net of investment expenses) and unrealized gains and losses are reported in the statement of activities as an increases or decreases in net assets.

The League's primary investment objective is to maximize total return. The stated goal is to preserve capital that is intended for the League's charitable purposes while generating cash flow to support current operations.

The League, as part of its investment policy, has adopted the Uniform Management of Institutional Fund Act ("UMIFA"). UMIFA allows investment income and unrealized and realized gains and losses from its investing of its permanently restricted net assets to be recorded as temporarily restricted revenue on its statement of activity. These earnings must still be used only for the purposes stipulated by the donors.

The Art Students League of New York and its Subsidiary

NOTES TO FINANCIAL STATEMENTS (continued)

May 31, 2005 and 2004

NOTE 2 - (continued)

E. Inventories

The League operates a store, which sells art supplies and books, and a cafeteria for the benefits of its students. The store's inventory consists of art supplies and books. The cafeteria's inventory consists of food products and related supplies. Inventories are stated at the lower of first-in, first-out cost or market.

F. Tuition and fees

Tuition and fees are usually collected from the students prior to beginning of each monthly session. Upon completion of the course by each student the related tuition and fees are recorded as revenue. Tuition and fees collected for courses commencing after the fiscal year end are recorded as deferred revenues on the statements of financial position.

G. Property and Equipment

The League capitalizes property and equipment at cost. Depreciation of property and equipment is provided on the straight-line method over the expected useful lives of the assets as follows:

Building and improvements	25-50 years
Property and equipment	3-10 years

H. Works of Art

The League maintains a permanent collection of paintings, drawings and sculptures of the League's instructors, students and other artists, which are held for public exhibitions and preserved by the League for this purpose. The permanent collection is not capitalized. The League has acquired other works by donation which may be sold to benefit ongoing programs.

I. In-Kind Contributions

In-kind contributions are reflected in the accompanying financial statements at the estimated fair value at the time of donation.

The Art Students League of New York and its Subsidiary

NOTES TO FINANCIAL STATEMENTS (continued)

May 31, 2005 and 2004

J. Functional Expenses Allocations

The cost of providing the classes and other activities of the League has been summarized on a functional basis in the accompanying statement of activities. Accordingly, certain costs have been allocated to providing classes and to supporting services benefited. Such allocation are determined by management in accordance with donor's stipulations and/or another equitable basis.

K. Prior Year Summarized Comparative Information

Information as of and for the year ended May 31, 2004 is presented for comparative purposes only. The notes to the financial statements and certain activity by net asset classification are not included in this report. Accordingly, such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the League's financial statements as of and for the year ended May 31, 2004, from which the summarized information was derived.

L. Use of Estimates

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

NOTE 3 - CASH AND CASH EQUIVALENTS

The League maintains cash and cash equivalents balances in financial institutions which, at times, may exceed federally insured limits. The League has not experienced any losses in such accounts

The Art Students League of New York and its Subsidiary

NOTES TO FINANCIAL STATEMENTS (continued)

May 31, 2005 and 2004

NOTE 4 - INVESTMENTS

Investments held by the League at May 31, 2005 and 2004 consisted of the following:

	<u>2005</u>		<u>2004</u>	
	<u>Cost</u>	<u>Market</u>	<u>Cost</u>	<u>Market</u>
Managed mutual funds	\$ 4,587,280	\$ 5,173,745	\$ 10,139,987	\$ 10,396,250
Index funds	5,093,879	5,914,715	5,900,932	6,428,237
Corporate stocks and bonds	9,608,416	10,371,433	3,704,426	4,240,723
Other investments - REITS	529,246	713,768	523,235	565,574
	<u>\$ 19,818,821</u>	<u>\$ 22,173,661</u>	<u>\$ 20,268,580</u>	<u>\$ 21,630,784</u>

A summary of net gains on investment transactions are described below:

	<u>2005</u>	<u>2004</u>
Unrealized gains	\$ 992,636	\$ 1,095,055
Realized gains	<u>315,428</u>	<u>625,565</u>
	1,308,064	1,720,620
Less: investment expenses	<u>(34,800)</u>	<u>(37,536)</u>
	<u>\$ 1,273,264</u>	<u>\$ 1,683,084</u>

Investment income is reported in the statement of activities net of investment expenses of \$34,800 and \$37,536 for the years ended May 31, 2005 and 2004, respectively.

NOTE 5 - PROPERTY AND EQUIPMENT, NET

A summary of property and equipment is as follows:

	<u>2005</u>	<u>2004</u>
Buildings and improvements	\$ 9,480,610	\$ 9,448,218
Land and improvements	595,480	581,000
Property and equipment	<u>471,644</u>	<u>412,451</u>
	10,547,734	10,441,669
Less: accumulated depreciation	<u>(1,242,487)</u>	<u>(843,286)</u>
	<u>\$ 9,305,247</u>	<u>\$ 9,598,383</u>

The Art Students League of New York and its Subsidiary

NOTES TO FINANCIAL STATEMENTS (continued)

May 31, 2005 and 2004

NOTE 6 - IN-KIND CONTRIBUTIONS

A summary of in-kind contributions is as follows:

	<u>2005</u>	<u>2004</u>
Space for a fundraising event	\$ 5,300	\$ 5,300
Classroom supplies	<u>1,500</u>	<u>-</u>
	<u>\$ 6,800</u>	<u>\$ 5,300</u>

NOTE 7- PERMANENTLY AND TEMPORARILY RESTRICTED NET ASSETS

Permanently and temporarily restricted net assets are available to satisfy the following purposes:

	<u>2005</u>	<u>2004</u>
<u>Permanently restricted net assets:</u>		
Facility support	\$ 1,972,859	\$ 1,972,859
Scholarships	7,379,970	7,379,970
General support	<u>2,091,146</u>	<u>2,091,146</u>
	<u>\$ 11,443,975</u>	<u>\$ 11,443,975</u>
<u>Temporarily restricted net assets:</u>		
Facility support	\$ 537,754	\$ 479,541
Scholarships	3,026,826	2,542,617
General support	<u>1,488,992</u>	<u>554,368</u>
	<u>\$ 5,053,572</u>	<u>\$ 3,576,526</u>

Certain permanently restricted funds fair market value at May 31, 2005 is less than the donor's original basis because of decline in the stock market prior to 2004. The League has adopted a policy limiting expenditures on these funds until their fair market value equals the donor's basis. The total aggregate amount of deficiencies at May 31, 2005 was \$196,383.

NOTE 8- SUBSEQUENT EVENT

In August, 2005, The American Fine Arts Society, Inc., the wholly owned subsidiary and owner of the building that houses the League 's school in New York City signed an agreement to sell its air rights for approximately \$23,000,000. The agreement required a deposit of \$ 1,000,000 to be made by purchaser upon the execution of the agreement. The balance of the purchase price will be paid at closing which is scheduled to take place before the end of 2005

SCHEDULE OF FUNCTIONAL EXPENSES

For the year ended May 31, 2005 with comparative totals for the year ended May 31, 2004

	Program Services	Supporting Services Management and		2005 Total Expenses	2004 Total Expenses
		General	Fundraising		
Compensation	\$ 757,241	\$ 344,738	\$ 89,438	\$ 1,191,417	\$ 1,103,121
Payroll taxes/ fringe benefits	127,885	48,316	7,937	184,138	178,611
Total compensation and related expenses	885,126	393,054	97,375	1,375,555	1,281,732
Other expenses:					
Instructors	1,249,000	-	-	1,249,000	1,089,458
Models	467,627	-	-	467,627	415,590
Utilities	183,109	-	-	183,109	136,057
Professional and consulting fees	54,913	84,461	-	139,374	56,163
Repairs and maintenance	124,156	-	299	124,455	137,747
Insurance	92,861	12,703	-	105,564	115,406
Merit scholarship	87,000	-	-	87,000	69,998
Office, computer supplies and programming	3,715	76,354	158	80,227	47,614
Catalogue	76,768	-	-	76,768	71,018
Permanent collection	79,866	-	-	79,866	67,283
Classroom supplies	48,739	-	-	48,739	23,336
Member services	43,046	-	-	43,046	14,628
League newsletter	24,139	-	-	24,139	24,292
Archive	9,606	-	-	9,606	17,046
Telephone and internet	18,002	20,714	-	20,714	22,431
Gallery and exhibitions	-	14,473	-	18,002	36,760
Advertising	-	3,264	461	14,473	4,680
Postage	-	-	-	3,725	6,012
Temporary rental of classrooms	-	-	-	-	73,036
Miscellaneous	15,206	95,183	15,656	126,045	92,688
Total other expenses	2,577,753	307,152	16,574	2,901,479	2,521,243
Total expenses before depreciation	3,462,879	700,206	113,949	4,277,034	3,802,975
Depreciation	359,064	39,896	-	398,960	252,533
Total expenses	\$ 3,821,943	\$ 740,102	\$ 113,949	\$ 4,675,994	\$ 4,055,508

This schedule should be read in conjunction with the accompanying financial statements and the notes thereto.

Art Students League of New York and its Subsidiary

SCHEDULES OF ART STORE AND CAFETERIA OPERATIONS

For the years ended May 31, 2005 and 2004

	<u>2005</u>	<u>2004</u>
Art store		
Revenues	\$ 561,988	\$ 430,439
Cost of operations:		
Inventory, beginning of year	103,103	44,596
Purchases	<u>381,641</u>	<u>307,202</u>
	484,744	351,798
Inventory, end of year	<u>138,508</u>	<u>103,103</u>
Cost of goods sold	<u>346,236</u>	<u>248,695</u>
Excess	215,752	181,744
Other expenses:		
Compensation	100,599	100,590
Payroll taxes/fringe benefits	16,191	18,808
Miscellaneous	<u>16,346</u>	<u>13,680</u>
Total other expenses	<u>133,136</u>	<u>133,078</u>
Excess of revenue over expenses	<u>\$ 82,616</u>	<u>\$ 48,666</u>
Cafeteria		
Revenues	\$ 171,059	\$ 135,302
Cost of operations:		
Inventory, beginning of year	3,208	1,645
Purchases	<u>72,992</u>	<u>59,260</u>
	76,200	60,905
Inventory, end of year	<u>3,632</u>	<u>3,208</u>
Cost of goods sold	<u>72,568</u>	<u>57,697</u>
Excess	98,491	77,605
Other expenses:		
Compensation	78,410	45,751
Payroll taxes/fringe benefits	9,819	6,413
Miscellaneous	19,354	16,603
Depreciation	<u>239</u>	<u>156</u>
Total other expenses	<u>107,822</u>	<u>68,923</u>
Excess (deficiency) of revenues over expenses	<u>\$ (9,331)</u>	<u>\$ 8,682</u>

This schedule should be read in conjunction with the accompanying financial statements and notes thereto.