

*ARKANSAS STATE
UNIVERSITY FOUNDATION, INC.*

Financial Statements as of and for the
Years Ended June 30, 2016 and 2015

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Arkansas State University Foundation, Inc.
Jonesboro, Arkansas

We have audited the accompanying financial statements of Arkansas State University Foundation, Inc. (the Foundation), which comprise the statements of financial position as of June 30, 2016 and 2015, and the related statements of activities and changes in net assets and 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.

Auditor's 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 the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Arkansas State University Foundation, Inc. as of June 30, 2016 and 2015, 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.

Jones & Company, LTD

Jones & Company, Ltd.
Jonesboro, Arkansas

September XX, 2016

Arkansas State University Foundation, Inc.
Statements of Financial Position

ASSETS

	June 30,	
	2016	2015
Cash	\$ 256,720	\$ 536,805
Repurchase agreements	5,947,903	5,543,759
Certificates of deposit	4,977,011	3,713,723
Prepaid expenses	59,474	19,468
Unconditional promises to give, net	1,860,793	1,527,983
Short-term investment, at fair value	85,690	83,997
Long-term investments, at fair value	54,414,788	55,419,584
Cash surrender value of life insurance	5,861	6,648
Property and equipment, net	934,840	985,017
Other assets	2,557	107,269
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Total Assets	\$ 68,545,637	\$ 67,944,253

LIABILITIES & NET ASSETS

Liabilities		
Accounts payable	\$ 97,137	\$ 92,925
Annuity obligations	3,239	27,956
Due to ASU campuses	410,506	517,256
Due to Alumni Association	597	-
Amounts held on behalf of Arkansas State University related entities	11,668,798	11,923,085
	<hr/>	<hr/>
Total Liabilities	\$ 12,180,277	\$ 12,561,222
Net Assets		
Unrestricted	\$ 2,264,840	\$ 2,458,885
Temporarily restricted	8,426,855	8,159,485
Permanently restricted	45,673,665	44,764,661
	<hr/>	<hr/>
Total Net Assets	\$ 56,365,360	\$ 55,383,031
	<hr/>	<hr/>
Total Liabilities and Net Assets	\$ 68,545,637	\$ 67,944,253

The accompanying notes are an integral part of these financial statements.

Arkansas State University Foundation, Inc.
Statement of Activities and Changes in Net Assets
For the Year Ended June 30, 2016

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenue and other support				
Contributions	\$ 84,763	\$ 3,006,538	\$ 3,020,180	\$ 6,111,481
Contributed services	211,862	-	-	211,862
Investment return, net	45,122	1,174,986	(2,071,744)	(851,636)
Other income	536,193	172,512	-	708,705
Net assets released from restrictions	4,127,995	(4,127,995)	-	-
	<u>\$ 5,005,935</u>	<u>\$ 226,041</u>	<u>\$ 948,436</u>	<u>\$ 6,180,412</u>
 Expenses and Losses				
Program services				
Academic activities	\$ 692,076	\$ -	\$ -	\$ 692,076
Administrative	274,090	-	-	274,090
Student activities	61,272	-	-	61,272
Transfers to Arkansas State University	3,123,598	-	-	3,123,598
 Supporting services				
Management and general	461,776	-	-	461,776
Fundraising	581,406	-	-	581,406
Change in split-interest agreements	-	-	3,865	3,865
	<u>\$ 5,194,218</u>	<u>\$ -</u>	<u>\$ 3,865</u>	<u>\$ 5,198,083</u>
 Increase (decrease) in net assets	<u>\$ (188,283)</u>	<u>\$ 226,041</u>	<u>\$ 944,571</u>	<u>\$ 982,329</u>
 Net assets at beginning of the year	\$ 2,458,885	\$ 8,159,485	\$ 44,764,661	\$ 55,383,031
 Reclassification and internal transfers	(5,762)	41,329	(35,567)	-
	<u>\$ 2,453,123</u>	<u>\$ 8,200,814</u>	<u>\$ 44,729,094</u>	<u>\$ 55,383,031</u>
 Net assets at the end of the year	<u>\$ 2,264,840</u>	<u>\$ 8,426,855</u>	<u>\$ 45,673,665</u>	<u>\$ 56,365,360</u>

The accompanying notes are an integral part of these financial statements.

Arkansas State University Foundation, Inc.
Statement of Activities and Changes in Net Assets
For the Year Ended June 30, 2015

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenue and other support				
Contributions	\$ 96,996	\$ 2,373,137	\$ 1,892,659	\$ 4,362,792
Contributed services	285,619	-	-	285,619
Support from the Arkansas State University Real Estate Foundation	-	-	1,981,310	1,981,310
Investment return, net	50,763	1,403,880	(460,867)	993,776
Grant income	-	74,997	-	74,997
Other income	533,048	368,528	-	901,576
Net assets released from restrictions	3,879,005	(3,879,005)	-	-
	<u>\$ 4,845,431</u>	<u>\$ 341,537</u>	<u>\$ 3,413,102</u>	<u>\$ 8,600,070</u>
Expenses and Losses				
Program services				
Academic activities	\$ 736,947	\$ -	\$ -	\$ 736,947
Administrative	261,049	-	-	261,049
Student activities	66,264	-	-	66,264
Transfers to Arkansas State University	3,015,738	-	-	3,015,738
Supporting services				
Management and general	488,708	-	-	488,708
Fundraising	323,287	-	-	323,287
Change in split-interest agreements	-	-	35,458	35,458
	<u>\$ 4,891,993</u>	<u>\$ -</u>	<u>\$ 35,458</u>	<u>\$ 4,927,451</u>
Increase (decrease) in net assets	<u>\$ (46,562)</u>	<u>\$ 341,537</u>	<u>\$ 3,377,644</u>	<u>\$ 3,672,619</u>
Net assets at beginning of the year	\$ 2,519,182	\$ 7,867,701	\$ 41,980,436	\$ 52,367,319
Reclassification and internal transfers Transfer of assets to Red Wolves Foundation	(13,735)	(49,753)	63,488	-
	-	-	(656,907)	(656,907)
	<u>\$ 2,505,447</u>	<u>\$ 7,817,948</u>	<u>\$ 41,387,017</u>	<u>\$ 51,710,412</u>
Net assets at the end of the year	<u>\$ 2,458,885</u>	<u>\$ 8,159,485</u>	<u>\$ 44,764,661</u>	<u>\$ 55,383,031</u>

The accompanying notes are an integral part of these financial statements.

Arkansas State University Foundation, Inc.
Statements of Cash Flows
For the Years Ended

	June 30,	
	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ 982,329	\$ 3,672,619
Adjustments to reconcile change in net assets to net cash (used for) provided by operating activities:		
Depreciation expense	50,177	58,249
Contributions restricted for long-term investment	(3,020,180)	(1,892,659)
Net realized and unrealized loss on investments	2,285,022	865,251
Change in value of split-interest agreements	3,865	36,000
Changes in:		
Unconditional promises to give	(332,810)	(96,523)
Cash surrender value of life insurance	787	507
Prepaid expenses	(40,006)	(13,639)
Other assets	(1,457)	(106,170)
Accounts payable	4,212	50,137
Annuity obligations	(24,717)	(60,343)
Funds held for others	(137,466)	918,810
Net cash (used for) provided by operating activities	\$ (230,244)	\$ 3,432,239
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of investments	\$ (293,678)	\$ (2,407,296)
Proceeds from sale of investments	241,577	238,211
Purchases of certificates of deposit	(1,245,000)	-
Net cash used for investing activities	\$ (1,297,101)	\$ (2,169,085)
CASH FLOWS FROM FINANCING ACTIVITIES		
Contributions restricted for long-term investments	\$ 3,020,180	\$ 1,892,659
Interest and dividends restricted for reinvestment	(1,368,776)	(2,030,667)
Transfer of assets to Red Wolves Foundation, Inc.	-	(656,907)
Net cash provided by (used for) financing activities	\$ 1,651,404	\$ (794,915)
NET CHANGE IN CASH	\$ 124,059	\$ 468,239
Cash and repurchase agreement, beginning of the year	6,080,564	5,612,325
Cash and repurchase agreement, end of the year	\$ 6,204,623	\$ 6,080,564
<i>Supplemental Disclosures for Cash Flows</i>		
Cash paid for interest	\$ -	\$ 37

The accompanying notes are an integral part of these financial statements.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

1) NATURE OF BUSINESS

Organization and Nature of Operations

Arkansas State University Foundation, Inc. (the Foundation) is an Arkansas corporation chartered March 7, 1977. The Foundation's primary purpose is to support the Arkansas State University System (the University) by advancing higher education, research and allied supportive activities through the promotion of private financial support. The Foundation is considered a component unit of Arkansas State University and is presented in the University's financial statements.

2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Advertising

Advertising costs are charged to operations when incurred. Advertising expense for the years ended June 30, 2016 and 2015 was \$28,825 and \$25,567 respectively.

Basis of Reporting

The financial statements of the Foundation have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). Under this method of accounting, revenue is recognized when earned and when the amount and timing of the revenue can be reasonably estimated. Expenses are recognized as they occur.

Basis of Presentation

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board (FASB), Accounting Standards Codification (ASC) 958-210; *Presentation of Financial Statements of Not-For-Profit Entities*. Under FASB ASC 958-210, the Foundation is required to report information regarding its financial position and activities according to three classes of net assets: permanently restricted net assets, temporarily restricted net assets, and unrestricted net assets.

Permanently restricted net assets – net assets subject to donor-imposed stipulations that the net assets be maintained permanently by the Foundation. Generally, the donors of these assets permit the Foundation to use all or part of the income earned on related investments for general or specific purposes in support of the University. The Foundation is allowed to expend principal in accordance with the spending policy established by the Foundation's Board of Directors (see Note 6).

Temporarily restricted net assets – net assets subject to donor-imposed stipulations that may or will be met by actions of the Foundation and/or passage of time. When a donor restriction expires, this is, when a stipulated time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and are reported in the statements of activities as net assets released from restriction. When the restrictions on contributions are met in the same period that the contribution is received, the contribution is reported in the statements of activities as temporarily restricted revenues and as net assets released from restrictions.

Unrestricted net assets – net assets which represent resources generated from operations or that are not subject to donor-imposed stipulations.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

2) **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

Basis of Presentation (continued)

Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Amounts received that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support that increases these net asset classes.

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 stipulations or by law. Expirations of restrictions on net assets (i.e. the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Foundation considers cash, repurchase agreements and certificates of deposit with an original maturity of three months or less to be cash equivalents. As of June 30, 2016, cash equivalents totaling \$5,067,715 have been restricted by donor imposed stipulations and cash equivalents of \$1,070,946 are being held under agency agreements. As of June 30, 2015, cash equivalents totaling \$4,909,445 have been restricted by donor imposed stipulations and cash equivalents of \$976,910 are being held under agency agreements.

Contributions

Contributions, including unconditional promises to give, are recorded as received or promised and classified as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. Unconditional promises to give due within one year are recorded at net realizable value. Unconditional promises to give due in subsequent years are reported at the present value of their net realizable value, using risk-free interest rates applicable to the years in which the promises are to be received.

Date of Management Review

The Foundation has evaluated events and transactions for potential recognition or disclosure in the financial statements through September XX, 2016, the date the report was available for release. No subsequent events have been recognized or disclosed.

Donated Noncash Assets and Donated Services

Donated noncash assets are recorded at their fair values in the period received. Contributions of donated services that create or enhance non-financial assets or that require specialized skills are recorded at their fair values in the period received. These donated services are provided by individuals possessing those skills and would typically need to be purchased if not provided by donation. The donated services were used for the management and administration of the Foundation.

Income Taxes

The Foundation is exempt from federal income tax under the provisions of section 501(a) of Internal Revenue Code as an organization described in section 501(c)(3). Therefore, no provision for federal or state income taxes has been made.

The Foundation files income tax returns in the U.S. federal jurisdiction.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income Taxes (continued)

The Foundation has reviewed and evaluated tax positions in accordance with the provisions of FASB ASC 740-10-55, *Accounting for Uncertainty in Income Taxes*, which provides a financial statement recognition threshold and measurement attribute for a tax position taken or to be taken in a tax return. The Foundation does not feel any tax positions meet the requirements for reporting under this standard.

Impairment of Long-lived Assets

Long-lived assets, such as land, buildings, and equipment, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If circumstances require a long-lived asset be tested for possible impairment, the Foundation first compares undiscounted cash flows expected to be generated by an asset to the carrying value of the asset. If the carrying value of the long-lived asset is not recoverable on an undiscounted cash flow basis, an impairment is recognized to the extent that the carrying value exceeds its fair value. Fair value is determined through various valuation techniques including discounting cash flow models and third-party independent appraisals, as considered necessary. No impairments were noted at June 30, 2016.

Investments

Investments consist primarily of marketable securities. Investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair value with gains and losses included in the statements of activities. Restricted investment income and investment gains whose restrictions are met in the same reporting period are shown as unrestricted support.

Liquidity

Assets are presented in the accompanying statements of financial position according to their nearness of conversion to cash and liabilities according to the nearness of their maturity and resulting use of cash.

Property and Equipment

Donations of property and equipment are recorded as support at their estimated fair value. Such donations are reported as unrestricted support unless the donor has restricted the donated asset to a specific purpose. The Foundation capitalizes all expenditures in excess of \$2,500 for property and equipment at cost. When property and equipment are retired, the related cost and accumulated depreciation is removed from the statement of financial position and any resultant gain or loss is recorded. Repairs and maintenance costs are expensed as incurred. Property and equipment are depreciated using the straight-line method over estimated useful lives as follows:

Buildings	30 years
Vehicles	5 years
Computer Systems	3 years
Furnishings and equipment	3 – 7 years

Use of Estimates

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

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

2) **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

Recent Accounting Pronouncements

The FASB has issued ASU No. 2015-07, *Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*. The amendment applies to reporting entities that elect to measure the fair value of an investment using the net asset value per share (or its equivalent) practical expedient. Currently, investments valued using the practical expedient are categorized within the fair value hierarchy on the basis of whether the investment is redeemable with the investee at net asset value on the measurement date, never redeemable with the investee at net asset value, or redeemable with the investee at net asset value at a future date. For investments that are redeemable with the investee at a future date, a reporting entity must consider the length of time until those investments become redeemable to determine the classification within the fair value hierarchy. The amendment removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. This ASU also removes the requirement to make certain disclosures for all investments that are eligible to be measured at fair value using the net asset value per share practical expedient. Rather, those disclosures are limited to investments for which the entity has elected to measure the fair value using that practical expedient. This ASU is effective for the Foundation for their fiscal year beginning after December 15, 2016 and requires retrospective treatment to all periods presented. Management is reviewing the requirements of this ASU but believes the only impact on the financial statements will be on disclosure of certain investments recorded at the net asset value practical expedient.

The FASB and other entities have issued other certain new or modifications to, or interpretations of, existing accounting guidance. The Foundation has considered the new pronouncements that altered U.S. GAAP, and does not believe that any other new or modified guidance will have a material impact on the Foundation's reported financial position or activities in the near term.

Reclassifications

Certain reclassifications have been made to the 2015 financial statements to conform with the 2016 presentation. These reclassifications had no effect on the Foundation's change in net assets.

3) **REPURCHASE AGREEMENT**

The Foundation has two agreements with two different financial institutions to sweep funds from its checking accounts into repurchase agreements. The funds are swept daily and are secured by U.S. treasury obligations, U.S. government securities, and municipal securities. These funds are considered cash equivalents for the statements of cash flows.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

4) UNCONDITIONAL PROMISES TO GIVE

Unconditional promises to give at June 30, 2016 and 2015 are as follows:

Receivable in:	<u>2016</u>	<u>2015</u>
Less than one year	\$ 7,250	\$ 33,480
One to five years	2,071,485	1,750,647
After five years	-	18,157
Total unconditional promises to give	<u>\$ 2,078,735</u>	<u>\$ 1,802,284</u>
Less unamortized discount	112,096	184,486
Less allowance for uncollectible promises	105,846	89,815
Net unconditional promises to give	<u><u>\$ 1,860,793</u></u>	<u><u>\$ 1,527,983</u></u>

Unconditional promises to give with due dates extending beyond one year are discounted using Treasury bill rates for similar term investments. The applicable rates at June 30, 2016 were 0.55% to 1.49%.

As of June 30, 2016, unconditional promises to give totaling \$1,713,458 have been restricted by donor stipulations. Also, two donors represented more than 10% of total promises to give at June 30, 2016. Donor A represented 24% and donor B represented 19%.

5) INVESTMENTS

The market values of the Foundation's portfolio of investments as of June 30, 2016 and 2015 are as follows:

	<u>2016</u>	<u>2015</u>
Money market funds	\$ 191,337	\$ 23,458
U.S. equity mutual funds	26,268,445	27,483,386
International equities mutual funds	4,728,919	5,557,416
Fixed income investments	18,613,992	18,093,438
Guaranteed investment contract	85,690	83,997
Partnership interests	4,612,095	4,261,886
	<u><u>\$ 54,500,478</u></u>	<u><u>\$ 55,503,581</u></u>

The Foundation provides for investments in various investment securities, which are in general exposed to various risks, such as interest rate, credit and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term, and those changes could materially affect the amounts reported in the statements of activities.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

5) INVESTMENTS (continued)

The following schedules summarizes the return on investments and interest bearing cash deposits for the years ended June 30, 2016 and 2015:

	2016			
	Net Unrealized/Realized Gains (Losses)	Investment Income (Expense)	Interest Income	Total
U.S. equity mutual funds	\$ (1,091,452)	\$ 232,698	\$ -	\$ (858,754)
Fixed income investments	(361,949)	1,137,701	-	775,752
International equities mutual funds	(966,964)	90,900	-	(876,064)
Guaranteed investment contract	-	-	1,692	1,692
Partnership interests	171,644	(117,675)	-	53,969
Money market funds	-	1	-	1
Assets held in trust	(16,646)	5,836	-	(10,810)
Certificates of deposit	-	-	30,242	30,242
Cash	-	-	32,336	32,336
	<u>\$ (2,265,367)</u>	<u>\$ 1,349,461</u>	<u>\$ 64,270</u>	<u>\$ (851,636)</u>

	2015			
	Net Unrealized/Realized Gains (Losses)	Investment Income (Expense)	Interest Income	Total
U.S. equity mutual funds	\$ 1,194,927	\$ 146,467	\$ -	\$ 1,341,394
Fixed income investments	(885,417)	1,255,253	-	369,836
International equities mutual funds	(215,737)	85,787	-	(129,950)
Guaranteed investment contract	-	-	1,826	1,826
Partnership interests	(740,488)	71,696	-	(668,792)
Money market funds	-	4	-	4
Assets held in trust	14,064	14,241	211	28,516
Certificates of deposit	-	-	12,309	12,309
Cash	-	-	38,633	38,633
	<u>\$ (632,651)</u>	<u>\$ 1,573,448</u>	<u>\$ 52,979</u>	<u>\$ 993,776</u>

Investment fees included in investment income totaled \$714,630 and \$611,710 for the years ended June 30, 2016 and 2015, respectively.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

5) INVESTMENTS (continued)

The following schedules summarize the investment return and its classification in the statements of activities for the years ended June 30, 2016 and 2015:

	2016			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest income	\$ 52,539	\$ 11,731	\$ -	\$ 64,270
Investment income (expense)	11,406	1,167,829	170,226	1,349,461
Net realized/ unrealized gains (losses)	(18,823)	(4,574)	(2,241,970)	(2,265,367)
Total investment return	\$ 45,122	\$ 1,174,986	\$ (2,071,744)	\$ (851,636)
	2015			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest income	\$ 42,931	\$ 10,048	\$ -	\$ 52,979
Investment income (expense)	13,104	1,395,108	165,236	1,573,448
Net realized/ unrealized gains (losses)	(5,272)	(1,276)	(626,103)	(632,651)
Total investment return	\$ 50,763	\$ 1,403,880	\$ (460,867)	\$ 993,776

6) ENDOWMENTS

FASB ASC 958-205, *“Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds”* provides guidance on the net asset classification of donor-restricted endowment funds for a nonprofit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). FASB ASC 958-205 also requires additional disclosures about an organization’s endowment funds (both donor restricted endowment funds and board-designated endowment funds) whether or not the organization is subject to UPMIFA.

The State of Arkansas enacted UPMIFA effective February 26, 2009, the provisions of which apply to endowment funds existing on or established after that date. The Foundation has adopted FASB ASC 958-205. The Board of Directors, on the advice of legal counsel, has determined that the majority of the Foundation’s permanently restricted net assets meet the definition of endowment funds under UPMIFA.

The Foundation’s endowment consists of approximately 324 individual funds established for a variety of purposes. As required by U.S. GAAP, net assets associated with endowment funds are classified and reported based on donor-imposed restrictions.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

6) ENDOWMENTS (continued)

Interpretation of Relevant Law: The Board of Directors of the Foundation has interpreted Senate Bill 254 UPMIFA as requiring the Board to use reasonable care, skill, and caution as exercised by a prudent investor in considering the investment management and expenditures of endowment funds.

In accordance with UPMIFA, the Board may expend so much of an endowment fund as the Board determines to be prudent for the uses and purposes for which the endowment fund is established, consistent with the goal of conserving the long-term purchasing power of the endowment fund. The Board considered the following factors in making its determination:

- 1) The purpose of the Foundation;
- 2) The intent of the donor of the endowment fund;
- 3) The terms of the applicable instrument;
- 4) The long-term and short-term needs of the Foundation and the University in carrying out its purposes;
- 5) General economic conditions;
- 6) The possible effect of inflation or deflation;
- 7) The other resources of the Foundation and the University; and,
- 8) Perpetuation of the endowment.

As a result of this interpretation, the Board classifies as permanently restricted net assets (a) the original value of gifts donated to a permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) the remaining amount of investment return less appropriated expenditures at the end of each year. However, by Board policy, any appreciation is considered an asset of the individual endowment fund and is not appropriated for general Foundation use.

Investment Return Objectives, Risk Parameters and Strategies: The Foundation has adopted investment and spending policies, approved by the Board of Directors, for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment funds while also maintaining the purchasing power of those endowment assets over the long-term. Accordingly, the investment process seeks to achieve an after-cost total real rate of return, including investment income as well as capital appreciation, which exceeds the annual distribution with acceptable levels of risk. Endowment assets are invested in a well-diversified asset mix, which includes equity and debt securities, real estate funds, and partnership interests that is intended to result in a consistent inflation-protected rate of return that has sufficient liquidity to make an annual distribution of 5%, while growing the funds if possible. Therefore, the Foundation expects its endowment assets, over time, to produce an average rate of return of approximately 8% annually. Actual returns in any given year may vary from this amount. Investment risk is measured in terms of the total endowment fund; investment assets and allocation between asset classes and strategies are managed to not expose the fund to unacceptable levels of risk.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

6) **ENDOWMENTS (continued)**

Spending Policy: The Foundation has a policy of appropriating for distribution each year 5% of its endowment fund's average fair value of the prior five calendar year-ends for most of its endowments. In establishing this policy, the Foundation considered the long-term expected return on its investment assets, the nature and duration of the individual endowment funds, many of which must be maintained in perpetuity because of donor-restrictions, and the possible effects of inflation. The Foundation expects the current spending policy to allow its endowment funds to grow at an average nominal rate of 3% annually, which is consistent with the Foundation's objective to maintain the purchasing power of the endowment assets as well as to provide additional real growth through investment return.

Distributions for endowment funds three years old or less are limited to actual cash yield; endowment funds less than \$10,000 will not be allowed to spend; and any "underwater" endowment funds will be limited to 3% of the rolling five year average fair value measured at calendar year-end.

Endowment net assets composition by type of fund as of June 30, 2016 and 2015 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowments</u>
Donor-restricted endowment funds June 30, 2016	\$ -	\$ -	\$ 45,673,665	\$ 45,673,665
Donor-restricted endowment funds June 30, 2015	\$ -	\$ -	\$ 44,764,661	\$ 44,764,661

Changes in endowment net assets as of June 30, 2016 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total Net Endowments</u>
Net endowment assets, beginning of year	\$ -	\$ -	\$ 44,764,661	\$ 44,764,661
Contributions	-	-	3,020,180	3,020,180
Investment income	-	1,168,388	170,226	1,338,614
Net depreciation	-	-	(2,241,970)	(2,241,970)
Appropriation of endowments for expenditure	-	(1,168,388)	-	(1,168,388)
Change in split interest	-	-	(3,865)	(3,865)
Reclassification	-	-	(35,567)	(35,567)
Net endowment assets, end of year	\$ -	\$ -	\$ 45,673,665	\$ 45,673,665

Funds with Deficiencies: As a result of market declines for certain recently established endowments, the fair value of certain donor-restricted endowments was less than the historical cost value (original gift/book value) of such funds ("underwater") by \$111,873 and \$3,286 at June 30, 2016 and 2015, respectively.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

7) PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	<u>2016</u>	<u>2015</u>
Land	\$ 110,093	\$ 110,093
Vehicles	105,986	105,986
Building	1,088,150	1,088,150
Furnishings and equipment	142,615	142,615
Computer systems	12,755	12,755
	<u>\$ 1,459,599</u>	<u>\$ 1,459,599</u>
Accumulated depreciation	524,759	474,582
	<u>\$ 934,840</u>	<u>\$ 985,017</u>

Depreciation expense was \$50,177 and \$58,249 for the fiscal years ended June 30, 2016 and 2015, respectively.

8) SPLIT INTEREST AGREEMENTS

The Foundation accepts gifts subject to split interest agreements. These gifts may be in the form of annuities, life estates, or charitable remainder trusts. At the time of receipt, a gift is recorded based upon fair value of assets donated less any applicable liabilities. Liabilities include the present value of projected future distributions to the annuity or trust beneficiaries and are discounted using discount rates based on U.S. treasury rates and actuarial assumptions in effect when the agreement originated. The terms of the agreements vary from payments made to life income beneficiary/recipients ranging from an annual amount equal to 5% of the net fair market value of trust assets determined as of the first day of the taxable year to fixed dollar amounts per year ranging from \$7,000 to \$9,000. Assets held under split interest agreements are included in long-term investments totaled \$148,526 and \$544,579 at June 30, 2016 and 2015, respectively.

9) TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes at June 30:

	<u>2016</u>	<u>2015</u>
Facilities	\$ 1,672,474	\$ 1,775,388
Institutional support	4,834,582	4,362,562
Faculty/Staff support	69,136	71,903
Research	992	1,400
Scholarships and awards	1,190,129	1,056,385
Student services	54,201	51,013
Community outreach	605,341	840,834
Periods after June 30,	<u>\$ 8,426,855</u>	<u>\$ 8,159,485</u>

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

9) TEMPORARILY RESTRICTED NET ASSETS (continued)

Net assets were released from donor restrictions by incurring expenses satisfying the purpose or time restrictions specified by donors as follows:

	2016	2015
Purpose for restriction accomplished:		
Academia and student activities	\$ 1,380,349	\$ 1,205,028
ASU colleges and departments	2,747,646	2,673,977
Total restrictions released	\$ 4,127,995	\$ 3,879,005

10) PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets are required to be invested in perpetuity. In accordance with donor stipulations, net appreciation in the value of endowed funds, less the amount equal to the spending rate as determined by the Board, is to be retained permanently. Permanently restricted net assets are designated for the following purposes at June 30:

	2016	2015
Facilities	\$ 4,711,320	\$ 4,912,432
Institutional support	5,521,525	5,227,933
Faculty/Staff support	8,492,757	8,327,983
Scholarships and awards	24,375,001	24,253,805
Student services	396,763	303,445
Community Outreach	2,176,299	1,739,063
	\$ 45,673,665	\$ 44,764,661

11) FAIR VALUES OF FINANCIAL INSTRUMENTS

FASB ASC 820-10, *Fair Value Measurements* (ASC 820-10), provides a framework for measuring fair value under U.S. GAAP. ASC 820-10 defines fair value as the exchange prices that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820-10 requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs. Observable inputs are inputs that market participants operating within the same marketplace as the Foundation would use in pricing the Foundation's asset or liability based on independently derived and observable market data. Unobservable inputs are inputs that cannot be sourced from a broad active market in which assets or liabilities identical or similar to those of the Foundation are traded. ASC 820-10 establishes a fair value hierarchy, which prioritizes the valuation inputs into three broad levels.

Level 1 – Quoted prices in active markets for identical assets the Foundation has the ability to access at the measurement date. These types of quoted prices would include publicly traded equity securities and mutual funds traded on a major exchange.

Level 2 – Inputs to the valuation methodology include:

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

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

11) FAIR VALUES OF FINANCIAL INSTRUMENTS (continued)

If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 – Pricing inputs that are unobservable and significant to the fair value measurement. Inputs were not developed by the Foundation for any of these assets.

An asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The availability of observable market data is monitored to assess the appropriate classification of financial instruments within the fair value hierarchy. Changes in economic conditions or model-based valuation techniques may require the transfer of financial instruments from one fair value level to another. In such instances, the transfer is reported at the beginning of the reporting period.

We have evaluated the significance of transfers between levels based upon the nature of the financial instruments and size of the transfer relative to total net assets available for benefits. For the years ended June 30, 2016 and 2015, there were no transfers in or out of levels 1, 2, or 3.

The following methods and assumptions were used by the Foundation in estimating the fair value of its financial instruments, which are reported at fair value:

Certificates of deposits: The carrying amounts reported in the statements of financial position approximate fair value because the stated rates approximate current prevailing rates.

Money market funds and repurchase agreements: These funds included investment in short-term U.S. Treasury obligations with maturities of less than one year, overnight bank deposits and other short-term highly liquid debt securities. The fair values of some of these fund investments were estimated using the net asset value per share of the respective investments provided by the fund manager.

Equity securities and mutual funds: Mutual funds represent investments with various investment managers. The fair value of these investments is determined by reference to the fund's underlying assets, which are principally marketable equity and fixed income securities. Shares held in mutual funds traded on national securities exchanges are valued at the net asset value.

Partnership interests: Given the absence of market quotations, the fair value is estimated at the net asset value of the units held by the Foundation at year end, as reported by the investment manager and within valuation guidelines stipulated in respective investment agreements.

Bonds and treasuries: Valued based upon quotes from independent pricing vendors based upon independent pricing models or other model-based valuation techniques such as the present value of the stream of expected cash flows adjusted for the securities credit rating and other factors such as credit loss assumptions.

Guaranteed investment contract: Valued at fair value by the insurance company by discounting the related cash flows based on current yields of similar instruments with comparable durations considering the credit-worthiness of the issuer.

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

11) FAIR VALUES OF FINANCIAL INSTRUMENTS (continued)

The preceding methods may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Foundation believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following table sets forth, by level, within the fair value hierarchy, amounts recorded in the Foundation's financial statements at fair value as of June 30, 2016:

	Level 1	Level 2	Level 3	Total
Mutual funds:				
U.S. equity mutual funds	\$ 26,268,445	\$ -	\$ -	\$ 26,268,445
Fixed income investments	5,808,987	-	-	5,808,987
International equities	4,728,919	-	-	4,728,919
Bonds and treasuries	12,805,005	-	-	12,805,005
Guaranteed investment contract	-	-	85,690	85,690
Partnership interests:				
Private real estate	-	-	2,812,745	2,812,745
Private equity	-	-	1,030,162	1,030,162
Mezzanine debt	-	-	761,527	761,527
Energy	-	-	7,661	7,661
Repurchase agreements	-	5,947,903	-	5,947,903
Certificates of deposit	-	4,977,011	-	4,977,011
Money market funds	191,337	-	-	191,337
Other	-	-	5,861	5,861
Total	<u>\$ 49,802,693</u>	<u>\$ 10,924,914</u>	<u>\$ 4,703,646</u>	<u>\$ 65,431,253</u>

The following table sets forth, by level, within the fair value hierarchy, amounts recorded in the Foundation's financial statements at fair value as of June 30, 2015:

	Level 1	Level 2	Level 3	Total
Mutual funds:				
U.S. equity mutual funds	\$ 27,346,187	\$ -	\$ -	\$ 27,346,187
Fixed income investments	18,093,438	-	-	18,093,438
Domestic small cap equities	137,199	-	-	137,199
International equities	5,557,416	-	-	5,557,416
Guaranteed investment contract	-	-	83,997	83,997
Partnership interests:				
Private real estate	-	-	2,905,260	2,905,260
Private equity	-	-	1,356,626	1,356,626
Repurchase agreements	-	5,543,759	-	5,543,759
Certificates of deposit	-	3,713,723	-	3,713,723
Money market funds	23,458	-	-	23,458
Other	-	-	6,648	6,648
Total	<u>\$ 51,157,698</u>	<u>\$ 9,257,482</u>	<u>\$ 4,352,531</u>	<u>\$ 64,767,711</u>

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

11) FAIR VALUES OF FINANCIAL INSTRUMENTS (continued)

The table below sets forth a summary of changes in the fair value of the Foundation's level 3 assets for the fiscal year ended June 30, 2016:

	<u>Other</u>	<u>Guaranteed Investment Contracts</u>	<u>Partnership Interests</u>	<u>Total</u>
Balance, July 1, 2015	\$ 6,648	\$ 83,997	\$ 4,261,886	\$ 4,352,531
Return of capital	-	-	(297,399)	(297,399)
Purchases	-	-	581,168	581,168
Investment income (expense)	-	1,693	(144,866)	(143,173)
Net realized/unrealized gains (losses)	(787)	-	211,306	210,519
Balance, June 30, 2016	<u>\$ 5,861</u>	<u>\$ 85,690</u>	<u>\$ 4,612,095</u>	<u>\$ 4,703,646</u>
Unrealized gains (losses)	<u>\$ (787)</u>	<u>\$ -</u>	<u>\$ 210,718</u>	<u>\$ 209,931</u>

The table below sets forth a summary of changes in the fair value of the Foundation's level 3 assets for the fiscal year ended June 30, 2015:

	<u>Other</u>	<u>Guaranteed Investment Contracts</u>	<u>Partnership Interests</u>	<u>Total</u>
Balance, July 1, 2014	\$ 7,155	\$ 87,171	\$ 3,195,310	\$ 3,289,636
Return of capital	-	(5,000)	(197,827)	(202,827)
Purchases	-	-	808,404	808,404
Investment income (expense)	-	1,826	(35,121)	(33,295)
Net realized/unrealized gains (losses)	(507)	-	491,120	490,613
Balance, June 30, 2015	<u>\$ 6,648</u>	<u>\$ 83,997</u>	<u>\$ 4,261,886</u>	<u>\$ 4,342,531</u>
Unrealized gains (losses)	<u>\$ (507)</u>	<u>\$ -</u>	<u>\$ 491,120</u>	<u>\$ 490,613</u>

12) INVESTMENTS VALUED AT NET ASSET VALUE

For investments in entities that calculate net asset value ("NAV") or its equivalent whose fair value is not readily determinable, the following table provides additional information about the probability of investments being sold at amounts different from the NAV per share at June 30, 2016:

	<u>Fair Value</u>	<u>Unfunded Commitments</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Partnership interest:				
Private real estate	\$ 2,812,745	\$ -	N/A	N/A
Private equity	\$ 1,030,162	\$ 799,805	N/A	N/A
Mezzanine debt	\$ 761,527	\$ 482,037	N/A	N/A
Energy	\$ 7,661	\$ 11,739	N/A	N/A

Arkansas State University Foundation, Inc.
Notes to the Financial Statements

13) AMOUNTS HELD ON BEHALF OF ARKANSAS STATE UNIVERSITY RELATED ENTITIES

The Foundation acts in an agency capacity for funds received and held for Arkansas State University System; Arkansas State University – Jonesboro; Arkansas State University – Beebe; Arkansas State University Alumni Association; and Arkansas State University Red Wolves Foundation, Inc. (the “Agencies”). The Foundation has no discretion over the use of these funds. Any resources received in connection with such agency transactions are recorded as liabilities rather than contributions. No revenue or expense is recorded on the statements of activities for activity in these funds.

14) CONCENTRATIONS

Substantially all of the Foundation’s long-term financial instruments are held with MV Securities, in uninsured funds, which provides investment asset management for educational institutions.

In addition, accounts in a financial institution are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. The amount in excess of the FDIC limit totaled \$6,503,589 as of June 30, 2016. However, \$5,947,903 of the excess is in three repurchase agreements which are collateralized by U.S. government and municipal securities.

15) RECLASSIFICATION AND INTERNAL TRANSFERS

At various times, scholarships and other restricted funds will be reclassified at the request of the donors. These reclassifications are reflected in the statements of activities.

16) MANAGEMENT AGREEMENTS

The Agencies (Note 13) and the Foundation have a memorandum of understanding whereby the Agencies loan certain endowment funds to the Foundation for the purpose of maximizing the investment yield and increasing the funds available for the Agency’s programs. The funds are managed with an asset allocation similar to that of the Foundation. The Foundation receives a management fee from the Agencies as compensation for managing the endowment funds. For the years ended June 30, 2016 and 2015, the Foundation received management fees totaling \$533,953 and \$532,863, respectively.

The Foundation also has an agreement with the University whereby they will donate the services of University employees to provide services for the Foundation. During the years ended June 30, 2016 and 2015, \$211,862 and \$285,619 worth of services were donated by the University. The services have been recognized as contributed services on the Statements of Activities.