

**The Association of Graduates of the  
United States Military Academy  
d/b/a West Point Association of Graduates**

Financial Statements

December 31, 2016 and 2015



Candor. Insight. Results.

# **The Association of Graduates of the United States Military Academy**

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## **Independent Auditors' Report**

Board of Directors  
The Association of Graduates of the United States Military Academy

We have audited the accompanying financial statements of The Association of Graduates of the United States Military Academy, d/b/a West Point Association of Graduates (the "Association"), which comprise the statement of financial position as of December 31, 2016 and 2015, and the related statements of activities, 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.

### **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 the audits to obtain reasonable assurance about whether the financial statements are free of 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 The Association of Graduates of the United States Military Academy as of December 31, 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.

*Baker Tilly Virchow Krause, LLP*

New York, New York  
May 9, 2017

# The Association of Graduates of the United States Military Academy

## Statement of Financial Position

December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
<b>Assets</b>		
Cash	\$ 5,173,882	\$ 7,412,821
Pledges receivable, net	20,160,863	22,519,737
Inventories and other assets	529,045	592,056
Investments	330,945,595	305,613,206
Split-interest and other trusts	20,941,495	27,130,934
Investments restricted by agreements	5,859,588	4,794,270
Building and equipment, net	7,209,300	7,247,946
	<u>390,819,768</u>	<u>375,310,970</u>
Total assets	<u>\$ 390,819,768</u>	<u>\$ 375,310,970</u>
<b>Liabilities and Net Assets</b>		
<b>Liabilities</b>		
Accounts payable and accrued expenses	\$ 2,523,542	\$ 1,892,719
Proffer payable	22,464,156	12,729,369
Deferred obligations and revenue	4,202,024	3,417,416
Liabilities - remainder trusts	4,345,997	4,148,056
Due to classes	2,469,563	2,619,927
Deferred compensation	615,603	499,092
	<u>36,620,885</u>	<u>25,306,579</u>
Total liabilities	<u>36,620,885</u>	<u>25,306,579</u>
<b>Net Assets</b>		
Unrestricted	36,158,947	29,451,514
Temporarily restricted	147,520,914	164,452,161
Permanently restricted	170,519,022	156,100,716
	<u>354,198,883</u>	<u>350,004,391</u>
Total net assets	<u>354,198,883</u>	<u>350,004,391</u>
Total liabilities and net assets	<u>\$ 390,819,768</u>	<u>\$ 375,310,970</u>

See notes to financial statements

**The Association of Graduates of the United States Military Academy**

Statement of Activities

Years Ended December 31, 2016 and 2015

	Years Ended December 31							
	2016			2015				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Revenues, Gains and Other Support</b>								
Contributions	\$ 682,592	\$ 28,197,677	\$ 6,086,779	\$ 34,967,048	\$ 710,084	\$ 25,133,483	\$ 11,093,500	\$ 36,937,067
Bequests	214,048	2,206,330	2,162,614	4,582,992	605,358	72,097	54,393	731,848
Royalties	540,568	76,264	3,640	620,472	558,438	83,601	4,325	646,364
Return on investments	3,079,476	669,245	-	3,748,721	2,563,531	1,803,051	-	4,366,582
Sales - gift shop	1,860,237	-	-	1,860,237	1,668,162	-	-	1,668,162
Subscriptions and advertising	232,439	-	-	232,439	492,759	-	-	492,759
Alumni activities	739,079	38,465	-	777,544	609,822	52,470	-	662,292
Other	305,440	(32,051)	-	273,389	514,784	(102,802)	6,000	417,982
<b>Net Assets Released from Restriction</b>								
Satisfaction of program restriction	42,991,275	(42,988,775)	(2,500)	-	24,392,492	(24,389,992)	(2,500)	-
Reimbursement for administrative and development expenses	5,673,243	(4,837,444)	(835,799)	-	4,878,020	(3,971,834)	(906,186)	-
Transfers, net	5,007,351	(11,478,198)	6,470,847	-	1,806,867	(9,803,796)	7,996,929	-
<b>Total revenue and support</b>	<b>61,325,748</b>	<b>(28,148,487)</b>	<b>13,885,581</b>	<b>47,062,842</b>	<b>38,800,317</b>	<b>(11,123,722)</b>	<b>18,246,461</b>	<b>45,923,056</b>
<b>Expenses</b>								
Program services								
Alumni services	3,096,651	-	-	3,096,651	3,053,270	-	-	3,053,270
Educational and historical	42,332,392	-	-	42,332,392	23,395,196	-	-	23,395,196
Communications & Marketing	1,129,740	-	-	1,129,740	1,175,426	-	-	1,175,426
(Recovery of) provision for uncollectible pledges, net	-	(775,369)	(532,725)	(1,308,094)	-	(2,495,903)	1,382,880	(1,113,023)
Supporting services								
Management and administration	3,730,448	-	-	3,730,448	3,878,851	-	-	3,878,851
Fund raising	6,801,692	-	-	6,801,692	6,408,451	-	-	6,408,451
<b>Total expenses</b>	<b>57,090,923</b>	<b>(775,369)</b>	<b>(532,725)</b>	<b>55,782,829</b>	<b>37,911,194</b>	<b>(2,495,903)</b>	<b>1,382,880</b>	<b>36,798,171</b>
<b>Change in Net Assets Before Investment Transactions</b>	<b>4,234,825</b>	<b>(27,373,118)</b>	<b>14,418,306</b>	<b>(8,719,987)</b>	<b>889,123</b>	<b>(8,627,819)</b>	<b>16,863,581</b>	<b>9,124,885</b>
<b>Net Realized and Unrealized Gains (Losses) on Investments</b>	<b>2,472,608</b>	<b>10,441,871</b>	<b>-</b>	<b>12,914,479</b>	<b>(1,208,251)</b>	<b>(4,411,755)</b>	<b>-</b>	<b>(5,620,006)</b>
<b>Change in Net Assets</b>	<b>\$ 6,707,433</b>	<b>\$ (16,931,247)</b>	<b>\$ 14,418,306</b>	<b>\$ 4,194,492</b>	<b>\$ (319,128)</b>	<b>\$ (13,039,574)</b>	<b>\$ 16,863,581</b>	<b>\$ 3,504,879</b>

See notes to financial statements

## The Association of Graduates of the United States Military Academy

### Statement of Net Assets

Years Ended December 31, 2016 and 2015

	<u>Total Unrestricted</u>	<u>Total Temporarily Restricted</u>	<u>Total Permanently Restricted</u>	<u>Total</u>
<b>Net Assets, January 1, 2015</b>	\$ 29,770,642	\$ 177,491,735	\$ 139,237,135	\$ 346,499,512
Net (decrease) increase in net assets balance for 2015	<u>(319,128)</u>	<u>(13,039,574)</u>	<u>16,863,581</u>	<u>3,504,879</u>
<b>Net Assets, December 31, 2015</b>	29,451,514	164,452,161	156,100,716	350,004,391
Net increase (decrease) in net assets balance for 2016	<u>6,707,433</u>	<u>(16,931,247)</u>	<u>14,418,306</u>	<u>4,194,492</u>
<b>Net Assets, December 31, 2016</b>	<u>\$ 36,158,947</u>	<u>\$ 147,520,914</u>	<u>\$ 170,519,022</u>	<u>\$ 354,198,883</u>

See notes to financial statements

# The Association of Graduates of the United States Military Academy

## Statement of Cash Flows

Years Ended December 31, 2016 and 2015

	<u>2016</u>	<u>2015</u>
<b>Cash Flows from Operating Activities</b>		
Change in net assets	\$ 4,194,492	\$ 3,504,879
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Contributions restricted for long-term investment	(8,253,033)	(11,158,218)
Net realized and unrealized (gain) loss on investments	(12,914,479)	5,620,006
Depreciation on building and equipment	549,051	420,772
Increase in value of trusts	(1,836,025)	(2,037,774)
Changes in:		
Unrestricted and temporarily restricted pledges receivable	2,369,533	6,366,944
Inventories and other assets	63,011	(1,364)
Accounts payable, accrued expenses and deferred compensation	747,334	(22,660)
Proffer payable	9,734,787	964,532
Deferred obligations and revenue	784,608	516,388
Liabilities associated with remainder trusts	197,941	423,929
Due to classes	(150,364)	73,675
	<u>(4,513,144)</u>	<u>4,671,109</u>
Net cash (used in) provided by operating activities		
<b>Cash Flows from Investing Activities</b>		
Purchase of investments	(151,828,825)	(80,360,422)
Proceeds from sale and maturity of investments	139,410,915	63,168,615
Purchase of building improvements and equipment	(510,405)	(2,006,276)
Receipts from settlement of split-interest agreements	8,353,111	3,124,050
Purchase of investments restricted by agreements	(1,392,965)	796,036
	<u>(5,968,169)</u>	<u>(15,277,997)</u>
Net cash used in investing activities		
<b>Cash Flows from Financing Activities</b>		
Proceeds from contributions	8,253,033	11,158,218
Changes in permanently restricted pledges receivable	(10,659)	(2,773,670)
	<u>8,242,374</u>	<u>8,384,548</u>
Net cash provided by financing activities		
<b>Net Decrease in Cash and Cash Equivalents</b>	(2,238,939)	(2,222,340)
<b>Cash and Cash Equivalents, Beginning</b>	<u>7,412,821</u>	<u>9,635,161</u>
<b>Cash and Cash Equivalents, Ending</b>	<u>\$ 5,173,882</u>	<u>\$ 7,412,821</u>

See notes to financial statements



# **The Association of Graduates of the United States Military Academy**

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Notes to Financial Statements  
December 31, 2016 and 2015

## **1. Organization and Summary of Significant Accounting Policies**

The Association of Graduates of the United States Military Academy, d/b/a West Point Association of Graduates (the "Association"), is an organization dedicated to furthering the ideals and promoting the welfare of the United States Military Academy (the "Academy"). The Association is exempt from federal income tax under the Internal Revenue Code. However, income from certain activities not directly related to the Association's tax-exempt purpose is subject to taxation as unrelated business income. In addition, the Association qualifies for the charitable contribution deduction under Internal Revenue Code (the "Code") rules and has been classified as an organization that is not a private foundation.

On June 12, 2014, the Association created the West Point Athletics Limited Liability Corporation (the "LLC") with the Association as its sole member. The primary purpose of the LLC is to assist the Academy in its objective to improve the intercollegiate athletic program. Under applicable U.S. Treasury regulations, the LLC is disregarded as a separate entity for income tax purposes and is reported within the Association's Federal *Return of Organization Exempt from Income Tax*.

### **Basis of Accounting**

The financial statements of the Association have been prepared using the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

### **Basis of Presentation**

The Association follows accounting and reporting guidelines established by the Financial Accounting Standards Board ("FASB"). The Association records written unconditional promises to give (pledges) as receivables and revenue, and in addition, distinguishes between contributions received for each net asset category in accordance with donor imposed restrictions. The Association has established standards for financial reporting, including the classification of resources into three classes of net assets: unrestricted, temporarily restricted and permanently restricted, based upon the absence or existence and nature of donor-imposed restrictions as follows:

**Unrestricted net assets** - Net assets that are not subject to donor-imposed stipulations.

**Temporarily restricted net assets** - Net assets subject to donor-imposed stipulations that can be fulfilled by actions of the Association pursuant to those stipulations or that expire by passage of time.

**Permanently restricted net assets** - Net assets subject to donor-imposed stipulations that they be maintained permanently by the Association. Generally, the donors of such assets permit the Association to use all or part of the income earned on the assets for specific purposes.

# **The Association of Graduates of the United States Military Academy**

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Notes to Financial Statements  
December 31, 2016 and 2015

## **Cash and Cash Equivalents**

The Association considers highly liquid debt instruments with original maturities of three months or less to be cash equivalents, excluding amounts held in Investments.

The Association places its cash and cash equivalents with high quality financial institutions where, balances generally exceed the Federal Deposit Insurance Corporation (the "FDIC") insurance limits. Accounts at each institution are insured by the FDIC up to \$250,000 for interest and non-interest bearing accounts.

## **Promises to Give**

Unconditional written promises to give (pledges) are recognized as contribution revenue in the period received and as assets. Promises to give are recorded at net realizable value and are discounted at an appropriate rate commensurate with the risks involved. Amortization of discounts is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions. An allowance for uncollectible promises to give is provided based upon management's judgment, including such factors as due date (aging), prior collection history, type of contribution, and nature of fundraising activity. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

## **Proffer Payable**

Proffer Payable represents unconditional promises to grant funds to the United States Military Academy that have been offered prior to year end, but remain unpaid as of the statement of financial position date.

The Association, in accordance with Army Regulations, proffers gifts it intends to make to the United States Military Academy, similar to making a promise to give. Proffers are recorded as liabilities at the time they are offered and are generally paid within a one year period.

## **Split-Interest and Other Trust Agreements**

The Association is a party to various types of split-interest and other trust agreements whereby the donor makes an initial gift in which the Association has a beneficial interest but may not be the sole beneficiary. These agreements include charitable remainder trusts, pooled life income funds, gift annuities, other types of trusts and irrevocable bequests, and are reported at fair market value.

## **Inventories**

Inventories consist of gift shop items and are stated at the lower of cost (first-in, first-out method) or market.

## **Building and Equipment**

Building and equipment are carried at cost or, if donated, at the estimated fair value at the date of donation. Depreciation is computed using the straight-line method and is based on the assets' estimated useful lives between three and five years for computer equipment, five and ten years for furniture and fixtures, ten to fifteen years for building improvements and equipment and forty years for the building.

# **The Association of Graduates of the United States Military Academy**

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Notes to Financial Statements  
December 31, 2016 and 2015

## **Donated Property and Securities**

Donated materials and equipment are reflected as contributions in the accompanying statements at their estimated fair value at date of donation. Donated marketable securities are recorded at their fair value at date of donation. Absent donor restrictions to the contrary, donated securities are sold immediately. Contributions for the year ended December 31, 2016, include \$6,218,201 of donated securities (\$8,488,152 in 2015).

## **Due to Classes**

The Association maintains commingled brokerage accounts consisting of cash and investments, on behalf of various graduated classes. These assets are recorded in the statement of financial position as investments, along with an offsetting liability. This liability is presented in the statement of financial position as "Due to classes" in the amounts of \$2,469,563 and \$2,619,927 at December 31, 2016 and 2015, respectively.

## **Restricted and Unrestricted Revenue**

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted revenue, depending on the existence and/or nature of any donor restrictions, and are reported as an increase in unrestricted, temporarily, or permanently restricted net assets. When a restriction expires (that is, when the 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.

## **Deferred Obligations and Revenue**

Deferred obligations and revenue consists primarily of obligations for payments relating to pooled life income funds and charitable gift annuities.

## **Tax Status and Expense**

The Association is classified for tax purposes as an organization under Section 501(c)(3) of the Code and, except for unrelated business income, is exempt from income taxes under Section 501(a) of the Code. Therefore, no provision for income taxes is made in the accompanying financial statements.

The income tax positions taken by the Association for any years open under the various statutes of limitations are that the Association continues to be exempt from income taxes and that the Association earns revenues from certain activities which are considered unrelated business taxable income under the Code. In both 2016 and 2015, however, unrelated business income (net of applicable expenses) resulted in no material tax expense. The Association believes that there are no other tax positions taken or expected to be taken that would significantly increase or decrease unrecognized tax expenses or benefits within 12 months of the reporting date. None of the Association's federal or state income tax returns is currently under examination by the Internal Revenue Service ("IRS") or state authorities.

# **The Association of Graduates of the United States Military Academy**

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Notes to Financial Statements  
December 31, 2016 and 2015

## **Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

## **Reclassifications**

Certain reclassifications have been made to the 2015 balances previously reported to conform to the current year presentation.

## **Subsequent Events**

Subsequent events have been evaluated for recognition or disclosure through May 9, 2017, the date when the financial statements were available to be issued.

## **New Accounting Standards**

In May 2014, the FASB issued Accounting Standards Update (“ASU”) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. ASU No. 2014-09 supersedes the revenue recognition requirements in Topic 605, *Revenue Recognition*, and most industry-specific guidance. Under the requirements of ASU No. 2014-09, the core principle is that entities should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The Association will be required to adopt the guidance in ASU No. 2014-09 for years beginning after December 15, 2018; early application is not permitted. The Association does not believe the adoption of this standard will have a material impact on its financial position or activities.

In May 2015, the FASB issued ASU 2015-07, *Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or its Equivalent)*. This ASU was issued to address the diversity in practice relating to how certain investments measured at net asset value are categorized in the fair value hierarchy. The amendments in ASU No. 2015-07 remove 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. ASU No. 2015-07 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. ASU No. 2015-07 is effective for the Association for the year beginning January 1, 2017; early adoption is permitted. The Association does not believe the adoption of this standard will have a material impact on its financial position or activities.

During August 2016, the FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The new guidance is intended to improve and simplify the current net asset classification requirements and information presented in financial statements and notes that is useful in assessing a not for-profit’s liquidity, financial performance and cash flows. ASU No. 2016-14 is effective for fiscal years beginning after December 15, 2017, with early adoption permitted. ASU No. 2016-14 is to be applied retroactively with transition provisions. The Association is currently assessing the effect that ASU No. 2016-14 will have on its financial statements.

# The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
December 31, 2016 and 2015

## 2. Pledges Receivable

Pledges receivable are written unconditional promises to give. The Association recognizes potentially uncollectible pledges and provides an allowance for the estimated uncollectible amount. Pledges receivable, net of the discount to present value (at a risk adjusted rate of 3%) and the allowance for uncollectible pledges, are as follows:

	<b>December 31,</b>	
	<b>2016</b>	<b>2015</b>
Receivable in less than one year	\$ 9,601,813	\$ 9,241,810
Receivable in one year to five years	17,320,877	21,633,204
Receivable in more than five years	3,826,212	4,069,728
Total unconditional promises to give	30,748,902	34,944,742
Less allowance for uncollectible pledges	(8,253,021)	(9,561,117)
Less discounts to net present value	(2,335,018)	(2,863,888)
Total	<u>\$ 20,160,863</u>	<u>\$ 22,519,737</u>

## 3. Investments

Investments, including pooled life income funds and gift annuities, are presented in the financial statements at fair value and are categorized as follows:

	<b>December 31,</b>	
	<b>2016</b>	<b>2015</b>
Investments	\$ 330,945,595	\$ 305,613,206
Investments - pooled life income funds	1,293,503	1,296,723
Investments - gift annuities	4,566,085	3,497,547
Investments restricted by agreements	5,859,588	4,794,270
Total	<u>\$ 336,805,183</u>	<u>\$ 310,407,476</u>

Investments are comprised of the following:

	<b>December 31,</b>	
	<b>2016</b>	<b>2015</b>
Short-term investments (money markets)	\$ 30,715,100	\$ 26,867,080
Fixed income funds	59,574,607	62,259,325
Equity securities	193,750,178	168,766,973
Alternative investments	51,215,561	52,151,293
Other	1,549,737	362,805
Total	<u>\$ 336,805,183</u>	<u>\$ 310,407,476</u>

# The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
December 31, 2016 and 2015

Return on investments, gains and losses on investment transactions are comprised of the following:

	<b>December 31,</b>	
	<b>2016</b>	<b>2015</b>
Unrestricted:		
Return on investments (interest and dividends)	\$ 3,079,476	\$ 2,563,531
Net realized gains on sale of investments	\$ 384,238	\$ 330,088
Net unrealized gains (losses) on investments	2,088,370	(1,538,339)
	<u>\$ 2,472,608</u>	<u>\$ (1,208,251)</u>
Temporarily restricted:		
Return on investments (interest and dividends)	\$ 669,245	\$ 1,803,051
Net realized gains on sale of investments	\$ 1,884,258	\$ 1,755,730
Net unrealized gains (losses) on investments	8,557,613	(6,167,485)
	<u>\$ 10,441,871</u>	<u>\$ (4,411,755)</u>

Investment gains (losses) on permanently restricted net assets are reported as increases (decreases) in unrestricted or temporarily restricted net assets depending upon donor restrictions placed on the use of the investment income.

The Association has entered into several agreements with Commonfund, a non-profit investment manager, to invest in various partnerships. These agreements contain provisions for capital calls by the general partner up to specified amounts. Total capital committed under the agreements amounts to \$13,750,000 and the total amount of capital contributed to the partnerships by the Association as of December 31, 2016 was \$12,928,291. This investment is included in alternative investments as Level 3 in the fair value table below. As capital calls are received, other investments are sold and the proceeds and available cash are used to fulfill the capital call. The Association has also entered into an agreement with AEW Capital Management, LP, to invest in a real estate investment trust. This agreement contains provisions for capital calls by the general partner up to specified amounts. Total capital committed under the agreement amounts to \$3,000,000. Capital calls funded by the Association as of December 31, 2016 are \$2,720,518. In accordance with these agreements, the redemption period for these funds range from 7 to 10 years and they are classified as fund of funds and real estate fund Level 3 investments in the fair value table below.

The Association entered into an agreement in 2014 with SVB Strategic Investors Fund VII, LP. The agreement contains provisions for capital calls by the partner up to specified amounts. The total capital committed under the agreement amounts to \$1,000,000. The total capital contributed to the Fund by the Association as of December 31, 2016 was \$380,000. The redemption period for this agreement is five years.

# **The Association of Graduates of the United States Military Academy**

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Notes to Financial Statements  
December 31, 2016 and 2015

The Association entered into an agreement in 2015 with Institutional Venture Partners XV, LP. The agreement contains provisions for capital calls by the partner up to specified amounts. The total capital committed under the agreement amounts to \$1,000,000. Capital Calls funded by the Association as of December 31, 2016 are \$400,000. The redemption period for this agreement is ten years, subject to two one-year extensions. The Association also entered into an agreement in 2015 with Oaktree Private Investment Fund IV, LP. The agreement contains provisions for capital calls by the partner up to specified amounts. The total capital committed under the agreement amounts to \$4,000,000. The total capital contributed to the Fund by the Association as of December 31, 2016 was \$680,000. The redemption period for this agreement is ten years, subject to extension.

The Association follows FASB guidance for Fair Value Measurement for investments, which establishes a framework for measuring fair value under generally accepted accounting principles, and also provides guidance regarding a fair value hierarchy. This hierarchy prioritizes information used to measure fair value and the effects of fair value measurements on earnings and provides for enhanced disclosures determined by the level within the hierarchy of information used in the valuation.

Fair value is defined as the price that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement assumes that the transaction to sell an asset occurs in the principal market for the asset, or in the absence of a principal market, the most advantageous market for the asset. The principal market is the market in which the reporting entity would sell or transfer the asset with the greatest volume or level of activity for the asset. In determining the principal market for an asset, it is assumed that the reporting entity has access to the market as of the measurement date. If no market for the asset exists or if the reporting entity does not have access to the principal market, the reporting entity uses a hypothetical market.

The level of fair value inputs used to measure investments is characterized in accordance with an established fair value hierarchy. Where inputs for an investment fall in more than one level in the fair value hierarchy, the investment is classified in its entirety based on the lowest level input that is significant to that investment's fair value measurement. Management uses judgment and considers factors specific to the investment in determining the significance of an input to a fair value measurement. The three levels of the fair value hierarchy and investments that fall into each of the levels are described as follows:

- Level 1: Level 1 inputs are unadjusted quoted market prices in active markets that are accessible at the measurement date for identical assets.
- Level 2: Level 2 are inputs other than quoted prices included in Level 1 that are observable for the asset, either directly or indirectly.
- Level 3: Level 3 inputs are unobservable and cannot be corroborated by observable market data.

# **The Association of Graduates of the United States Military Academy**

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Notes to Financial Statements  
December 31, 2016 and 2015

The basis of fair value for underlying assets is as follows:

- Short-term investments consist of money market and bond funds in which the carrying value approximates fair value because of the short maturity of these instruments.
- Fixed income and equity funds classified as Level 1 are valued at the last sales price on the date of valuation or, if no sale occurred on such date, at the last bid price thereon.
- Equity, real estate and limited partnerships classified as Level 2 or 3 are valued based on the net asset value (NAV) of a share. Fair value is determined by reference to the fund's reported NAV per share as a practical expedient, unless it is probable that the investment will be disposed at some value other than NAV per share in which case reference would be made to the expected disposal price or other indicators of value. The investments valued using the NAV per share include a strategy that invests in publicly traded equity securities, fixed income securities and marketable alternative investments. These funds do not have redemption restrictions or commitments.
- Fund of funds and real estate funds classified as Level 3 include private capital securities that are generally valued according to the "mark-to-market method" which attempts to apply a fair value standard by referring to meaningful third-party transactions, comparable public market valuations or the income approach, in which market expectations of future cash flows or earnings are converted to a present value. However, in some instances, it may be most appropriate to value an investment at cost, if little has changed since the initial investment in the company. This valuation process is often used in the early years of investments in a private company, and in these instances cost is reflective of fair value.



## The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
December 31, 2016 and 2015

The following fair value hierarchy table sets forth the investment portfolio by level as of December 31, 2016 and 2015 where carrying value equals fair value (refer to Note 4 for split-interests and other trusts):

	<b>2016</b>			<b>Total</b>
	<b>Quoted Prices in Active Markets (Level 1)</b>	<b>Other Observable Inputs (Level 2)</b>	<b>Unobservable Inputs (Level 3)</b>	
Short-term investments	\$ 30,566,766	\$ 148,334	\$ -	\$ 30,715,100
Fixed income funds				
Mortgage backed	12,584,251	-	-	12,584,251
Government funds	46,990,356	-	-	46,990,356
Equity funds				
Domestic equity	17,721,343	99,140,701	-	116,862,044
International equity	76,888,134	-	-	76,888,134
Alternative investments				
Limited partnerships	-	-	39,179,046	39,179,046
Fund of funds	-	-	3,054,218	3,054,218
Real estate funds	-	7,135,287	1,847,010	8,982,297
Other	1,549,737	-	-	1,549,737
<b>Total</b>	<b>\$ 186,300,587</b>	<b>\$ 106,424,322</b>	<b>\$ 44,080,274</b>	<b>\$ 336,805,183</b>
	<b>2015</b>			
Short-term investments	\$ 26,781,638	\$ 85,442	\$ -	\$ 26,867,080
Fixed income funds				
Mortgage backed	14,653,542	-	-	14,653,542
Government funds	47,605,783	-	-	47,605,783
Equity funds				
Domestic equity	14,212,659	83,550,026	-	97,762,685
International equity	71,004,288	-	-	71,004,288
Alternative investments				
Limited partnerships	-	-	40,239,661	40,239,661
Fund of funds	-	-	3,367,959	3,367,959
Real estate funds	-	6,733,569	1,810,104	8,543,673
Other	362,805	-	-	362,805
<b>Total</b>	<b>\$ 174,620,715</b>	<b>\$ 90,369,037</b>	<b>\$ 45,417,724</b>	<b>\$ 310,407,476</b>

# The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
December 31, 2016 and 2015

The following table sets forth a summary of changes in fair value of investments measured using Level 3 inputs for the year ended December 31:

	<u>2016</u>	<u>2015</u>
Balance, beginning of year	\$ 45,417,724	\$ 42,230,160
Purchases	893,811	6,062,879
Earnings	(197,859)	(267,328)
Sales	<u>(2,033,402)</u>	<u>(2,607,987)</u>
Balance, end of year	<u>\$ 44,080,274</u>	<u>\$ 45,417,724</u>

Overall challenges to the economic environment have created significant financial market volatility and illiquidity. The Association is not immune to the impacts of these market conditions. It should be noted that it is at least possible that fair values could change rapidly.

Investments are primarily pooled in investment portfolios containing multiple unrestricted, temporarily restricted and permanently restricted funds. The investment income is allocated to the individual funds within the pool based upon the proportional invested balance of each fund.

#### 4. Split-Interest Trusts, Other Trusts and Investments Restricted by Agreements

The Association is the beneficiary of various split-interest agreements, investments restricted by agreements and other trusts as follows:

##### Irrevocable Trusts and Others

Donors have established irrevocable trusts held by third party trustees. The trusts consist of various investment portfolios. Pursuant to the trust agreements, the donor's designated beneficiary is entitled to the income earned on the trust during the beneficiary's lifetime and upon death the assets in the trust will be available to the Association. The present value of the estimated amount to be received was calculated using a risk adjusted discount rate (approximately 5%) and the applicable mortality table.

##### Remainder Trusts

Donors have established charitable remainder trusts naming the Association as the trustee. Charitable remainder trusts provide for the payment of distributions to designated beneficiaries over the trusts' terms (usually the designated beneficiary's lifetime). At the end of each trust's term, the remaining assets are available for the Association's use, subject to the donor-imposed restrictions. Assets held in charitable remainder trusts totaled \$6,992,470 at December 31, 2016 (\$6,665,363 in 2015) and are recorded at estimated realizable value. On an annual basis the Association revalues the liability to make distributions to the designated beneficiaries based on actuarial assumptions. The present value of the estimated future payments (\$4,345,997 and \$4,148,056 at December 31, 2016 and 2015, respectively) is calculated using a discount rate (approximately 3%) and applicable mortality tables.

# **The Association of Graduates of the United States Military Academy**

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Notes to Financial Statements  
December 31, 2016 and 2015

Donors have established charitable remainder trusts for which the Association is not the trustee. The present value of the estimated beneficial interest to be received at the end of the trusts' terms (usually the designated beneficiary's lifetime) totaled \$9,071,159 at December 31, 2016 (\$13,868,984 at 2015).

## **Perpetual Trust**

A donor has established a perpetual trust under which the Association receives 35% of the trust's 5% annual distribution. The asset is recorded based on the net present value of future cash flows expected to be received.

## **Pooled Life Income Funds**

The Association has a pooled life income fund whereby donors contribute into an investment pool and are assigned a specific number of units. The donor or designated beneficiary receives an allocation of income on a quarterly basis. Upon the death of the beneficiary, the value of the assigned units reverts to the Association. The Association's remainder interest in the assets received is measured at the fair value of the assets to be received discounted for the estimated time period until the death of the designated beneficiary using the applicable mortality tables. The liability for future payments is recorded as deferred obligations and approximated \$650,473 at December 31, 2016 (\$663,893 in 2015).

## **Gift Annuities**

The Association receives certain gifts whereby it is contractually obligated to make periodic payments to the donor for the remainder of his or her life. Currently, gift annuity contributions are deposited into an investment portfolio at a financial institution. The assets received are recorded at fair value and an annuity payment liability is recorded as deferred obligations at the present value of the future cash flows expected to be paid to the designated beneficiary using the applicable mortality table. At December 31, 2016 deferred obligations associated with gift annuities approximated \$3,253,701 (\$2,526,983 in 2015).

As required by insurance law, the Association maintains an annuity reserve greater than 115% of associated liabilities. The reserve requirement is met using the specific assets and liabilities of the pooled life income funds and gift annuities. At December 31, 2016 and 2015, the Association maintained sufficient assets in excess of liabilities to fulfill the requirement under the law. The Association was in full compliance with reserve requirements under the insurance law at December 31, 2016 and 2015.

# The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
December 31, 2016 and 2015

The split-interest and other trusts are considered Level 3 investments as defined in Note 3. The changes in split-interest and other trusts for 2016 and 2015 were as follows:

	<b>Split-Interest and Other Trusts</b>			<b>Total Split-Interest &amp; Other Trusts</b>
	<b>Irrevocable &amp; Other Trusts</b>	<b>Remainder Trusts</b>	<b>Perpetual Trust</b>	
Balance at December 31, 2014	\$ 7,381,983	\$ 19,324,803	\$ 1,032,537	\$ 27,739,323
Contributions	806,415	2,368,792	-	3,175,207
Cash realized	(2,622,095)	(450,328)	(51,627)	(3,124,050)
Change in value	86,640	(708,920)	(37,266)	(659,546)
Balance at December 31, 2015	5,652,943	20,534,347	943,644	27,130,934
Contributions	1,060,093	594,262	-	1,654,355
Cash realized	(2,847,110)	(5,458,819)	(47,182)	(8,353,111)
Change in value	66,413	393,839	49,065	509,317
Balance at December 31, 2016	<u>\$ 3,932,339</u>	<u>\$ 16,063,629</u>	<u>\$ 945,527</u>	<u>\$ 20,941,495</u>

The changes in investments restricted by agreements for 2016 and 2015 were as follows:

	<b>Investments Restricted by Agreements</b>		
	<b>Pooled Life Income Funds</b>	<b>Gift Annuities</b>	<b>Total Investments Restricted by Agreements</b>
Balance at December 31, 2014	\$ 2,236,129	\$ 3,227,295	\$ 5,463,424
Contributions	-	625,500	625,500
Cash realized	(880,501)	(6,802)	(887,303)
Adjustments	-	(100,000)	(100,000)
Change in value	(58,905)	(248,446)	(307,351)
Balance at December 31, 2015	1,296,723	3,497,547	4,794,270
Contributions	-	1,175,000	1,175,000
Cash realized	(3,267)	-	(3,267)
Change in value	47	(106,462)	(106,415)
Balance at December 31, 2016	<u>\$ 1,293,503</u>	<u>\$ 4,566,085</u>	<u>\$ 5,859,588</u>

# The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
December 31, 2016 and 2015

## 5. Building and Equipment

A summary of building and equipment is as follows:

	December 31,	
	2016	2015
Equipment	\$ 961,367	\$ 449,715
Building & improvements	11,273,612	11,275,189
Furniture & fixtures	886,261	885,931
	13,121,240	12,610,835
Less accumulated depreciation	5,911,940	5,362,889
Total	<u>\$ 7,209,300</u>	<u>\$ 7,247,946</u>

Depreciation expense was \$549,052 and \$420,772 as of December 31, 2016 and 2015, respectively.

## 6. Lines of Credit

The Association has entered into a \$7,000,000 line of credit with a bank. This line was established under a working capital support agreement dated June 16, 2014, with interest rate options of LIBOR plus 1.4% or Prime Rate minus 1.25%. There were no outstanding balances at December 31, 2016 or 2015. The credit line expires on June 29, 2017.

The Association incurred no interest expense for the years ended December 31, 2016 and 2015.

## 7. Deferred Compensation

The Association has arrangements with its executive officers whereby specified amounts of their compensation are deferred. These amounts are invested on behalf of the executives and are payable upon their retirement. At December 31, the Association's investments and obligation pursuant to these arrangements was:

	2016	2015
Investments	<u>\$ 615,603</u>	<u>\$ 499,092</u>
Deferred compensation liability	<u>\$ (615,603)</u>	<u>\$ (499,092)</u>

# The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
December 31, 2016 and 2015

## 8. Pension Plan

The Association sponsors a defined contribution retirement plan under Section 403(b) of the Code that allows for contributions by employees as well as the Association. Substantially all employees are eligible to participate in this plan. The Association's contributions to the plan are based on a percentage of the employee's elective contribution and totaled approximately \$365,657 for the year ended December 31, 2016 (\$332,086 for 2015).

## 9. Property Lease

In 1992, the Association entered into a fifty year lease with the Secretary of the Army for approximately 1.5 acres of land on which its alumni center was constructed. This lease has a renewal option for an additional fifty years and is revocable by the Secretary of the Army. The land is being leased at no charge to the Association.

## 10. Restrictions on Net Assets

Temporarily restricted net assets are available for the support of various projects related to the Academy and its graduates.

Permanently restricted net assets consist of endowment funds and are restricted to the following:

	<u>December 31,</u>	
	<u>2016</u>	<u>2015</u>
Permanent endowment with no restrictions on the use of income	\$ 36,172,801	\$ 32,825,771
Permanent endowments with income restricted to the support of projects and programs related to the Academy and its graduates	<u>134,346,221</u>	<u>123,274,945</u>
Total	<u>\$ 170,519,022</u>	<u>\$ 156,100,716</u>

## 11. Transfers

Transfers are made among the net asset classes to reclassify previously recognized revenue that has been re-allocated based upon the occurrence of certain events or the determination that a transfer is needed to reflect the donors' intent for the contribution. The Association ensures donors' consent before making net asset transfers to and from temporarily restricted to permanently restricted.

## 12. Functional Allocation of Expenses

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

# The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
December 31, 2016 and 2015

## 13. Description of Program and Supporting Services

The following program and supporting services are included in the accompanying financial statements:

**Communications and Marketing** - Disseminates information on current events and the history, activities, objectives and purpose of the United States Military Academy through certain publications and media.

**Management and Administration** - Relates to the overall administration of the Association.

**Fund Raising** - Provides the structure necessary to solicit, secure and steward private financial support from individuals, foundations and corporations.

**Educational and Historical** - Provides gift funds and assets to the United States Military Academy ("USMA") with the purpose to include the encouragement of the study of leadership and to enhance the image of USMA. The Association recorded \$42,332,392 of grants to USMA in 2016 (\$23,395,196 in 2015), related to educational and historical programs and support services. During 2016, the Association recorded a grant to USMA of approximately \$22 million for the construction of the Visitors Center. As of December 31, 2016, approximately \$17 million of this grant is a proffer payable to USMA and will be paid within one year as construction is expected to be completed in fall of 2017.

**Alumni Services** - Encompasses activities, support and services provided to graduates including events, awards and the maintenance of detailed biographical and historical records on graduates of USMA and includes expenses for the operation of a gift shop.

Total programming and supporting services are comprised of the following expense categories:

	<u>2016</u>	<u>2015</u>
Grants to USMA	\$ 42,332,392	\$ 23,395,196
Salaries	7,478,532	7,135,971
Benefits	1,528,613	1,447,246
Professional services	642,567	1,173,486
Printing	224,116	245,813
Postage and shipping	468,844	516,305
Cost of goods sold	976,429	845,646
Employee travel	240,166	260,989
Awards and alumni events	257,757	347,055
Donor recognition expense	717,220	309,399
Donor acquisition	628,270	852,847
Office expenses	106,197	119,254
Building expenses	272,874	282,240
Depreciation	549,051	420,772
All other	667,895	558,975
	<u>\$ 57,090,923</u>	<u>\$ 37,911,194</u>

# **The Association of Graduates of the United States Military Academy**

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Notes to Financial Statements  
December 31, 2016 and 2015

## **14. Endowment**

In September 2010, the State of New York enacted the New York Prudent Management of Institutional Funds Act (NYPMIFA, the "Act"). The Act provides specific guidance regarding investment management and spending policies related to funds donated as "endowment" to the organization. Among its many provisions, the Act promotes a total return approach to spending, with the goals of investing at a rate that will preserve the purchasing power of the principal over the long term as well as a spend rate that, over the long term, will reflect the donor's intentions. The Act requires each organization to establish written investment and spending policies to ensure compliance with the Act. The Act also outlines the following eight standards for prudent spending, including a requirement that organizations have a written policy describing how such standards were adopted:

1. The duration and preservation of the endowment fund
2. The purpose of the institution and the endowment fund
3. General economic conditions
4. The possible effect of inflation or deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the institution
7. Where appropriate and circumstances would otherwise warrant, alternatives to expenditure of the endowment fund, giving due consideration to the effect that such alternatives may have on the institution
8. The investment policy of the institution

In addition, the Act establishes that a yearly spend of more than 7% of an endowment's market value, based on quarterly market values of the endowment calculated over a period of not less than 5 years, creates a rebuttal presumption of imprudence. The Act also requires written notification to all existing endowment donors allowing them to indicate whether or not they will allow the endowment to be spent below the original gift amount.

The primary investment objective is to maximize total return within prudent risk guidelines. The secondary objective is preserve capital - less risk will be assumed for funds intended for near-term use, while greater risk may be assumed for longer-term funds, including endowments.

For endowments whose income is unrestricted or restricted for specific purposes, the Association uses a total return policy whereby a fixed percentage (4% for restricted in 2016 and 2015, and 4.5% and 5% for unrestricted in 2016 and 2015, respectively) of the prior twelve quarters' market value of permanently restricted investments and their related temporarily restricted income accounts is available for distribution in the ensuing year for the intended endowment purposes. The unrestricted endowed assets represent income available for unrestricted purposes. If endowments have negative balances in their income accounts at year end, the availability of distributions is limited to interest and dividend income earned by the endowment fund during the calendar year.



# The Association of Graduates of the United States Military Academy

Notes to Financial Statements  
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In addition, it is the Association's current policy to recognize the historic dollar value of all endowment funds and not spend any portion of the corpus. The Association classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment and (b) the original value of subsequent gifts to the permanent endowment. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Association in a manner consistent with the Act.

Changes in endowed net assets for the year ended December 31, 2016, are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, end of year, December 31, 2015	\$ 10,016,927	\$ 41,624,642	\$ 156,100,716	\$ 207,742,285
Contributions	-	62,106	8,249,393	8,311,499
Return on investment	118,774	465,859	-	584,633
Realized and unrealized gain on investment	2,034,901	7,734,259	-	9,769,160
Transfers and other, net	-	(697,159)	6,168,913	5,471,754
Amount appropriated for expenditure	<u>(1,758,300)</u>	<u>(3,218,356)</u>	<u>-</u>	<u>(4,976,656)</u>
Endowment net assets, end of year, December 31, 2016	<u>\$ 10,412,302</u>	<u>\$ 45,971,351</u>	<u>\$ 170,519,022</u>	<u>\$ 226,902,675</u>

Changes in endowed net assets for the year ended December 31, 2015, are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, end of year, December 31, 2014	\$ 11,949,156	\$ 47,337,435	\$ 139,237,135	\$ 198,523,726
Contributions	-	176,305	11,147,894	11,324,199
Return on investment	339,612	1,310,854	-	1,650,466
Realized and unrealized loss on investment	(839,035)	(3,176,163)	-	(4,015,198)
Transfers and other, net	(31,021)	(1,136,348)	5,715,687	4,548,318
Amount appropriated for expenditure	<u>(1,401,785)</u>	<u>(2,887,441)</u>	<u>-</u>	<u>(4,289,226)</u>
Endowment net assets, end of year, December 31, 2015	<u>\$ 10,016,927</u>	<u>\$ 41,624,642</u>	<u>\$ 156,100,716</u>	<u>\$ 207,742,285</u>