

**THE ASSOCIATION OF  
GRADUATES OF THE UNITED  
STATES MILITARY ACADEMY**

AUDITED FINANCIAL STATEMENTS

Years ended December 31, 2007 and 2006

# THE ASSOCIATION OF GRADUATES OF THE UNITED STATES MILITARY ACADEMY

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## INDEPENDENT AUDITOR'S REPORT

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

We have audited the accompanying statements of financial position of The Association of Graduates of the United States Military Academy as of December 31, 2007 and 2006, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Association's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Association of Graduates of the United States Military Academy as of December 31, 2007 and 2006 and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

*UHY* LLP

Albany, New York  
May 23, 2008

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
STATEMENTS OF FINANCIAL POSITION**

|                                       | <b>December 31,</b>   |                       |
|---------------------------------------|-----------------------|-----------------------|
|                                       | <b>2007</b>           | <b>2006</b>           |
| <b>ASSETS</b>                         |                       |                       |
| Cash                                  | \$ 1,829,886          | \$ 1,626,883          |
| Pledges receivable, net               | 18,065,075            | 14,936,150            |
| Inventories and other assets          | 569,568               | 556,538               |
| Investments                           | 160,521,413           | 139,680,215           |
| Investments restricted by agreements  | 4,772,366             | 4,357,869             |
| Split interest trusts                 | 16,022,702            | 15,955,694            |
| Building and equipment, net           | <u>6,583,780</u>      | <u>6,860,179</u>      |
| Total assets                          | <u>\$ 208,364,790</u> | <u>\$ 183,973,528</u> |
| <b>LIABILITIES AND NET ASSETS</b>     |                       |                       |
| <b>LIABILITIES</b>                    |                       |                       |
| Notes payable                         | \$ 2,345,450          | \$ 2,336,500          |
| Accounts payable and accrued expenses | 544,040               | 741,337               |
| Proffer payable                       | 158,003               | 4,229,091             |
| Deferred revenue                      | 2,768,437             | 2,468,989             |
| Liabilities - remainder trusts        | 2,860,662             | 2,449,608             |
| Deferred compensation                 | <u>308,574</u>        | <u>310,317</u>        |
| Total liabilities                     | <u>8,985,166</u>      | <u>12,535,842</u>     |
| <b>NET ASSETS</b>                     |                       |                       |
| Unrestricted                          | 24,076,003            | 21,574,206            |
| Temporarily restricted                | 83,404,493            | 67,649,684            |
| Permanently restricted                | <u>91,899,128</u>     | <u>82,213,796</u>     |
| Total net assets                      | <u>199,379,624</u>    | <u>171,437,686</u>    |
| Total liabilities and net assets      | <u>\$ 208,364,790</u> | <u>\$ 183,973,528</u> |

See notes to financial statements.

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
STATEMENTS OF ACTIVITIES**

|   | Years Ended December 31, |                        |                        |                |               |                        |                        |                |
|---|--------------------------|------------------------|------------------------|----------------|---------------|------------------------|------------------------|----------------|
|   | 2007                     |                        |                        |                | 2006          |                        |                        |                |
|   | Unrestricted             | Temporarily Restricted | Permanently Restricted | Total          | Unrestricted  | Temporarily Restricted | Permanently Restricted | Total          |
| Revenues, gains and other support                         |                          |                        |                        |                |               |                        |                        |                |
| Contributions   | \$ 56,473                | \$ 25,050,307          | \$ 7,399,080           | \$ 32,505,860  | \$ 58,436     | \$ 18,843,323          | \$ 2,184,654           | \$ 21,086,413  |
| Bequests  | 103,163                  | 1,871,744              | 1,513,979              | 3,488,886      | 536,874       | 358,485                | 485,362                | 1,380,721      |
| Royalties   | 287,742                  | 62,419                 | 12,366                 | 362,527        | 275,429       | 9,014                  | 16,127                 | 300,570        |
| Return on investments                                     | 3,710,213                | 7,815,369              | -                      | 11,525,582     | 3,784,457     | 9,710,032              | -                      | 13,494,489     |
| Sales - gift shop   | 1,394,131                | -                      | -                      | 1,394,131      | 1,452,271     | -                      | -                      | 1,452,271      |
| Subscriptions and advertising                             | 765,193                  | -                      | -                      | 765,193        | 735,011       | -                      | -                      | 735,011        |
| Alumni activities   | 860,300                  | 1,443,541              | -                      | 2,303,841      | 606,064       | 1,406,394              | -                      | 2,012,458      |
| Other   | 203,201                  | (5,118)                | 30,639                 | 228,722        | 212,444       | (7,922)                | 26,512                 | 231,034        |
| (Provision) recovery for uncollectible pledges            | -                        | (731,382)              | (1,310,938)            | (2,042,320)    | -             | 886,903                | (357,106)              | 529,797        |
|   |                          |                        |                        |                |               |                        |                        | -              |
| Net assets released from restriction                      |                          |                        |                        |                |               |                        |                        | -              |
| Satisfaction of program restriction                       | 12,331,825               | (12,331,825)           | -                      | -              | 20,199,008    | (20,199,008)           | -                      | -              |
| Reimbursement for administrative and development expenses | 4,727,084                | (3,679,797)            | (1,047,287)            | -              | 3,617,049     | (2,809,716)            | (807,333)              | -              |
| Transfers   | 652,956                  | (3,740,449)            | 3,087,493              | -              | 132,249       | (4,197,322)            | 4,065,073              | -              |
|   |                          |                        |                        |                |               |                        |                        | -              |
| Total revenues, gains and other support                   | 25,092,281               | 15,754,809             | 9,685,332              | 50,532,422     | 31,609,292    | 4,000,183              | 5,613,289              | 41,222,764     |
| Expenses  |                          |                        |                        |                |               |                        |                        |                |
| Program services  |                          |                        |                        |                |               |                        |                        |                |
| Alumni services   | 3,465,907                | -                      | -                      | 3,465,907      | 3,521,953     | -                      | -                      | 3,521,953      |
| Educational and historical                                | 11,246,850               | -                      | -                      | 11,246,850     | 18,951,545    | -                      | -                      | 18,951,545     |
| Publications  | 662,222                  | -                      | -                      | 662,222        | 716,269       | -                      | -                      | 716,269        |
| Supporting services                                       |                          |                        |                        |                |               |                        |                        | -              |
| Management and administration                             | 3,745,870                | -                      | -                      | 3,745,870      | 3,074,730     | -                      | -                      | 3,074,730      |
| Fund raising  | 3,469,635                | -                      | -                      | 3,469,635      | 3,222,648     | -                      | -                      | 3,222,648      |
|   |                          |                        |                        |                |               |                        |                        | -              |
| Total expenses  | 22,590,484               | -                      | -                      | 22,590,484     | 29,487,145    | -                      | -                      | 29,487,145     |
| Change in net assets                                      | 2,501,797                | 15,754,809             | 9,685,332              | 27,941,938     | 2,122,147     | 4,000,183              | 5,613,289              | 11,735,619     |
| Net assets, beginning                                     | 21,574,206               | 67,649,684             | 82,213,796             | 171,437,686    | 19,452,059    | 63,649,501             | 76,600,507             | 159,702,067    |
| Net assets, ending  | \$ 24,076,003            | \$ 83,404,493          | \$ 91,899,128          | \$ 199,379,624 | \$ 21,574,206 | \$ 67,649,684          | \$ 82,213,796          | \$ 171,437,686 |

See notes to financial statements.

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
STATEMENTS OF CASH FLOWS**

|   | <b>Years Ended December 31,</b> |                            |
|---|---------------------------------|----------------------------|
|   | <b>2007</b>                     | <b>2006</b>                |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>   |                                 |                            |
| Change in net assets  | \$ 27,941,938                   | \$ 11,735,619              |
| Adjustments to reconcile change in net assets to net cash used in operating activities: |                                 |                            |
| Contributions of securities and property  | (2,510,393)                     | (2,145,103)                |
| Contributions restricted for long-term investment                                       | (3,815,059)                     | (1,615,906)                |
| Net realized and unrealized gains on investments  | (7,474,975)                     | (10,358,180)               |
| Depreciation on building and equipment  | 386,527                         | 382,025                    |
| Increase in value of split-interest agreements  | (136,743)                       | (785,852)                  |
| Changes in:   |                                 |                            |
| Pledges receivable  | (3,128,925)                     | 2,010,983                  |
| Inventories and other assets  | (13,030)                        | (118,385)                  |
| Accounts payable and accrued expenses   | (197,297)                       | 113,286                    |
| Proffer payable   | (4,071,088)                     | (7,117,819)                |
| Deferred revenue  | 299,448                         | 105,740                    |
| Liabilities associated with charitable remainder trusts                                 | 411,054                         | 82,106                     |
| Net cash provided by (used in) operating activities                                     | <u>7,691,457</u>                | <u>(7,711,486)</u>         |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>   |                                 |                            |
| Purchase of investments   | (47,316,408)                    | (48,694,610)               |
| Proceeds from the sale and maturity of investments                                      | 35,503,831                      | 55,170,946                 |
| Purchase of building and equipment  | (110,129)                       | (72,256)                   |
| Receipts from settlement of split interest agreements                                   | 1,025,470                       | 151,992                    |
| Purchase of investments restricted for long-term purposes                               | (415,227)                       | (85,705)                   |
| Net cash (used in) provided by investing activities                                     | <u>(11,312,463)</u>             | <u>6,470,367</u>           |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>   |                                 |                            |
| Proceeds from borrowings  | 8,950                           | 682,176                    |
| Proceeds from contributions restricted for investment in endowment                      | 3,815,059                       | 1,615,906                  |
| Net cash provided by financing activities   | <u>3,824,009</u>                | <u>2,298,082</u>           |
| <b>NET INCREASE IN CASH</b>   | <b>203,003</b>                  | <b>1,056,963</b>           |
| <b>Cash, beginning of year</b>  | <u><b>1,626,883</b></u>         | <u><b>569,920</b></u>      |
| <b>Cash, end of year</b>  | <u><b>\$ 1,829,886</b></u>      | <u><b>\$ 1,626,883</b></u> |
| <b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>                                 |                                 |                            |
| Cash payments for interest  | <u><b>\$ 178,436</b></u>        | <u><b>\$ 60,824</b></u>    |

See notes to financial statements.

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2007 and 2006**

**NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Organization**

The Association of Graduates of the United States Military Academy (Association) is an organization dedicated to furthering the ideals and promoting the welfare of the United States Military Academy (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 rules and has been classified as an organization that is not a private foundation.

**Summary of Significant Accounting Policies**

**Basis of accounting:**

The financial statements of the Association have been prepared on the accrual basis of accounting and accordingly reflect all significant receivables, payables, and other liabilities.

**Basis of presentation:**

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board in its Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not-for-Profit Organizations*. Under SFAS No. 117, the Association is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets 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 the 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.

**Cash and cash equivalents:**

The Association considers highly liquid debt instruments with original maturities of three months or less to be cash equivalents. Cash equivalents consist of funds held in a sweep account in a financial institution.

The Association places its cash and cash equivalents with high quality financial institutions, balances generally exceed the FDIC insurance limits.

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2007 and 2006**

**NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**  
(Continued)

**Summary of Significant Accounting Policies** (Continued)

**Promises to give:**

Unconditional promises to give are recognized as contribution revenue in the period received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Promises to give are recorded at net realizable value if expected to be collected in one year. Promises to give to be received after one year are discounted at an appropriate discount 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 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.

Proffers represent unconditional promises to grant funds to the United States Military Academy that have been authorized prior to year end, but remain unpaid as of the statement of financial position date.

The Association is a party to various types of split-interest agreements whereby the donor makes an initial gift in which the Association has a beneficial interest but is not the sole beneficiary. These agreements include charitable remainder trusts, pooled life income funds and gift annuities.

**Inventories:**

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

**Investments:**

Investments consist principally of marketable debt and equity securities and are carried at market value at the date of the statement of financial position.

Investments are primarily pooled in investment portfolios containing multiple funds. On a quarterly basis investment income is allocated to the individual funds within the pool based upon the market value of each fund's cash and investments.

For endowments whose income is restricted for specific purposes, the Association uses a total return policy whereby a fixed percentage (4% for 2007 and 2006) of the prior twelve quarters' market value of permanently restricted investments and their related temporarily restricted income accounts is distributed in the ensuing year for the intended endowment purposes. For endowments whose income accounts reflected negative balances at year end, the distribution is limited to interest and dividend income earned by the endowment fund during the calendar year.

**Property and equipment:**

Property and equipment are carried at cost or, if donated, at the approximate fair value at the date of donation. Depreciation is computed using primarily the straight-line method. The records automation system and other equipment are depreciated over estimated useful lives of between three and ten years, the building over its useful life of forty years.



**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2007 and 2006**

**NOTE 1 – ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**  
(Continued)

**Summary of Significant Accounting Policies (Continued)**

**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 market value at date of donation. Absent donor restrictions to the contrary, donated securities are sold immediately. Support and revenue, for the year ended December 31, 2007, includes approximately \$1,563,000 of donated securities (approximately \$1,791,000 in 2006).

**Restricted and unrestricted revenue and support:**

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or 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 revenue:**

Deferred revenue consists of advance payments for subscriptions and advertising relating to the Association's two publications, The Assembly and The Register. Amounts received and not yet earned are reported as deferred revenue.

**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.

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2007 and 2006**

**NOTE 2 – PLEDGES RECEIVABLE**

Pledges receivable include unconditional promises to give. The Association recognizes potentially uncollectible pledges at their gross value and provides an allowance for the estimated uncollectible amount. Pledges receivable, net of the discount to present value (at rates ranging from 3% to 7%) and the allowance for uncollectible pledges, are as follows:

|  | <b>December 31,</b>  |                      |
|--|----------------------|----------------------|
|  | <b>2007</b>          | <b>2006</b>          |
| Receivable in less than one year         | \$13,706,898         | \$ 12,437,873        |
| Receivable in one year to five years     | 11,746,037           | 9,721,716            |
| Receivable in more than five years       | <u>3,427,599</u>     | <u>1,110,264</u>     |
| Total unconditional promises to give     | 28,880,534           | 23,269,853           |
| Less allowance for uncollectible pledges | (9,408,216)          | (7,365,896)          |
| Less discounts to net present value      | <u>(1,407,243)</u>   | <u>(967,807)</u>     |
| Net unconditional promises to give       | <u>\$ 18,065,075</u> | <u>\$ 14,936,150</u> |

**NOTE 3 – INVESTMENTS**

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

|  | <b>December 31,</b>   |                       |
|--|-----------------------|-----------------------|
|  | <b>2007</b>           | <b>2006</b>           |
| Investments                            | \$ 160,521,413        | \$ 139,680,215        |
| Investments - pooled life income funds | 2,544,690             | 2,527,635             |
| Investments - gift annuities           | 2,131,702             | 1,741,431             |
| Investments - gift annuity reserve     | <u>95,974</u>         | <u>88,803</u>         |
| Investments restricted by agreements   | <u>4,772,366</u>      | <u>4,357,869</u>      |
|  | <u>\$ 165,293,779</u> | <u>\$ 144,038,084</u> |

Investments are comprised of the following:

|  | <b>December 31,</b>   |                       |
|--|-----------------------|-----------------------|
|  | <b>2007</b>           | <b>2006</b>           |
| Short-term investments (money markets) | \$ 349,957            | \$ 186,267            |
| Fixed income securities                | 63,742,490            | 51,260,165            |
| Equity securities                      | 79,751,172            | 75,282,054            |
| Alternative investments                | 21,068,717            | 16,756,427            |
| Mutual funds                           | 274,626               | 269,901               |
| Other                                  | <u>106,817</u>        | <u>283,270</u>        |
|  | <u>\$ 165,293,779</u> | <u>\$ 144,038,084</u> |

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2007 and 2006**

**NOTE 3 – INVESTMENTS** (Continued)

Return on investments is comprised of the following:

|                               | <b>December 31,</b> |                     |
|-------------------------------|---------------------|---------------------|
|                               | <b>2007</b>         | <b>2006</b>         |
| Unrestricted                  |                     |                     |
| Interest, dividends and other | \$ 2,078,230        | \$ 1,359,493        |
| Investment expenses           | (278,238)           | (239,439)           |
| Net gains                     | <u>1,910,221</u>    | <u>2,664,403</u>    |
|                               | <u>\$ 3,710,213</u> | <u>\$ 3,784,457</u> |
| Temporarily restricted        |                     |                     |
| Interest, dividends and other | \$ 2,971,417        | \$ 2,826,126        |
| Investment expenses           | (720,802)           | (809,871)           |
| Net gains                     | <u>5,564,754</u>    | <u>7,693,777</u>    |
|                               | <u>\$ 7,815,369</u> | <u>\$ 9,710,032</u> |

Investment earnings (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. The total amount of capital contributed to the partnerships by the Association at December 31, 2007 was \$3,309,669. This investment is included in alternate investments. As capital calls are received, other investments are sold. The proceeds along with available cash are used to fulfill the capital call.

**NOTE 4 – SPLIT INTEREST AGREEMENTS**

The Association is the beneficiary of various split interest agreements as follows:

**Irrevocable Trust**

A donor has established an irrevocable trust held by a third party trustee. The trust consists of an investment portfolio. Pursuant to the trust agreement, 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 distributed to the Association to establish a permanently restricted fund. The present value of the estimated amount to be received was calculated using a discount rate of 6% and the applicable mortality table.

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2007 and 2006**

**NOTE 4 – SPLIT INTEREST AGREEMENTS (Continued)**

**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 the trusts' terms, the remaining assets are available for the Association's use, subject to the donor-imposed restrictions. Assets held in charitable remainder trusts totaled \$5,358,062 at December 31, 2007 (\$5,189,125 in 2006) and are reported at fair 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 (\$2,860,662 and \$2,449,608 at December 31, 2007 and 2006, respectively) is calculated using a discount rate of 3% and applicable mortality tables.

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 \$3,986,884 at December 31, 2007 (\$4,186,657 at 2006).

**Perpetual Trust**

A donor has established a perpetual trust under which the Association receives 35% of the Trust's 5% annual distribution. The net present value of future cash flows expected to be received from the Trust approximated \$1,189,000 at December 31, 2007 (\$1,200,000 in 2006).

**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 discount for future interest (6.2%) is recorded as deferred income and approximated \$925,000 at December 31, 2007 (\$952,000 in 2006).

**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. In certain instances, the Association purchases annuity contracts from insurance companies to fund these obligations. 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 at the present value (discounted at 3.4% for gift annuities received in 2004 and later and at 4.2% for gift annuities received prior to 2004) of the future cash flows expected to be paid to the designated beneficiary using the applicable mortality tables. At December 31, 2007, the future liability approximated \$1,375,000 (\$1,128,000 in 2006), and is included in deferred revenue in the statement of financial position.

**THE ASSOCIATION OF GRADUATES OF THE  
UNITED STATES MILITARY ACADEMY  
NOTES TO FINANCIAL STATEMENTS  
December 31, 2007 and 2006**

**NOTE 4 – SPLIT INTEREST AGREEMENTS (Continued)**

**Gift Annuities (Continued)**

As required by insurance law, the Association maintains an annuity reserve equal to greater than 110% of associated liabilities. The reserve requirement is met using the specific assets and liabilities of the pooled life income funds and gift annuities as well as an additional reserve. At December 31, 2007, the Association's gift annuity and pooled life income fund assets and liabilities amounted to \$4,676,392 and \$2,768,437 respectively (\$4,269,066 and \$2,468,989 in 2006). At December 31, 2007, assets equal 169% of liabilities (173% in 2006), thus fulfilling the requirement under the law. The Association maintains an additional reserve, included in investments, in a portfolio at a financial institution. At December 31, 2007, the fair value of the amount reserved was approximately \$96,000 (\$89,000 in 2006). The Association was in full compliance with reserve requirements under the insurance law at December 31, 2007 and 2006.

The change in split-interest agreements for 2007 and 2006 was as follows:

|                              | <u>Irrevocable<br/>Trust</u> | <u>Remainder<br/>Trusts</u> | <u>Perpetual<br/>Trust</u> | <u>Total Split<br/>Interest<br/>Trusts</u> | <u>Pooled Life<br/>Income<br/>Funds</u> | <u>Gift<br/>Annuities</u> |
|------------------------------|------------------------------|-----------------------------|----------------------------|--|---|---------------------------|
| Balance at December 31, 2005 | \$ 4,844,500                 | \$ 9,008,903                | \$ 1,110,106               | \$ 14,963,509                              | \$ 2,536,881                            | \$ 1,655,662              |
| Contributions                | -                            | 353,748                     | -                          | 353,748                                    | -                                       | 160,461                   |
| Distributions                | -                            | (151,992)                   | -                          | (151,992)                                  | (109,329)                               | (210,444)                 |
| Change in value              | <u>528,500</u>               | <u>165,123</u>              | <u>96,806</u>              | <u>790,429</u>                             | <u>100,083</u>                          | <u>135,752</u>            |
| Balance at December 31, 2006 | 5,373,000                    | 9,375,782                   | 1,206,912                  | 15,955,694                                 | 2,527,635                               | 1,741,431                 |
| Contributions                | -                            | 1,097,952                   | -                          | 1,097,952                                  | -                                       | 418,076                   |
| Distributions                | -                            | (1,025,470)                 | -                          | (1,025,470)                                | (133,341)                               | (167,612)                 |
| Change in value              | <u>116,000</u>               | <u>(103,318)</u>            | <u>(18,156)</u>            | <u>(5,474)</u>                             | <u>150,396</u>                          | <u>139,807</u>            |
| Balance at December 31, 2007 | <u>\$ 5,489,000</u>          | <u>\$ 9,344,946</u>         | <u>\$ 1,188,756</u>        | <u>\$ 16,022,702</u>                       | <u>\$ 2,544,690</u>                     | <u>\$ 2,131,702</u>       |

**NOTE 5 – BUILDING AND EQUIPMENT**

A summary of building and equipment is as follows:

|                               | <u>December 31,</u> |                     |
|-------------------------------|---------------------|---------------------|
|                               | <u>2007</u>         | <u>2006</u>         |
| Records automation system     | \$ 906,907          | \$ 867,967          |
| Other equipment               | 267,449             | 238,115             |
| Building                      | <u>9,432,480</u>    | <u>9,390,625</u>    |
|                               | 10,606,836          | 10,496,707          |
| Less accumulated depreciation | <u>4,023,056</u>    | <u>3,636,528</u>    |
|                               | <u>\$ 6,583,780</u> | <u>\$ 6,860,179</u> |

Depreciation expense for the year ended December 31, 2007 was \$386,527 (\$382,025 in 2006).

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**NOTE 6 – PROFFER PAYABLE**

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 made and generally are paid within a one year period.

**NOTE 7 – NOTES PAYABLE**

The Association has entered into the following lines of credit:

- Demand Grid Note dated December 12, 2005 with an original face value of \$3,000,000 for working capital and \$7,000,000 for an indoor athletic training facility, with interest rate options of LIBOR plus 1.4% or Prime Rate minus 1.25%. These Grid Notes contain certain financial covenants, including maintaining a minimum of \$70,000,000 in investments of which no less than \$5,000,000 are unrestricted and a maximum debt to net asset ratio of no greater than .50 to 1.0. The face value of the \$7,000,000 Demand Grid Note decreases as the principal is repaid and is not allowed to be increased. There was an outstanding balance \$2,345,450 against the indoor athletic training facility note at December 31, 2007 (\$2,336,500 in 2006).

Interest expense for the year ended December 31, 2007 was approximately \$284,000 (\$60,800 in 2006).

**NOTE 8 – DEFERRED COMPENSATION**

The Association has arrangements with its executive officers whereby specified amounts of their compensation is deferred. These amounts are invested on behalf of the executives and are payable upon their retirement. At December 31, 2007, the Association's obligation pursuant to these arrangements was approximately \$309,000 (\$310,000 in 2006).

**NOTE 9 – PENSION PLAN**

The Association sponsors a defined contribution retirement plan under IRC 403(b) 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 \$212,000 for the year ended December 31, 2007 (\$205,000 for 2006).

**NOTE 10 – PROPERTY LEASE**

In 1992, the Association entered into a 50 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.

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**NOTE 11 – RESTRICTIONS ON NET ASSETS**

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

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

|   | <u>December 31,</u>  |                      |
|---|----------------------|----------------------|
|   | <u>2007</u>          | <u>2006</u>          |
| Permanent endowment with no restrictions on the use of income   | \$ 21,935,615        | \$ 19,350,158        |
| Permanent endowments with income restricted to the support of projects and programs related to the United States Military Academy and its graduates | <u>69,963,513</u>    | <u>62,863,638</u>    |
|   | <u>\$ 91,899,128</u> | <u>\$ 82,213,796</u> |

**NOTE 12 – 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 more accurately reflect the intent of a contribution. Generally, transfers are a result of a donor's request to change the designated purpose of a previously recorded contribution. In other instances transfers are recorded when a donor requests that the balance remaining from contributions previously given and used for a specific, temporarily restricted purpose, be used to establish a permanently restricted fund.

**NOTE 13 – 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.

**NOTE 14 – DESCRIPTION OF PROGRAM AND SUPPORTING SERVICES**

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

**Alumni Services** - Encompasses activities and services provided for living graduates including the maintenance of detailed biographical and historical records on graduates of the United States Military Academy.

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**NOTE 14 – DESCRIPTION OF PROGRAM AND SUPPORTING SERVICES (Continued)**

**Educational and Historical** - Comprises activities for the dissemination of information on the history, objectives and methods of the United States Military Academy to include the encouragement of the study of military science and leadership and to enhance the image of the United States Military Academy. The Association recorded approximately \$9,000,000 of proffers to the United States Military Academy in 2007 (\$16,000,000 in 2006), related to educational and historical programs and support services.

**Publications** - Disseminates information on the history, activities, objectives and methods of the United States Military Academy through two publications.

**Management and General** - Relates to the overall direction of the Association and includes expenses for the operation of the gift shop.

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