

Financial Statements and Report of Independent
Certified Public Accountants

The University of Cincinnati Foundation

June 30, 2017 and 2016



Dave Yost • Auditor of State

Board of Trustees
The University of Cincinnati Foundation
51 Goodman Drive
Suite 100
Cincinnati, Ohio 45219

We have reviewed the *Independent Auditor's Report* of The University of Cincinnati Foundation, Hamilton County, prepared by Plante and Moran, PLLC, for the audit period July 1, 2016 through June 30, 2017. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The University of Cincinnati Foundation is responsible for compliance with these laws and regulations.

A handwritten signature in black ink that reads "Dave Yost".

Dave Yost
Auditor of State

October 16, 2017

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Independent Auditor's Report

To the Board of Trustees
The University of Cincinnati Foundation

Report on the Financial Statements

We have audited the accompanying financial statements of The University of Cincinnati Foundation (the "Foundation"), which comprise the statement of financial position as of June 30, 2017 and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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 University of Cincinnati Foundation as of June 30, 2017 and the change in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of Trustees
The University of Cincinnati Foundation

Supplementary Information

We have audited the financial statements of The University of Cincinnati Foundation as of and for the year ended June 30, 2017 and have issued our report thereon dated September 19, 2017, which contained an unmodified opinion on those financial statements. Our audit was performed for the purpose of forming an opinion on the 2017 financial statements as a whole. The supplemental schedule of detail of operating expenses and supplemental schedule of activities - unrestricted net assets (deficit) is presented for the purpose of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the 2017 financial statements. The information has been subjected to the auditing procedures applied in the audit of the 2017 financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the 2017 financial statements as a whole.

Emphasis of Matter

As described in Note H to the financial statements, the Foundation has investments valued at approximately \$343,443,000 (69 percent of net assets) and \$298,875,000 (67 percent of net assets) as of June 30, 2017 and 2016, respectively, whose fair values have been estimated by management in the absence of readily determinable fair values. Management's estimates are based on information provided by the University of Cincinnati. Our opinion is not modified with respect to this matter.

Report on Prior Year Financial Statements

The financial statements of The University of Cincinnati Foundation as of June 30, 2016 were audited by other auditors, whose report dated October 5, 2016 expressed an unmodified opinion on those statements.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 19, 2017 on our consideration of The University of Cincinnati Foundation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering The University of Cincinnati Foundation's internal control over financial reporting and compliance.

Plante & Moran, PLLC

September 19, 2017

THE UNIVERSITY OF CINCINNATI FOUNDATION

STATEMENTS OF FINANCIAL POSITION

June 30, 2017 and 2016

ASSETS	<u>2017</u>	<u>2016</u>
Cash and cash equivalents	\$ 10,349,843	\$ 15,479,099
Due from University of Cincinnati	980,246	2,163,938
Due from UC Health Foundation	763,054	250,341
Accrued interest receivable	655,052	545,200
Stock proceeds receivable	282,270	68,878
Prepaid expenses	433,777	274,328
Pledges receivable, net of allowance	94,699,382	90,143,068
Trusts held by others	10,157,614	9,633,268
Cash surrender value of life insurance policies	1,288,061	1,225,565
Other	96,914	14,149
Investments:		
Mutual funds	23,523,168	20,363,020
Common stocks and exchange traded funds	11,691,018	11,414,580
Other	10,753,057	2,566,112
Corporate bonds	9,172,872	9,886,632
U.S. Government and agency obligations	4,209,417	3,411,108
Real estate	840,000	215,000
University pooled investments	342,520,697	298,660,384
Total investments	<u>402,710,229</u>	<u>346,516,836</u>
Property and equipment:		
Leasehold improvements, net of accumulated amortization of \$1,374,707 in 2017 and \$1,265,810 in 2016	174,804	205,803
Equipment and software, net of accumulated depreciation of \$3,037,463 in 2017 and \$1,982,328 in 2016	<u>3,035,097</u>	<u>3,896,159</u>
	<u>\$ 525,626,343</u>	<u>\$ 470,416,632</u>
LIABILITIES AND NET ASSETS		
LIABILITIES		
Accounts payable	\$ 965,715	\$ 886,888
Accrued liabilities	1,028,011	1,000,418
Accrued compensated absences	768,712	706,165
Agency payable	12,580,686	14,531,146
Deferred support	232,573	-
Trusts held for the benefit of others	1,455,514	1,368,252
Refundable deposits	779,384	731,817
Accrued interest income due to investment pool	341,864	281,988
Present value of annuities payable	<u>6,619,239</u>	<u>6,462,009</u>
TOTAL LIABILITIES	<u>24,771,698</u>	<u>25,968,683</u>
NET ASSETS (DEFICIT)		
Unrestricted	(19,072,101)	(30,023,140)
Temporarily restricted	175,571,158	147,247,583
Permanently restricted	<u>344,355,588</u>	<u>327,223,506</u>
TOTAL NET ASSETS	<u>500,854,645</u>	<u>444,447,949</u>
	<u>\$ 525,626,343</u>	<u>\$ 470,416,632</u>

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

THE UNIVERSITY OF CINCINNATI FOUNDATION

STATEMENT OF ACTIVITIES

Year ended June 30, 2017

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenues and other additions:				
Contributions:				
University	\$ 497,758	\$ 55,016,420	\$ 15,280,597	\$ 70,794,775
Donated services	198,766	-	-	198,766
University fee	11,971,542	24,975	-	11,996,517
UC Health Foundation Fee	2,105,297	-	-	2,105,297
Assessment fee	11,206,249	-	-	11,206,249
Change in value of split interest agreements	(4,617)	151,815	377,148	524,346
Other income	319,788	675,393	238,037	1,233,218
Investment income:				
Dividend and interest income	338,720	6,928,905	54,739	7,322,364
Net unrealized and realized gains	9,418,738	19,656,560	2,867,007	31,942,305
Pledge loss	-	-	(1,699,765)	(1,699,765)
Net assets released from restrictions - satisfaction of donor restrictions	53,892,824	(53,892,824)	-	-
Total revenues and other additions	<u>89,945,065</u>	<u>28,561,244</u>	<u>17,117,763</u>	<u>135,624,072</u>
Expenses and other deductions:				
Distributions to University of Cincinnati	50,471,635	-	-	50,471,635
Operating expenses	25,433,764	-	-	25,433,764
Assessment fee	5,073,849	-	-	5,073,849
Total expenses	<u>80,979,248</u>	<u>-</u>	<u>-</u>	<u>80,979,248</u>
Change in present value of annuities payable	-	468,823	(11,388)	457,435
Total expenses and other deductions	<u>80,979,248</u>	<u>468,823</u>	<u>(11,388)</u>	<u>81,436,683</u>
Change in net assets before acquisition income	8,965,817	28,092,421	17,129,151	54,187,389
Excess of fair value of net assets over consideration in acquisition of the acquired entity	1,985,222	231,154	2,931	2,219,307
Change in net assets	10,951,039	28,323,575	17,132,082	56,406,696
Net assets (deficit) at beginning of year	(30,023,140)	147,247,583	327,223,506	444,447,949
Net assets (deficit) at end of year	<u>\$ (19,072,101)</u>	<u>\$ 175,571,158</u>	<u>\$ 344,355,588</u>	<u>\$ 500,854,645</u>

The accompanying notes are an integral part of this financial statement.

THE UNIVERSITY OF CINCINNATI FOUNDATION

STATEMENT OF ACTIVITIES

Year ended June 30, 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues and other additions:				
Contributions:				
University	\$ 586,809	\$ 55,025,154	\$ 15,932,155	\$ 71,544,118
Foundation	-	631	-	631
University fee	8,629,717	-	-	8,629,717
UC Alumni Association fee	1,236,036	-	-	1,236,036
UC Health Foundation fee	1,430,343	-	-	1,430,343
Assessment fee	11,325,596	-	-	11,325,596
Change in value of split interest agreements	8,450	86,597	80,763	175,810
Other income	228	619,197	1,776,073	2,395,498
Investment income:				
Dividend and interest income	340,159	9,101,319	58,758	9,500,236
Net unrealized and realized gains (losses)	(13,545,967)	553,010	1,270,774	(11,722,183)
Pledge loss	-	(2,604,117)	(295,724)	(2,899,841)
Net assets released from restrictions - satisfaction of donor restrictions	51,731,020	(51,731,020)	-	-
Total revenues and other additions	<u>61,742,391</u>	<u>11,050,771</u>	<u>18,822,799</u>	<u>91,615,961</u>
Expenses and other deductions:				
Distributions to University of Cincinnati	45,719,993	-	-	45,719,993
Operating expenses	22,540,299	-	-	22,540,299
Assessment fee	4,784,834	-	-	4,784,834
Total expenses	<u>73,045,126</u>	<u>-</u>	<u>-</u>	<u>73,045,126</u>
Change in present value of annuities payable	-	323,468	(161,591)	161,877
Total expenses and other deductions	<u>73,045,126</u>	<u>323,468</u>	<u>(161,591)</u>	<u>73,207,003</u>
Change in net assets	(11,302,735)	10,727,303	18,984,390	18,408,958
Net assets (deficit) at beginning of year	(18,720,405)	136,520,280	308,239,116	426,038,991
Net assets (deficit) at end of year	<u>\$ (30,023,140)</u>	<u>\$ 147,247,583</u>	<u>\$ 327,223,506</u>	<u>\$ 444,447,949</u>

The accompanying notes are an integral part of this financial statement.

THE UNIVERSITY OF CINCINNATI FOUNDATION

STATEMENTS OF CASH FLOWS

Years ended June 30, 2017 and 2016

	2017	2016
Operating activities:		
Payments to the University of Cincinnati	\$ (50,460,168)	\$ (46,861,408)
University fees, assessment fees and other	21,857,027	19,750,895
Cash paid for compensation	(16,976,997)	(15,110,639)
Cash received for gifts	39,712,359	25,963,502
Investment income available for distribution	6,517,432	9,024,700
Cash paid for operating expenses	(6,337,725)	(6,046,273)
Net cash used in operating activities	(5,688,072)	(13,279,223)
Investing activities:		
Proceeds from sale of investments	24,482,923	26,443,467
Purchase of investments	(48,729,975)	(36,743,386)
Purchase of property and equipment	(550,358)	(1,193,379)
Addition of Alumni Assets	2,219,307	-
Net cash used in investing activities	(22,578,103)	(11,493,298)
Financing activities:		
Proceeds from contributions to endowment and similar funds	22,441,839	32,736,286
Investment income restricted for reinvestment	695,080	771,785
Net cash provided by financing activities	23,136,919	33,508,071
Net (decrease) increase in cash and cash equivalents	(5,129,256)	8,735,550
Cash and cash equivalents, beginning of year	15,479,099	6,743,549
Cash and cash equivalents, end of year	\$ 10,349,843	\$ 15,479,099
Reconciliation of change in net assets to net cash used in operating activities:		
Change in net assets	\$ 54,187,389	\$ 18,408,958
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Provision for losses on pledges receivable	1,384,616	2,920,338
Depreciation and amortization	1,434,349	869,070
Loss on disposal of property and equipment	4,035	1,861
Decrease (increase) in due from University of Cincinnati	1,183,692	(437,160)
Increase in due from UC Health Foundation	(512,713)	(250,341)
(Increase) decrease in accrued interest receivable	(109,852)	296,251
Increase in stock proceeds receivable	(213,392)	(47,786)
(Increase) decrease in prepaid expenses	(159,449)	203,734
Increase in pledges receivable	(5,940,931)	(15,281,926)
Increase in cash surrender value of life insurance policies	(62,496)	(60,620)
(Increase) decrease in other assets	(82,765)	2,308
Increase (decrease) in accounts payable	78,827	(510,988)
Increase in accrued liabilities	27,593	188,647
Increase in accrued compensated absences	62,547	20,606
(Decrease) increase in agency payable	(1,950,460)	2,795,650
Increase in trusts held for the benefit of others	87,262	451,434
Increase (decrease) in refundable deposits	47,567	(54,100)
Increase in deferred support	232,573	-
Increase (decrease) in accrued interest income due to investment pool	59,876	(262,104)
Increase (decrease) in present value of annuities payable	157,230	(571,357)
Contributions to endowment and similar funds	(22,441,839)	(32,736,286)
Change in value of split interest agreements	(524,346)	(175,810)
Investment income restricted for reinvestment	(695,080)	(771,785)
Net unrealized and realized (gains) losses	(31,942,305)	11,722,183
Net cash used in operating activities	\$ (5,688,072)	\$ (13,279,223)

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

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE A – DESCRIPTION OF ORGANIZATION

The University of Cincinnati Foundation (the Foundation) is a not-for-profit organization that operates for the benefit of the University of Cincinnati (the University). Its principal function is to solicit, receive, hold, invest and administer funds and to make distributions to the benefit of the University. The Foundation also provides executive, administrative and fund raising services to the UC Health Foundation (UCHF).

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Basis of Presentation

The financial statements of the Foundation are presented on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (US GAAP). Balances and transactions are presented based on the existence or absence of donor-imposed restrictions. Resources for various purposes are classified into net assets classes that are in accordance with activities or objectives specified by donors.

Net assets, revenues, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

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

Temporarily restricted – Net assets subject to donor-imposed stipulations that may or will be met either by actions of the Foundation and/or the passage of time, and the portion of perpetual endowment funds subject to a time restriction under an enacted version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA).

Permanently restricted – Net assets subject to donor-imposed stipulations that must be maintained permanently by the Foundation. Generally, the donors of these assets permit the Foundation to use all or part of the income earned on related investments for general or specific purposes.

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of events specified by the donors or by the change of restrictions specified by the donors. In 2017, the Foundation released approximately \$53,893,000 in restricted assets (\$7,478,000 for operations, maintenance, plant, \$26,162,000 for college programs, \$3,405,000 for instruction, \$835,000 for auxiliary, \$7,189,000 for scholarship, \$2,325,000 for academic support, \$4,333,000 for research and \$2,166,000 for other). In 2016, the Foundation released approximately \$51,731,000 in restricted assets (\$6,947,000 for operations, maintenance, plant, \$27,166,000 for college programs, \$2,948,000 for instruction, \$815,000 for auxiliary, \$7,025,000 for scholarship, \$2,608,000 for academic support, \$2,589,000 for research and \$1,633,000 for other).

Contributions received by the Foundation for the benefit of the University are classified as University contributions on the Statements of Activities. Revenues from sources other than contributions are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Contributions are reported as increases in the appropriate category of net assets. Expenses are reported as decreases in unrestricted net assets. Expirations of temporary restrictions recognized on net assets (i.e., the

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

1. Basis of Presentation (continued)

donor-imposed purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as released from restriction from temporarily restricted net assets to unrestricted net assets. The Foundation recognizes temporarily restricted contributions and investment income in which donor-imposed restrictions are met within the same period as temporarily restricted net assets and then reclassifies the revenue to unrestricted net assets through net assets released from restriction on the accompanying Statements of Activities. Temporary restrictions on gifts to acquire long-lived assets are considered met in the period in which the assets are acquired or placed in service.

Occasionally, the Foundation receives modifications or clarifications to gift agreements or pledges made in previous years. These modifications and clarifications are reviewed by Foundation management for approval, and once approved, may result in a reclassification among net asset classes or a pledge loss if the donor specifies a beneficiary other than the Foundation or the University. No such modifications or clarifications occurred during the years ended June 30, 2017 or 2016.

Gains and losses on investments are reported as increase or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulations or by law.

Contributions, including unconditional promises to give, are recognized as revenues in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value at the date of gift. Contributions to be received after one year are discounted at a rate commensurate with the risk involved. Amortization of the discount is recorded as additional contribution revenue and used in accordance with donor-imposed restrictions, if any, on the contributions.

Allowance is made for uncollectible contributions based upon management's judgment and analysis of the creditworthiness of the donors, past collection experience and other relevant factors. Unconditional promises to give of \$10,000 or more, and more than one year old, are evaluated annually for collectability. An appropriate reserve for each pledge is established based on the evaluation. Pledges of this size are not written off without senior management approval. Unconditional promises to give of less than \$10,000, expected to be satisfied by multiple payments, are generally completely reserved once twelve months have elapsed from receipt of the last pledge payment. These pledges are written off once the development officer assigned to the donor believes that further collection efforts will not be successful. Finally, unconditional promises to give arising from Telefund and other annual giving programs are generally written off to pledge loss once the donor has failed to respond to eleven consecutive monthly pledge reminders.

Contributions in the form of charitable gift annuities are recognized as revenue at fair value when received, and an annuity payment liability is recognized at the present value of future cash flows expected to be paid to the donors. Payments made to donors reduce the annuity liability. Adjustments to the annuity liability to reflect changes in the life expectancy of the donor are recognized in the Statements of Activities as a change in present value of annuities payable.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2. Cash Equivalents

Cash equivalents consist principally of overnight funds, money market securities and certificates of deposit. As of June 30, 2017 and 2016, approximately \$11,996,000 and \$16,998,000 respectively, of cash and cash equivalents were in excess of federally insured limits. The overnight funds were collateralized by U.S. government backed securities. Cash equivalents are carried at amortized cost, and mature in 90 days or less.

3. Investment Securities

The Foundation's investments are reported at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

4. Property and Equipment

Property and equipment are recorded at cost (or fair value in the case of a gift) less accumulated depreciation and amortization. The estimated useful lives are principally four years for automobile and computer equipment, five years for office equipment, and five years for software. All assets are depreciated/amortized using the straight-line method over the estimated useful lives of the assets.

5. Agency Transactions

The Foundation has received funds whereby the Foundation is named as the trustee of the related assets. The gift arrangements direct the Foundation to distribute portions of the related assets to other charitable organizations when restrictions are met. A portion of the assets will benefit the Foundation. The amount of assets that are due to other third party organizations is recorded as a payable of approximately \$12,581,000 and \$14,531,000 at June 30, 2017 and 2016, respectively.

6. Income Taxes

The Foundation is a not-for-profit organization as defined under Section 501(c)(3) of the Internal Revenue Code and, as such, is exempt from federal income taxes.

The Foundation evaluates its uncertain tax positions as to whether it is more likely than not a tax position could be sustained in the event of an audit by the applicable taxing authority. Accordingly, a loss contingency is recognized when it is probable that a liability has been incurred as of the date of the financial statements, and the amount of the loss can be reasonably estimated. The amount recognized is subject to estimate and management judgment with respect to the likely outcome of each uncertain tax position. The amount that is ultimately sustained for an individual uncertain tax position or for all uncertain tax positions in the aggregate could differ from the amount recognized. Open tax years for the Foundation include 2016, 2015 and 2014. As of June 30, 2017 and 2016, the Foundation has no assets or liabilities recorded related to uncertain tax positions.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

7. Use of Estimates

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

8. Risks and Uncertainties

The Foundation holds a variety of investments, the underlying securities of which are exposed to various risks, such as interest rate, market and credit risk. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in the value of investment securities would occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

9. Fair Value Measurements

Fair value is generally determined based on quoted market prices in active markets for identical assets or liabilities. If quoted market prices are not available, the Foundation uses valuation techniques that place greater reliance on observable inputs and less reliance on unobservable inputs. In measuring fair value, the Foundation may make adjustments for risks and uncertainties, if a market participant would include such an adjustment in its pricing.

10. Functional Reporting of Expenses

The Foundation was created to provide support to the University. Therefore, program services consist of distributions to University of Cincinnati in the accompanying Statement of Activities. Support services consist of the Foundation's operating expenses, which primarily relate to development and fundraising activities, as well as the assessment fee charged against funds held by the Foundation which is part of general and administrative expenses. See also Note O.

11. New Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (Topic 606), which will supersede the current revenue recognition requirements in Topic 605, Revenue Recognition. The ASU is based on the principle that revenue is recognized to depict the transfer of 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 ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The Foundation's primary revenue sources are not expected to be significantly impacted by the standard; however, a complete review of all revenue sources has not yet been completed. In addition, management is currently analyzing the disclosures that will be required with this pronouncement. The new guidance will be effective for the Foundation's year ending June 30, 2020.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

In February 2016, the FASB issued ASU 2016-02, Leases, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the balance sheet. The reporting of lease-related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the Foundation's year ending June 30, 2020 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The ASU will increase short and long-term assets and liabilities upon adoption. The effects on the results of operations are not expected to be significant as recognition and measurement of expenses and cash flows for leases will be substantially the same under the new standard.

In August 2016, the FASB issued ASU No. 2016-14, Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities. ASU 2016-14 requires significant changes to the financial reporting model of organizations who follow FASB not-for-profit rules, including changing from three classes of net assets to two classes, net assets with donor restrictions and net assets without donor restrictions. The ASU will also require changes in the way certain information is aggregated and reported by the Foundation, including required disclosures about the liquidity and availability of resources. The Foundation is currently evaluating the impact of the standard and will present the two classes of net assets, add the liquidity footnote, expense matrix, and related disclosures. The new standard is effective for the Foundation's year ending June 30, 2019 and thereafter and must be applied on a retrospective basis.

NOTE C – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets as of June 30 are restricted for the following purposes:

	<u>2017</u>	<u>2016</u>
College programs	\$ 105,291,232	\$ 87,599,715
Capital projects	25,838,511	18,684,478
Scholarships	20,426,890	18,654,121
Instruction	6,352,386	5,534,133
Academic support	4,559,117	4,232,944
Research	4,247,313	3,852,566
Annuity and life income funds	3,481,853	4,099,560
Auxiliary	1,851,765	1,278,566
Other	3,522,091	3,311,500
Total temporarily restricted net assets	<u>\$ 175,571,158</u>	<u>\$ 147,247,583</u>

Endowment funds included in temporarily restricted net assets are \$101,463,551 and \$84,285,458 as of June 30, 2017 and 2016, respectively.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE D – PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets as of June 30 are restricted for the following purposes:

	<u>2017</u>	<u>2016</u>
College programs	\$ 154,982,908	\$ 149,915,749
Scholarships	83,164,892	75,545,932
Academic support	32,485,597	34,438,181
Instruction	32,433,738	30,542,698
Research	26,367,445	22,365,427
Auxiliary	7,650,275	7,331,973
Annuity and life income funds	2,666,655	2,682,445
Other	<u>4,604,078</u>	<u>4,401,101</u>
Total permanently restricted net assets	<u>\$ 344,355,588</u>	<u>\$ 327,223,506</u>

Endowment funds included in permanently restricted net assets are \$311,745,795 and \$295,855,901 as of June 30, 2017 and 2016, respectively.

NOTE E – PLEDGES RECEIVABLE

Contributors to the Foundation have made unconditional pledges totaling approximately \$108,634,000 and \$102,861,000 as of June 30, 2017 and 2016, respectively. For payments that extend beyond one year, these pledges receivable have been discounted at rates ranging from 0.8% to 6% to a net present value of approximately \$99,007,000 and \$93,255,000 as of June 30, 2017 and 2016, respectively.

As of June 30, the unpaid pledges are due as follows:

	<u>2017</u>	<u>2016</u>
Less than one year	\$ 29,100,702	\$ 29,509,698
One to five years	45,552,418	36,257,362
More than five years	<u>33,980,463</u>	<u>37,094,050</u>
	108,633,583	102,861,110
Less discount to present value	(9,626,201)	(9,606,242)
Less allowance for uncollectible pledges	<u>(4,308,000)</u>	<u>(3,111,800)</u>
	<u>\$ 94,699,382</u>	<u>\$ 90,143,068</u>

The Foundation records unconditional promises to give at fair value on the date the promise to give is received using the expected present value technique (“EPV”). EPV calculates present value by discounting risk-adjusted expected cash flows using a risk-free interest rate (yield to maturity on U.S. Treasuries representing the average pledge term). Amortization of the discount is recorded as additional contribution revenue.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE E – PLEDGES RECEIVABLE (continued)

Amounts due from irrevocable bequests, which are unconditional promises to give, as of June 30, 2017 and 2016 are approximately \$18,263,000 and \$18,942,000 respectively. The irrevocable bequests are included in the total amount of unconditional pledges due and fall within either the due in one to five years or due in more than five years categories. The allowance for uncollectible pledges includes approximately \$36,000 and \$34,000 associated with the irrevocable bequests, as of June 30, 2017 and 2016, respectively.

As of June 30, 2017, sixteen donors currently have outstanding conditional pledges to the Foundation. As of June 30, 2017, the conditions were not substantially met, therefore, the net present value of the pledges is not included in the carrying amount of pledges receivable. The net present value of the conditional pledges approximated \$7,553,000 as of June 30, 2017. There were twelve donors with outstanding conditional pledges as of June 30, 2016. The net present value of the conditional pledges at June 30, 2016 was approximately \$2,387,000.

NOTE F – ENDOWMENT FUNDS

Endowment assets are invested in a manner consistent with statutory fiduciary responsibilities and policies adopted by the Foundation's Board of Trustees. The primary objective is to produce long-term real growth in assets, net of administrative and investment fees, by generating a total endowment rate of return which is greater than the spending rate plus the Consumer Price Index. Strategies to achieve the primary objective at a prudent level of risk include: (a) diversification of assets among various classes; (b) diversification of investment styles within asset class; and (c) ongoing review of investment manager performance with respect to rate of return, adherence to investment style and compliance with investment guidelines.

The Foundation's endowment pool and separately invested endowment funds include donor restricted endowment funds, funds designated by the Board of Trustees for reinvestment in the endowment funds, and investment income on the endowment funds that have been appropriated for expenditure. As required by US GAAP, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the absence or existence of donor-imposed restrictions.

The Board of Trustees has interpreted the State of Ohio's UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment fund absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

In accordance with the Foundation's interpretation of UPMIFA, investment income and appreciation/depreciation earned on investments held in the permanently restricted endowment funds are credited to temporarily restricted net assets, unless otherwise stipulated by the donor. Financial assets are to be invested in a manner consistent with statutory fiduciary responsibilities and policies adopted by the Foundation's Board of Trustees.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE F – ENDOWMENT FUNDS (continued)

There are 1,115 and 1,044 endowment funds, at June 30, 2017 and 2016, respectively. As of June 30, 2017 and 2016, the fair value of these funds collectively was \$32,008,350 and \$41,482,784 less than the original gift amounts, respectively.

The Foundation has adopted a spending rate policy that limits the distribution of endowment income. The spending rate in fiscal years 2017 and 2016 was 4.5% of the moving average market value for the twelve-quarter period ended each December. Earnings above the spend rate limit are reinvested in the endowment fund for the purposes of promoting endowment fund growth. During 2017 and 2016, income earned in the investment pool was less than the amount allocated for expenditure by approximately \$11,561,000 and \$7,960,000, respectively. This shortfall was funded by cumulative capital gains in the investment pool for the years ended June 30, 2017 and 2016.

The endowment net asset composition by type of fund as of June 30, 2017, was as follows:

	2017			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Donor restricted endowment funds	\$ (32,008,350)	\$ 101,463,551	\$ 311,745,795	\$ 381,200,996
Board designated endowment funds	3,866,709	-	-	3,866,709
Total	\$ (28,141,641)	\$ 101,463,551	\$ 311,745,795	\$ 385,067,705

The change in endowment fund net assets for the year ended June 30, 2017, is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets (deficit), beginning of year	\$ (37,694,169)	\$ 84,285,458	\$ 295,855,901	\$ 342,447,190
Investment income:				
Interest and dividend income	259,285	6,796,649	4,948	7,060,882
Net realized/unrealized gain	9,548,116	8,625,691	-	18,173,807
Total investment income	9,807,401	15,422,340	4,948	25,234,689
Contributions and other transfers	-	7,733,186	14,708,653	22,441,839
Appropriation of endowment assets for expenditure	(259,285)	(6,838,931)	(48,023)	(7,146,239)
Other changes:				
Other income	-	525,977	806,404	1,332,381
Income reinvestment	4,412	335,521	417,912	757,845
Endowment net assets (deficit), end of year	\$ (28,141,641)	\$ 101,463,551	\$ 311,745,795	\$ 385,067,705

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE F – ENDOWMENT FUNDS (continued)

The endowment net asset composition by type of fund as of June 30, 2016, was as follows:

	2016			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor restricted endowment funds	\$ (41,482,784)	\$ 84,285,458	\$ 295,855,901	\$ 338,658,575
Board designated endowment funds	3,788,615	-	-	3,788,615
Total	\$ (37,694,169)	\$ 84,285,458	\$ 295,855,901	\$ 342,447,190

The change in endowment fund net assets for the year ended June 30, 2016, is as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets (deficit), beginning of year	\$ (23,890,377)	\$ 78,754,894	\$ 273,076,168	\$ 327,940,685
Investment income (loss):				
Interest and dividend income	340,158	8,827,137	6,703	9,173,998
Net realized/unrealized loss	(13,535,105)	(6,103,707)	-	(19,638,812)
Total investment income (loss)	(13,194,947)	2,723,430	6,703	(10,464,814)
Contributions and other transfers	-	12,557,242	20,179,044	32,736,286
Appropriation of endowment assets for expenditure	(614,027)	(10,178,340)	(206,879)	(10,999,246)
Other changes:				
Other income	-	113,154	2,411,745	2,524,899
Income reinvestment	5,182	315,078	389,120	709,380
Endowment net assets (deficit), end of year	\$ (37,694,169)	\$ 84,285,458	\$ 295,855,901	\$ 342,447,190

Permanently restricted endowment assets appropriated for expenditure relate primarily to contributions received where a donor originally permanently restricted the donation and subsequently changed the nature of the restriction.

NOTE G – INVESTMENTS

The Foundation combines its pooled investment securities with the investment pool of the University in order to maximize investment diversification and realize economies of scale with respect to costs of managing the investments. The Foundation continues to serve as trustee for these assets. The Foundation

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE G – INVESTMENTS (continued)

maintains individual records of each fund included in the transfer of assets to the investment pool of the University. Each fund subscribes to, or disposes of, units in the pool at the unit market value at the end of each month. Income is allocated to each fund in the pool based on units of participation. The investment pool consists of Fund A and Fund C. In July 2016, Fund C was created by segregating each share of Fund A into one share of Fund A, which owns the diversified portfolio of investment funds in separate accounts, in one share of Fund C, which owns NDCLs and strategic real estate. As NDCLs and strategic real estate produce distributions to Fund C unitholders, the proceeds will be used to periodically purchase newly-created Fund A units for the Fund C unitholders. No additional assets will be purchased within Fund C. It is expected that Fund C will cease to exist in approximately 2040 as the last distributions are made from NDCLs. As of June 30, 2017 and 2016, the University is holding approximately \$8,927,000 and \$712,000, respectively, that is to be invested in the University pooled investments. These amounts are recorded as other investments in the Statements of Financial Position.

The Foundation also manages other investments, which amounted to approximately \$51,263,000 and \$47,144,000 as of June 30, 2017 and 2016, respectively. These funds represent separately invested endowments, temporary cash investments, and split-interest trusts where the Foundation is the remainderman.

The following presents investments held by the Foundation as of June 30, 2017 and 2016:

	<u>2017</u>		<u>2017</u>		<u>2016</u>		<u>2016</u>
	Fair Value		Cost		Fair Value		Cost
Cash equivalents	\$ 10,753,057	\$	10,753,057	\$	2,566,112	\$	2,566,112
U.S. Government and agency obligations	4,209,417		4,171,133		3,411,108		3,294,853
Corporate bonds	9,172,872		9,285,420		9,886,632		9,870,855
Mutual funds	23,523,168		20,386,225		20,363,020		19,117,911
Common stocks	11,691,018		9,251,173		11,414,580		8,783,185
Real Estate	840,000		840,000		215,000		215,000
University pooled investments	<u>342,520,697</u>		<u>361,333,575</u>		<u>298,660,384</u>		<u>332,961,944</u>
Total	<u>\$ 402,710,229</u>	\$	<u>416,020,583</u>	\$	<u>346,516,836</u>	\$	<u>376,809,860</u>

The number of units in Fund A owned by the Foundation totaled 4,250,044 and 3,870,700, which represents 37% and 35% share of the Fund A pool, as of June 30, 2017 and 2016, respectively. Fund A holds primarily common stock, mutual funds, and corporate and government fixed income obligations, which are stated at fair value as determined by market prices. In addition, the Foundation owned 3,870,700 shares of Fund C as of June 30, 2017 which represents 35% of the pool which invests in loans to certain not-for-profit entities for the purpose of developing residential and commercial facilities near the University's main campus. These loans are secured by mortgages, some of which are subordinated to external financing arrangements, on parcels of land purchased by these not-for-profit entities for development. Certain investments in the University pooled investments are stated at fair value, as provided by the investment managers. Audited financial statements of the underlying investments in the University pooled investments as of June 30, 2017 and 2016, are used as a basis for fair value when available. When not available, the fair value is based upon financial information as of an interim date, adjusted for cash receipts, cash disbursements and other

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE G – INVESTMENTS (continued)

distributions made through June 30, 2017 and 2016. The Foundation believes that the carrying value of these investments is a reasonable estimate of fair value at June 30, 2017 and 2016. Certain underlying investments in the University pooled investments are not readily marketable; therefore, the estimated values of these investments are subject to certain risks. As a result, the fair value of the University pooled investments could differ from the value that may have been determined had a market for certain investments in the University investment pool existed.

The underlying investments that comprise University pooled investments as of June 30 are as follows:

	<u>2017</u>	<u>2016</u>
Fund A		
U.S. and international equity securities	45%	36%
Hedge funds and private equity capital	34	43
Fixed income securities	14	13
Fund C		
Real estate and community development	<u>7</u>	<u>8</u>
Total	<u>100%</u>	<u>100%</u>

NOTE H – FAIR VALUE MEASUREMENTS

Fair value is defined as the price that will be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements and disclosures are based on a three level hierarchy as follows:

Level 1 Inputs are quoted prices (unadjusted) in active markets for identical investments that the Foundation has the ability to access at the measurement date.

Level 2 Inputs are quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in inactive markets; other-than-quoted prices that are observable for the asset or liability; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 Inputs are unobservable and significant to the fair value measurement.

Financial instruments measured at fair value on a recurring basis using quoted prices for identical instruments in an active market (or level 1 inputs) include publicly-traded common stock, mutual funds, and certain corporate bonds. Financial instruments measured at fair value using inputs based on quoted market prices for similar instruments in active markets (or level 2 inputs) include certain common stock, U.S. Government and agency obligations and certain corporate bonds. U. S. Government and agency obligations are priced using auction data or yield curve analysis. Corporate bonds are priced using trading data if available, or when trading data is unavailable, pricing models, matrix pricing, or discounted cash flows using inputs such as weighted-average coupon rate, weighted-average maturity, and consideration of credit ratings. Financial instruments measured at fair value using inputs based on quoted prices for identical assets

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NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE H – FAIR VALUE MEASUREMENTS (continued)

in inactive markets (or level 2 inputs) include certain equity investments in privately-held corporations. The Foundation also invests in the University pooled investments which are stated at fair value using primarily the net asset value of the underlying investments. For those investments in the pool where pricing information is not available as of the measurement date, the fair value is determined based on information as of an interim date, adjusted for distributions, redemptions, market changes, and other financial and operational information obtained by the Foundation's management. These fair value instruments are measured at fair value on a recurring basis using significant unobservable inputs (or level 3 inputs).

Trusts held by others include the Foundation's beneficial interest in trusts held by other trustees. The Foundation calculates the fair value of these trusts using the investment statement from the trustee at the balance sheet date, adjusting the balance for projected future investment income at a rate based on historical returns for the each trust's mix of assets. The projected future income is then discounted back to the balance sheet date using a discount rate commensurate with the risks involved. The trusts primarily consist of common stock, mutual funds, corporate bonds and other fixed income obligations. Due to the assumptions involved in determining the fair value, these trusts are classified as level 3 in the fair value hierarchy.

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NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE H – FAIR VALUE MEASUREMENTS (continued)

The following table summarizes the valuation of financial instruments measured at fair value on a recurring basis on the Statement of Financial Position at June 30, 2017:

	Balance at June 30, 2017	Quoted prices in active markets for identical assets	Significant other observable inputs	Significant unobservable inputs
		(Level 1)	(Level 2)	(Level 3)
Assets				
Investments:				
Common stock:				
Consumer	\$ 2,690,471	\$ 2,690,471	\$ -	\$ -
Health care	1,793,315	1,793,315	-	-
Financial	2,669,127	2,669,127	-	-
Technology	1,433,657	1,433,657	-	-
Materials	55,406	55,406	-	-
Energy	777,874	777,874	-	-
Industrial	1,500,197	1,500,197	-	-
Utilities	2,536	2,536	-	-
Telecommunication	553,725	553,725	-	-
Other	214,710	132,210	-	82,500
Total common stocks	11,691,018	11,608,518	-	82,500
Mutual funds:				
Fixed	8,299,651	8,299,651	-	-
Value	3,754,818	3,754,818	-	-
Growth	1,284,502	1,284,502	-	-
Index	1,017,955	1,017,955	-	-
Blended	8,719,392	8,719,392	-	-
Other	446,850	446,850	-	-
Total mutual funds	23,523,168	23,523,168	-	-
Corporate bonds	9,172,872	-	9,172,872	-
U.S. Government and agency obligations	4,209,417	-	4,209,417	-
University pooled investments	342,520,697	-	-	342,520,697
Real estate	840,000	-	-	840,000
Total investments at fair value	\$ 391,957,172	\$ 35,131,686	\$ 13,382,289	\$ 343,443,197
Trusts held by others	\$ 10,157,614	\$ -	\$ -	\$ 10,157,614
Liabilities				
Trusts held for the benefit of others	\$ 1,455,514	\$ -	\$ -	\$ 1,455,514

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE H – FAIR VALUE MEASUREMENTS (continued)

The following table summarizes the valuation of financial instruments measured at fair value on a recurring basis on the Statement of Financial Position at June 30, 2016:

	Balance at June 30, 2016	Quoted prices in active markets for identical assets	Significant other observable inputs	Significant unobservable inputs
		(Level 1)	(Level 2)	(Level 3)
Assets				
Investments:				
Common stock:				
Consumer	\$ 1,894,241	\$ 1,894,241	\$ -	\$ -
Health care	2,027,859	2,027,859	-	-
Financial	2,003,251	2,003,251	-	-
Technology	1,961,599	1,961,599	-	-
Materials	98,677	98,677	-	-
Energy	946,193	946,193	-	-
Industrial	1,560,597	1,560,597	-	-
Utilities	5,201	5,201	-	-
Telecommunication	528,879	528,879	-	-
Other	388,083	388,083	-	-
Total common stocks	<u>11,414,580</u>	<u>11,414,580</u>	<u>-</u>	<u>-</u>
Mutual funds:				
Fixed	7,621,726	7,621,726	-	-
Value	3,588,539	3,588,539	-	-
Growth	1,460,038	1,460,038	-	-
Index	983,749	983,749	-	-
Blended	6,384,061	6,384,061	-	-
Other	324,907	324,907	-	-
Total mutual funds	<u>20,363,020</u>	<u>20,363,020</u>	<u>-</u>	<u>-</u>
Corporate bonds	9,886,632	-	9,886,632	-
U.S. Government and agency obligations	3,411,108	-	3,411,108	-
University pooled investments	298,660,384	-	-	298,660,384
Real estate	215,000	-	-	215,000
Total investments at fair value	<u>\$ 343,950,724</u>	<u>\$ 31,777,600</u>	<u>\$ 13,297,740</u>	<u>\$ 298,875,384</u>
Trusts held by others	<u>\$ 9,633,268</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 9,633,268</u>
Liabilities				
Trusts held for the benefit of others	<u>\$ 1,368,252</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,368,252</u>

The Foundation's policy is to recognize transfers between levels of the fair value hierarchy as of the end of the reporting period. In 2016, the real estate investments were valued with observable inputs in the market. In 2017, the real estate investments were transferred to Level 3 from Level 2 due to the lack of observable market data for these investments. As a result of this change, the fair value tables in 2017 and 2016 were updated.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE H – FAIR VALUE MEASUREMENTS (continued)

The Foundation's investments in cash equivalents are carried at amortized cost. These investments do not qualify as securities as defined in FASB ASC 320, *Investments – Debt and Equity Securities*, thus the fair value disclosures required by US GAAP are not provided. Cash equivalents at June 30, 2017 and 2016, are \$10,753,057 and \$2,566,112 and are included in other investments on the accompanying June 30, 2017 Statement of Financial Position.

Realized and unrealized gains (losses) related to these fair value instruments total \$31,942,305 and \$(11,722,183) as of June 30, 2017 and 2016, respectively, and are included in net unrealized and realized gains (losses) in the accompanying Statements of Activities, except for those fair value instruments where the Foundation is not the beneficiary.

A reconciliation of the balance of level 3 financial instruments for the year ended June 30, 2017, is as follows:

	University pooled investments	Trusts held by others	Trusts held for the benefit of others	Real Estate
Beginning balance	\$ 298,660,384	\$ 9,633,268	\$ 1,368,252	\$ 215,000
Purchases/contributions	26,081,395	-	1,015	1,144,000
Interest and dividend income	2,454,388	-	64,678	-
Reinvested income	906,769	-	-	-
Liquidations/sales	(14,144,710)	-	(65,667)	(455,000)
Net realized and unrealized gains/(losses)	28,562,471	524,346	87,236	(64,000)
Ending balance	<u>\$ 342,520,697</u>	<u>\$ 10,157,614</u>	<u>\$ 1,455,514</u>	<u>\$ 840,000</u>

A reconciliation of the balance of level 3 financial instruments for the year ended June 30, 2016, is as follows:

	University pooled investments	Trusts held by others	Trusts held for the benefit of others	Real Estate
Beginning balance	\$ 219,617,756	\$ 9,457,458	\$ 916,818	\$ -
Purchases/contributions	27,685,302	-	500,999	215,000
Interest and dividend income	4,575,110	-	45,537	-
Reinvested income	863,932	-	-	-
Liquidations	(14,332,924)	-	(45,537)	-
Net realized and unrealized gains (losses)	(11,748,792)	175,810	(49,565)	-
Ending balance	<u>\$ 298,660,384</u>	<u>\$ 9,663,268</u>	<u>\$ 1,368,252</u>	<u>\$ 215,000</u>

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE H – FAIR VALUE MEASUREMENTS (continued)

Gains and losses for these Level 3 fair value instruments are included in net unrealized and realized gains (losses) in the accompanying Statements of Activities. The total amount of gains (losses) above included in changes in net assets that is attributable to assets held at June 30, 2017 and 2016 is \$29,022,817 and \$(11,572,982), respectively.

Quantitative information about significant unobservable inputs used in level 3 fair value measurements

The Foundation’s share of University pooled investments is categorized as level 3 in the fair value hierarchy due to several significant unobservable inputs related primarily to loans made to neighborhood development corporations (“NDC”). The remaining investments are categorized as level 1 or level 2 in the fair value hierarchy if active trading data are available for similar or identical financial instruments at or near the balance sheet date, or in the case of hedge funds, the net asset value is provided via annual audited financial statements at or near the balance sheet date, and redemption provisions are not prohibitive. The pool also contains private equity funds, which are categorized as level 3 in the fair value hierarchy due to prohibitive redemption provisions, and are recorded at net asset value based on the most recently available audited financial statements and fund manager information as of March 31, 2017 or 2016, as applicable. NDC loans are stated at the principal amount plus accrued interest less an allowance for loan losses. As of June 30, 2017 and 2016, approximately 49% of the principal and accrued interest was offset by an allowance for loan losses. The valuation technique, significant unobservable inputs and the ranges of input values for the loan loss reserve are as follows:

<u>Valuation technique</u>	<u>Unobservable inputs</u>	<u>Range</u>
Expected future cash flows	Future occupancy rates	85% - 100%
	Future operating expenses (as a percentage of total revenue)	36% - 57%

University management obtains current cash flow information from each NDC. Based upon either the expected completion date of construction, or current occupancy rates if the property is actively rented, management then projects the approximate date when principal payments will begin and conclude. If, based upon this analysis, it appears unlikely that the loan principal and accrued interest can be repaid, an increase to the loan loss reserve is recorded.

On an annual basis, the Foundation estimates the fair value of its beneficial interest in trusts held by other trustees. Management obtains trust statements as of the balance sheet date, and calculates the fair value of their beneficial interest based on expected investment returns, and the life expectancies of any other income beneficiaries, discounted at a 6% interest rate. The following table represents the Foundation’s valuation technique, significant unobservable inputs, and ranges of values of those inputs for trusts held by others which are \$10,157,614 and \$9,633,268 at June 30, 2017 and 2016, respectively.

<u>Valuation technique</u>	<u>Unobservable inputs</u>	<u>Range</u>
Discounted cash flows	Projected investment income	0% – 8%
	Life expectancy of beneficiaries	2 - 22 years
	Discount rate	6%

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE H – FAIR VALUE MEASUREMENTS (continued)

Trusts held for the benefit of others are included as a liability on the accompanying June 30, 2017 and 2016 Statements of Financial Position. The trusts are stated at fair value, which is an equal and offsetting amount to the trusts' underlying investments which are included in University pooled investments at fair value on the accompanying June 30, 2017 and 2016 Statements of Financial Position. As University pooled investments are also categorized as a level 3 financial instrument, the significant unobservable inputs for this investment are disclosed previously in this footnote.

NOTE I – FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate fair value of each class of financial instruments for which it is practicable to estimate fair value:

The carrying amounts of cash and cash equivalents, due from University of Cincinnati, due from UC Health Foundation, receivables (other than pledges), prepaid expenses, cash surrender value of life insurance policies, other assets, accounts payable, agency payable, accrued liabilities, accrued compensated absences, and refundable deposits approximate fair value because of the short maturity of these instruments. The fair value of pledges receivable and annuities payable have been estimated by management to approximate carrying value using a current discount rate commensurate with the risk involved.

The fair values of investments and trusts held for the benefit of others are generally estimated based on quoted market prices for those investments. Certain investments held in the University's investment pool do not have readily determinable market values. These investments are carried at estimated fair value provided by the investment managers. The majority of these investments are valued based upon independently audited financial information or other information provided as of an interim date, which is adjusted for cash receipts, cash disbursements, and other distributions made through June 30, 2017 and 2016, respectively. The fair value of trusts held by others is based upon the discounted cash flows at a rate commensurate with the risk involved. The Foundation believes that the carrying value of investments in the University pooled investments is a reasonable estimate of fair value at June 30, 2017 and 2016. See also Notes G, H, and M.

NOTE J – EQUIPMENT AND SOFTWARE

Equipment and software as of June 30 consist of the following:

	<u>2017</u>	<u>2016</u>
Office equipment	\$ 798,879	\$ 671,383
Software	4,899,686	4,883,628
Automobile	53,504	22,320
Computer equipment	320,491	301,156
	<u>6,072,560</u>	<u>5,878,487</u>
Accumulated depreciation and amortization	<u>(3,037,463)</u>	<u>(1,982,328)</u>
	<u>\$ 3,035,097</u>	<u>\$ 3,896,159</u>

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE J – EQUIPMENT AND SOFTWARE (continued)

Amortization expense related to computer software was approximately \$888,000 and \$692,000 for the years ended June 30, 2017 and 2016, respectively, and is included in operating expenses in the accompanying Statement of Activities.

NOTE K – LEASES

Rental expense for operating leases was \$239,470 for 2017 and 2016. The Foundation leases certain office space directly from the University. The lease expires on September 30, 2024, and is renewable for two additional terms of 20 years each.

Future minimum lease payments under noncancelable operating leases (with initial or remaining terms in excess of one year) as of June 30 are:

2018	\$	239,470
2019		239,470
2020		239,470
2021		239,470
2022		239,470
Thereafter		<u>538,810</u>
Total minimum lease payments	\$	<u>1,736,160</u>

NOTE L – LIFE INSURANCE POLICIES

The Foundation is the beneficiary of certain life insurance policies that are recorded at their cash surrender value in the Statements of Financial Position. The cash surrender value represents the amount the Foundation, as beneficiary, would realize if such policies were surrendered as of June 30, 2017 and 2016. The face value of these policies, which would be paid only upon death of the insured and maturity of the contracts, is \$4,412,074 and \$4,515,676 as of June 30, 2017 and 2016, respectively.

NOTE M – BENEFICIAL INTEREST IN TRUSTS – OTHER TRUSTEES

The Foundation has been notified of thirteen trusts held by other trustees where the remainder interest will irrevocably benefit the University. In addition, the Foundation has been notified of two charitable lead unitrusts held by other trustees where annual payments are received by the Foundation. The Foundation values these assets by projecting the value of the trust assets to future periods and then discounting the anticipated cash flows at a rate reflective of the credit risk involved.

Beneficial interest in trusts held by other trustees amounted to approximately \$10,158,000 and \$9,633,000 as of June 30, 2017 and 2016, respectively.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE N – UNIVERSITY FEE

In accordance with an agreement with the University, operating support of \$10,768,326 and \$7,331,676 was provided by the University during the years ended June 30, 2017 and 2016, respectively. The Foundation also receives interest income earned on unexpended gift fund balances held at the University and reimbursement from certain colleges of the University for salaries and fringe benefits paid to college development employees. For the years ended June 30, 2017 and 2016, interest income and salary and benefits were \$1,228,191 and \$1,030,951, respectively. During the year 2016, the University provided operating support and contributions for costs incurred related to software development in the amount of \$267,090.

The University provided to the Foundation at no charge, the use of the building in which the Alumni Relations Department conducts business for the year ended June 30, 2017. The value of donated occupancy costs is estimated to be \$271,743 each year, and is included in university fee with an equal and offsetting amount recorded in operating expenses on the accompanying Statements of Activities.

NOTE O – ASSESSMENT FEE

The Foundation is also funded by a fee assessed on certain endowment funds held by the University and the Foundation. Funds that are eligible for the fee assessment include quasi-endowment funds, funds that are broadly restricted by college or department, funds whereby the donor has not prohibited assessment of the fee, and unrestricted funds that do not have an internal designation. The gross assessment rate was 1.25% and 1.5%, respectively, in 2017 and 2016. Revenue to the Foundation from the fee was approximately \$8,962,000 and \$9,141,000 in 2017 and 2016, respectively, and is used to fund Foundation operations. Approximately \$3,290,000 and \$3,135,000 of this fee was recorded from funds held by the Foundation in 2017 and 2016, respectively.

The Foundation charges an endowment administrative fee to recover gift stewardship costs incurred by the Foundation for those endowments which are not charged the general endowment assessment fee. The endowment administrative rate was 5% in 2017 and 2016, of the spending policy distribution made to the endowment spending account. Revenue to the Foundation from the fee was approximately \$391,000 and \$488,000 in 2017 and 2016, respectively. Approximately \$104,000 and \$152,000 of this fee was recorded from funds held by the Foundation in 2017 and 2016, respectively.

The Foundation charges a fee to be assessed upon all spendable, cash gifts made to the University, the Foundation or the UC Health Foundation. The gift administrative rate was 5% for gifts less than five million and 2% for gift commitments of five million and greater in 2017 and 2016, upon the receipt of cash to gift, plant and loan funds. Revenue to the Foundation from the fee was approximately \$1,853,000 and \$1,697,000 in 2017 and 2016, respectively. Approximately \$1,679,000 and \$1,497,000 of this fee was recorded from funds received by the Foundation in 2017 and 2016, respectively.

NOTE P – ANNUITY AND LIFE INCOME FUNDS

The Foundation actively markets annuities and life income agreements as part of the development program. These agreements include gift annuities and split-interest trusts where the income beneficiaries receive an

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE P – ANNUITY AND LIFE INCOME FUNDS (continued)

income stream for their lifetimes, or a fixed number of years, and the Foundation is the remainderman. Present value of annuities payable is recorded using the Foundation’s estimated borrowing rate. The present value is calculated by discounting the life income payments using an average interest rate swap plus 200 BP for the time period which most closely matches the average life expectancy of our income beneficiaries. Changes in future payments due to the life expectancy of beneficiaries and amortization of the discount are reflected in change in present value of annuities payable on the accompanying Statement of Activities. The assets and liabilities of these funds as of June 30 are:

	2017	2016
Annuities		
Investments, at fair value	\$ 3,376,525	\$ 2,378,343
Less present value of annuities payable	<u>(1,606,882)</u>	<u>(1,180,759)</u>
	<u>\$ 1,769,643</u>	<u>\$ 1,197,584</u>
	2017	2016
Trusts		
Investments, at fair value	\$ 10,891,065	\$ 10,620,055
Less present value of annuities payable	<u>(5,012,357)</u>	<u>(5,281,250)</u>
	<u>\$ 5,878,708</u>	<u>\$ 5,338,805</u>

For the year ended June 30, 2017, the Foundation received contributions of approximately \$1,119,000 and \$22,000 for annuities and trusts, respectively. For the year ended June 30, 2016, the Foundation received contributions of approximately \$151,000 and \$39,000 for annuities and trusts, respectively.

The Foundation monitors applicable state laws related to legally-mandated reserves for charitable gift annuities, and maintains reserves for various states, as appropriate.

NOTE Q – RETIREMENT PLANS

The Foundation participates in a qualified and contributory retirement plan (TIAA) covering eligible employees. Under this arrangement, the Foundation and plan participants make annual contributions to purchase individual annuities equivalent to retirement benefits earned. The Foundation’s share of the cost of these benefits was approximately \$877,000 and \$756,000 for the years ended June 30, 2017 and 2016, respectively.

The Foundation also maintains a Section 457(f) plan for highly compensated employees. Accounts for participating employees are currently funded solely by salary reduction contributions. The plan is structured to permit Foundation contributions on behalf of the participants, as defined. There were no amounts contributed by the Foundation for the years ended June 30, 2017 and 2016.

THE UNIVERSITY OF CINCINNATI FOUNDATION

NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

NOTE R – RELATED PARTY TRANSACTIONS

During the year ended June 30, 2016, the Foundation entered into agreements with the UC Alumni Association (UCAA) and the UC Health Foundation (UCHF) to provide executive, administrative and fund raising services for a monthly fee. The fee is reimbursement for the cost incurred by the Foundation for providing support to UCAA and UCHF. During 2017 and 2016, the Foundation incurred \$2,105,297 and \$2,666,379, respectively in expenses and recognized corresponding revenue under the terms of the agreements. These expenses and revenues are reported in operating expenses and fees in the accompanying Statement of Activities.

Certain board members of the Foundation made contributions of \$3,161,380 and \$15,075,146 during fiscal year 2017 and 2016, respectively. In addition, certain board members are employees of organizations which provide services to the Foundation. Total fees paid to these organizations were \$186,411 and \$265,383 for the years ended June 30, 2017 and 2016, respectively.

See also the description of various related party transactions with the University in Notes G, H, K, M, N, and O.

NOTE S – ALUMNI ASSOCIATION MERGER

Effective July 1, 2016, the UC Alumni Association was merged with and into the Foundation, with the Foundation being the surviving entity per the Agreement and Plan of Merger. The merger occurred in order to create efficiencies and develop a sustainable funding model for the Alumni Association. The merger resulted in an increase to the Foundation's asset base of approximately \$2.2 million, which is primarily comprised of investments of similar composition to the Foundation.

NOTE T – SUBSEQUENT EVENTS

The Foundation evaluated its June 30, 2017 financial statements for subsequent events through September 19, 2017, the date the financial statements were available to be issued.

SUPPLEMENTAL SCHEDULES

THE UNIVERSITY OF CINCINNATI FOUNDATION

SUPPLEMENTAL SCHEDULE OF DETAIL OF OPERATING EXPENSES

Years ended June 30, 2017 and 2016

	<u>Foundation Operations</u>	<u>College/ University Expenses</u>	<u>Total 2017</u>	<u>Total 2016</u>
Salaries and wages	\$ 13,029,784	\$ -	\$ 13,029,784	\$ 11,736,909
Fringe benefits	4,047,828	-	4,047,828	3,582,982
Professional services	2,124,419	17,238	2,141,657	2,236,567
Depreciation and amortization	1,434,349	-	1,434,349	869,070
Promotional materials and events	1,225,576	4,700	1,230,276	716,228
Computer and word processing	619,872	-	619,872	871,539
Building lease	239,472	-	239,472	239,470
Donated office space	271,743	-	271,743	-
Telephone and postage	423,667	-	423,667	366,421
Business meetings	323,348	-	323,348	404,298
Travel	304,485	-	304,485	288,039
Development and recruiting	293,461	-	293,461	220,940
Direct marketing	221,952	-	221,952	241,891
Cultivation	167,032	-	167,032	199,367
Miscellaneous	117,268	(7,227)	110,041	63,709
Cleaning	115,376	-	115,376	103,684
Membership dues	89,457	-	89,457	67,919
Utilities, repairs and maintenance	77,773	-	77,773	60,622
Parking	53,463	-	53,463	48,523
Supplies	50,267	-	50,267	55,624
Subsidies to Alumni constituents	45,250	-	45,250	-
General support - Alumni Association	-	-	-	38,704
Insurance	44,466	-	44,466	36,176
Resource materials	41,861	-	41,861	44,203
Copying charges	33,732	-	33,732	29,329
Gift annuity reserve	23,152	-	23,152	18,085
	\$ <u>25,419,053</u>	\$ <u>14,711</u>	\$ <u>25,433,764</u>	\$ <u>22,540,299</u>

THE UNIVERSITY OF CINCINNATI FOUNDATION

SUPPLEMENTAL SCHEDULE OF ACTIVITIES - UNRESTRICTED NET ASSETS (DEFICIT)

Year ended June 30, 2017

	Gifts and Transfers	Foundation Operations	Total
Revenues and other additions:			
Contributions	\$ 364,489	\$ 133,269	\$ 497,758
Donated services	-	198,766	198,766
University fee	-	11,971,542	11,971,542
UC Health Foundation fee	-	2,105,297	2,105,297
Assessment fee	-	11,206,249	11,206,249
Change in value of split interest agreements	(4,617)	-	(4,617)
Other income	46	319,742	319,788
Investment income:			
Dividend and interest income	258,017	80,703	338,720
Net unrealized and realized losses	9,388,343	30,395	9,418,738
Net assets released from restrictions - satisfaction of donor restrictions	53,892,824	-	53,892,824
Total revenues and other additions	63,899,102	26,045,963	89,945,065
Expenses and other deductions:			
Distributions to the University of Cincinnati	50,471,635	-	50,471,635
Operating expenses	14,711	25,419,053	25,433,764
Assessment fee	5,073,849	-	5,073,849
Total expenses and other deductions	55,560,195	25,419,053	80,979,248
Change in net assets before acquisition income	8,338,907	626,910	8,965,817
Excess of fair value of net assets over consideration in acquisition of the acquired entity	13,048	1,972,174	1,985,222
Change in net assets	8,351,955	2,599,084	10,951,039
Net assets (deficit), beginning of year	(34,529,522)	4,506,382	(30,023,140)
Net assets (deficit), end of year	\$ (26,177,567)	\$ 7,105,466	\$ (19,072,101)

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Independent Auditor's Report

To Management and the Board of Trustees
The University of Cincinnati Foundation

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of The University of Cincinnati Foundation (the "Foundation"), which comprise the statement of financial position as of June 30, 2017 and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements and have issued our report thereon dated September 19, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Foundation's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control. Accordingly, we do not express an opinion on the effectiveness of the Foundation's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Foundation's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Foundation's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

To Management and the Board of Trustees
The University of Cincinnati Foundation

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Foundation's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Foundation's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Plante & Moran, PLLC

September 19, 2017



Dave Yost • Auditor of State

UNIVERSITY OF CINCINNATI FOUNDATION

HAMILTON COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

CERTIFIED
NOVEMBER 9, 2017