# The Kresge Foundation

(A Michigan Trustee Corporation)

Financial Statements as of and for the
Years Ended December 31, 2018 and 2017, and
Independent Auditors' Report

**THE KRESGE FOUNDATION**
**(A Michigan Trustee Corporation)**

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# INDEPENDENT AUDITORS' REPORT

To the Board of Trustees of
The Kresge Foundation Troy, Michigan

We have audited the accompanying financial statements of The Kresge Foundation (the "Foundation"), which comprise the statements of financial position as of December 31, 2018 and 2017, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

## Management's Responsibility for the Financial Statements

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

## Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Foundation'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 Foundation'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 Foundation as of December 31, 2018 and 2017, and the results of its activities and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## Emphasis of Matter

As discussed in Note 2 to the financial statements, in 2018, the Foundation adopted new accounting guidance ASU No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. Our opinion is not modified with respect to this matter.

Deloitte & Touche LLP

June 6, 2019

## THE KRESGE FOUNDATION
**(A Michigan Trustee Corporation)**

**STATEMENTS OF FINANCIAL POSITION**
**AS OF DECEMBER 31, 2018 AND 2017**

| | 2018 | 2017 |
|---|---|---|
| **ASSETS** | | |
| CASH | $ 1,768,211 | $ 1,764,857 |
| INVESTMENTS—At fair market value | 3,621,635,389 | 3,860,906,367 |
| PROGRAM-RELATED INVESTMENTS—Net of allowance of $4,322,495 and $4,527,049, respectively | 73,915,091 | 62,370,967 |
| COLLATERAL UNDER SECURITIES LENDING AGREEMENT | 3,073,895 | 2,905,846 |
| ACCRUED INTEREST AND DIVIDENDS | 1,145,966 | 1,502,881 |
| PROPERTY AND EQUIPMENT—Net of accumulated depreciation of $11,860,423 and $10,752,186, respectively | 17,866,451 | 19,101,169 |
| OTHER | 8,281,254 | 6,084,838 |
| TOTAL | $ 3,727,686,257 | $ 3,954,636,925 |
| **LIABILITIES AND NET ASSETS WITHOUT DONOR RESTRICTIONS** | | |
| LIABILITIES: | | |
| Grants payable—net of discount of $1,465,277 and $997,732, respectively | $ 56,755,202 | $ 89,753,579 |
| Accounts payable and other liabilities | 5,508,504 | 6,237,260 |
| Other postemployment benefit liability | 7,606,091 | 8,777,196 |
| Borrowings under revolving line of credit | 46,465,824 | 25,776,663 |
| Payable under securities lending agreement | 3,073,895 | 2,905,846 |
| Deferred federal excise taxes | 12,882,553 | 19,016,682 |
| Total liabilities | 132,292,069 | 152,467,226 |
| NET ASSETS | 3,595,394,188 | 3,802,169,699 |
| TOTAL | $ 3,727,686,257 | $ 3,954,636,925 |

See notes to financial statements.

**THE KRESGE FOUNDATION**
**(A Michigan Trustee Corporation)**

**STATEMENTS OF ACTIVITIES**
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**

| | 2018 | 2017 |
|---|---|---|
| INCOME AND LOSS: | | |
| Net investment (loss) income | $ (62,992,883) | $ 476,349,227 |
| Program-related investment income | 1,351,228 | 1,080,035 |
| Total (loss) income | (61,641,655) | 477,429,262 |
| EXPENSES: | | |
| Grants—net of change in discount of $467,545 and $608,042, respectively | 114,829,604 | 149,311,048 |
| Administrative expenses | 31,083,794 | 30,022,832 |
| Total expenses | 145,913,398 | 179,333,880 |
| OTHER POSTEMPLOYMENT ADJUSTMENTS | 779,542 | (1,032,459) |
| CHANGE IN NET ASSETS | (206,775,511) | 297,062,923 |
| NET ASSETS: | | |
| Beginning of year | 3,802,169,699 | 3,505,106,776 |
| End of year | $ 3,595,394,188 | $ 3,802,169,699 |

See notes to financial statements.

## THE KRESGE FOUNDATION
**(A Michigan Trustee Corporation)**

**STATEMENTS OF CASH FLOWS**
**FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017**

| | 2018 | 2017 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Change in net assets | $ (206,775,511) | $ 297,062,923 |
| Adjustments to reconcile change in net assets to net cash used in operating activities: | | |
| Depreciation | 1,649,245 | 1,705,338 |
| Loss on disposals of property and equipment | 8,718 | 6,375 |
| (Decrease) Increase in program-related investments provision | (65,048) | 1,655,834 |
| Change in value of grants payable | (467,545) | (608,042) |
| Net realized and unrealized losses (gains) on investments | 69,866,094 | (479,866,469) |
| Net unrealized loss on program related investments | - | 40,000 |
| Changes in assets and liabilities: | | |
| Accrued interest and dividends | 356,915 | 830,651 |
| Other assets | (2,196,416) | (1,981,847) |
| Approved grants payable | (32,530,832) | 2,288,332 |
| Accounts payable and other liabilities | (728,756) | 677,761 |
| Other postemployment benefit liability | (1,171,105) | 651,612 |
| Deferred federal excise taxes | (6,134,129) | 4,362,638 |
| Net cash used in operating activities | (178,188,370) | (173,174,894) |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Proceeds from sales of investments | 1,575,581,517 | 1,270,637,933 |
| Purchases of investments | (1,406,176,633) | (1,074,102,635) |
| Returns of principal for program-related investments | 6,316,497 | 4,915,604 |
| Disbursements for program-related investments | (17,795,573) | (24,989,215) |
| Purchases of property and equipment | (423,245) | (329,091) |
| Net cash provided by investing activities | 157,502,563 | 176,132,596 |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from revolving line of credit | 61,465,824 | 25,776,663 |
| Repayments of revolving line of credit | (40,776,663) | (27,709,850) |
| Net cash provided by (used in) financing activities | 20,689,161 | (1,933,187) |
| NET INCREASE IN CASH | 3,354 | 1,024,515 |
| CASH: | | |
| Beginning of year | 1,764,857 | 740,342 |
| End of year | $ 1,768,211 | $ 1,764,857 |

See notes to financial statements.

## 1. ORGANIZATION AND NATURE OF OPERATIONS

The Kresge Foundation (the "Foundation") is a tax-exempt private foundation that works to expand opportunities in America's cities through grantmaking and investing in arts and culture, education, environment, health, human services, and community development. The Foundation was established in June 1924 as a Michigan trustee corporation. Its office is in Troy, Michigan.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Basis of Financial Presentation**—The accompanying financial statements are prepared on the accrual basis and in conformity with accounting principles generally accepted in the United States of America (GAAP).

**Program-Related Investments (PRIs)**—In accordance with Section 4944 of the Internal Revenue Code (the "Code"), the Foundation is permitted to make investments that further some aspect of its charitable mission. In 2008, the Foundation began making PRIs. These investments are anticipated to have lower-than-market returns on a risk-adjusted basis. Like grants, these investments count toward the Foundation's payout requirement in the year of distribution. Return of PRI principal affects the annual payout requirement in a similar manner as a grant refund.

**Property and Equipment**—Property and equipment represents primarily land and buildings. Property and equipment is depreciated on the straight-line basis over the estimated useful lives of the assets, which range from 3 to 45 years. The associated depreciation was $1,649,245 and $1,705,338 as of December 31, 2018 and 2017, respectively. The Foundation annually reviews the property and equipment records for impairment of the carrying value and records any adjustments necessary to reflect impacts in the carrying value.

Property and equipment as of December 31, 2018 and 2017, consists of the following:

| | 2018 | 2017 |
|---|---|---|
| Building and improvements | $ 24,298,520 | $ 24,154,705 |
| Furniture and fixtures | 2,004,799 | 1,995,019 |
| Computer and office equipment | 2,624,353 | 3,048,491 |
| | 28,927,672 | 29,198,215 |
| Less accumulated depreciation and amortization | (11,860,423) | (10,752,186) |
| Subtotal depreciable assets—net | 17,067,249 | 18,446,029 |
| Land | 500,000 | 500,000 |
| Art | 149,786 | 140,466 |
| Construction in progress | 149,416 | 14,674 |
| Subtotal nondepreciable assets | 799,202 | 655,140 |
| Total property and equipment—net | $ 17,866,451 | $ 19,101,169 |

**Grant Expenditures**—Grant expenditures are recognized in the period the grant is approved, provided the grant is not subject to significant future conditions. Conditional grants are recognized as grant expense and as a grant payable in the period in which the grantee substantially meets the terms of the conditions. The Foundation had approximately $77,800,000 and $85,100,000 in conditional grants as of December 31, 2018 and 2017, respectively. At December 31, 2018, conditional grants included $75,000,000 to the Foundation for Detroit's Future (FDF), payable in equal installments over a 15 year-period, subject to any terms and conditions of the Foundation FDF Agreement.

**Line of Credit**—The Foundation has an unsecured line of credit totaling $100,000,000 as of December 31, 2018 and 2017. The line of credit has been recorded at carrying value, which approximates fair value. The credit line has a three-month LIBOR effective rate of 3.26% and 2.14% and contains a commitment fee on the unused available balance of .17% as of December 31, 2018 and 2017. As of December 31, 2018 and 2017, the outstanding borrowings were $46,465,824 and $25,776,663, respectively. The aggregate outstanding principal, interest, and related fees are due in full on the commitment termination date August 31, 2019. Interest and related fees payable at year-end are included in accounts payable and other liabilities.

**Net Assets**—The presentation of net assets represents net assets without donor restrictions.

**Tax Status**—The Foundation is an organization exempt from federal income taxation under Section 501(c)(3) and is a private foundation as described in Section 509(a) of the Code. The Foundation is subject to federal excise taxes. It is also subject to federal and state income tax on its unrelated business taxable income. Management believes it is no longer subject to federal tax examinations for years prior to December 31, 2015. The Foundation evaluates uncertain tax positions for more-likely than-not sustainability. The

Foundation has concluded that as of December 31, 2018 and 2017, there are no uncertain tax positions taken or expected to be taken that would require recognition of a liability or disclosure in the financial statements.

On December 22, 2017, the U.S. Government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the "Tax Act"). The Tax Act makes broad and complex changes to the U.S. tax code, including, but not limited to, (1) reducing the U.S. federal corporate tax rate from 35% to 21%; (2) eliminating the corporate alternative minimum tax (AMT) and changing how existing AMT credits can be realized; and (3) changing rules related to uses and limitation of net operating loss carryforwards created in tax years beginning after December 31, 2017. The impact of the Tax Act on the Foundation is not considered significant.

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

**Investment Risks**—Investment securities are exposed to various risks, such as interest rate, market, and credit. 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 values in the near term could materially affect the amounts reported in the accompanying financial statements.

**Adoption of Accounting Pronouncements**—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*. This guidance simplifies and improves how not-for-profit entities classify net assets as well as the information presented in the financial statements and notes about liquidity, financial performance, and cash flows. The guidance has been adopted as of January 1, 2018 with retrospective application for all comparative periods with certain disclosure exceptions. The implementation of this guidance has resulted in additional disclosures related to the Foundation's functional expenses and liquidity. In addition, certain direct investment expenses were reclassified out of administrative expenses into net investment (loss) income in the statements of activities.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. This guidance has been adopted as of January 1, 2018. The adoption of this guidance had no impact on how the Foundation presents and classifies certain cash receipts and cash payments in the statements of cash flows.

In June 2018, the FASB issued ASU No. 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The new guidance clarifies the definitions of reciprocal and non-reciprocal transactions and modifies the criteria used to evaluate conditional vs. unconditional contributions. In addition, the new guidance defines that a conditional contribution exists when the agreement contains both a right of return of the contributed asset and a barrier that must be overcome. The guidance is effective for the Foundation for years beginning after December 15, 2019. The Foundation early adopted this guidance on January 1, 2019. The adoption of this guidance had no impact on how the Foundation accounts for its grantmaking activities.

In August 2018, the FASB issued ASU No. 2018-13, *Fair Value Measurements (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurements*. The guidance is effective for the Foundation for years beginning after December 15, 2019. The Foundation early adopted this guidance on December 31, 2018. The adoption of this guidance has eliminated the need to present information regarding transfers between level 1 and level 2 investments in the fair value hierarchy. In addition, disclosures for transfers into and out of level 3 investments and purchases of level 3 investments have been presented in lieu of a level 3 rollforward. Lastly, the changes in unrealized gains and losses for level 3 investments has been eliminated from the disclosure for the year ended December 31, 2018 but remains included for the year ended December 31, 2017.

## 3. INVESTMENTS AND FAIR VALUE

**Temporary Investments**—The Foundation considers temporary investments to be unsettled trade purchases and sales and cash and cash equivalents held as part of the long-term investment strategy of the Foundation. Cash equivalents are considered to be investments with an original maturity of three months or less. The Foundation records investments as of the trade date. Unsettled trade purchases and sales are reported in the investment category on the statements of financial position. The Foundation had unsettled trade purchases of approximately $0 and $1,107,000 as of December 31, 2018 and 2017, respectively. The Foundation had unsettled trade sales of approximately $89,044,000 and $21,215,000 as of December 31, 2018 and 2017, respectively.

**Fixed-Income, U.S. Equity, and Foreign Equity Securities**—Fixed-income, U.S. equity, and foreign equity securities include investments in securities as well as commingled funds. The securities have readily determinable fair market values based on quoted prices in active markets. The commingled funds calculate a net asset value per share in accordance with near term guidance.

**Hedge Funds, Natural Resources, Private Equity, and Real Estate**—Hedge funds' fair values are based on information provided by the administrators of each underlying fund. Natural resources, private equity, and real estate limited partnerships are accounted for on the equity method or pricing models that use both observable and unobservable inputs. Gains and losses on investments include equity earnings from limited partnerships.

**Securities Lending**—The Foundation participates in a securities lending program with its custodian bank. Under the terms of its securities lending agreement, the Foundation requires collateral of a value at least equal to 102% of the fair value of loaned investments. Securities lending collateral is not subject to a master netting arrangement. Loaned investments consist of equity securities and U.S. treasury bills. Securities loaned are fully collateralized. All cash collateral received is invested in approved money market and short-term funds. The Foundation maintains effective control of the loaned investments during the term of the agreement. As of December 31, 2018 and 2017, the Foundation had loaned securities with a total market value of approximately $5,093,000 and $3,940,000, respectively, and received related cash collateral of approximately $3,074,000 and $2,906,000, respectively. The carrying value of securities lending collateral approximates fair value as recorded collateral is composed of cash and cash equivalents that are received. Income from the program was approximately $21,000 and $17,000 for the years ended December 31, 2018 and 2017, respectively.

The changes in security lending collateral of approximately $168,000 and $178,000 as of December 31, 2018 and 2017, respectively, are considered noncash transactions.

**Realized and Unrealized Gains/Losses**—Net realized gains and change in net unrealized market gains are determined by comparing cost to proceeds and fair market value, respectively. Cost is determined on a first-in, first-out basis. The gains or losses on the Foundation's investment portfolio for the years ended December 31, 2018 and 2017, consist of the following:

| | **2018** | **2017** |
|---|---|---|
| Net realized gains | $ 236,840,345 | $ 261,734,575 |
| Net unrealized (losses) gains | (306,706,439) | 218,131,894 |
| Net realized and unrealized (losses) gains on investments | $ (69,866,094) | $ 479,866,469 |

**Fair Value Hierarchy**—The Foundation is subject to the provisions of FASB issued ASC 820, *Fair Value Measurements and Disclosures*, which establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value.

The carrying amounts reported in the statements of financial position for cash, accrued interest and dividends, accounts payable and other liabilities, borrowings under revolving line of credit, and deferred federal excise taxes approximate fair value because of their short-term nature.

ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability. As a basis for considering market participant assumptions in fair value measurements, ASC 820 establishes a fair value hierarchy that distinguishes between market participant assumptions based on market data obtained from sources independent of the reporting entity (observable inputs that are classified within Levels 1 and 2 of the hierarchy) and the reporting entity's own assumption about market participant assumptions (unobservable inputs classified within Level 3 of the hierarchy).

ASC 820 classifies the inputs used to measure fair value into the following hierarchy:

***Level 1***—Quoted market prices in active markets for identical assets or liabilities.

***Level 2***—Observable market-based inputs and unobservable inputs that are corroborated by market data.

***Level 3***—Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities. Level 3 includes values determined using pricing models, discounted cash flow methodologies, or similar techniques reflecting the Foundation's accounting policies.

Securities that provide a net asset value (NAV) or that are recorded under the equity method of accounting are considered to be recorded at Management's best estimate of fair value. These securities are included in the fair value table on the Investments measured at net asset value line.

In certain instances, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such instances, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The Foundation's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The financial assets and liabilities recorded at fair value on a recurring basis within the fair value hierarchy as of December 31, 2018, are as follows:

| | **2018** | **Level 1** | **Level 2** | **Level 3** |
|---|---|---|---|---|
| Temporary investments | $ (160,740) | $ (160,740) | $ - | $ - |
| Fixed-income securities: | | | | |
| U.S. treasury securities | 12,930,760 | 12,930,760 | - | - |
| Credit and other | 91,865,244 | 5,888,964 | 77,381,895 | 8,594,385 |
| U.S. equity securities | 120,547,244 | 120,547,244 | - | - |
| Foreign equity securities | 109,716,485 | 109,716,485 | - | - |
| Derivative contracts: | | | | |
| Equity | 25,186,069 | - | 25,186,069 | - |
| Foreign exchange | (1,513,822) | - | (1,513,822) | - |
| Other | (873,543) | - | (873,543) | - |
| Private equity | 82,701,718 | - | - | 82,701,718 |
| Real estate | 10,955,265 | - | - | 10,955,265 |
| Total fair value measurements | 451,354,680 | 248,922,713 | 100,180,599 | 102,251,368 |
| Investments measured at net asset value | 3,170,280,709 | - | - | - |
| Total investments | $ 3,621,635,389 | $ 248,922,713 | $ 100,180,599 | $ 102,251,368 |
| Collateral under securities lending agreement | $ 3,073,895 | $ 3,073,895 | $ - | $ - |

The financial assets and liabilities recorded at fair value on a recurring basis within the fair value hierarchy as of December 31, 2017, are as follows:

| | 2017 | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Temporary investments | $ 388,469 | $ 388,469 | $ - | $ - |
| Fixed-income securities: | | | | |
| U.S. treasury securities | 51,966,853 | 51,966,853 | - | - |
| Credit and other | 67,526,334 | 1,735,838 | 55,490,312 | 10,300,184 |
| U.S. equity securities | 158,225,104 | 158,225,104 | - | - |
| Foreign equity securities | 184,324,346 | 184,324,346 | - | - |
| Derivative contracts: | | | | |
| Equity | 13,765,912 | - | 13,765,912 | - |
| Foreign exchange | (3,585,623) | - | (3,585,623) | - |
| Natural resources | 86,324,055 | - | - | 86,324,055 |
| Private equity | 97,478,607 | - | - | 97,478,607 |
| Real estate | 13,953,207 | - | - | 13,953,207 |
| Total fair value measurements | 670,367,264 | 396,640,610 | 65,670,601 | 208,056,053 |
| Investments measured at net asset value | 3,190,539,103 | - | - | - |
| Total investments | $ 3,860,906,367 | $ 396,640,610 | $ 65,670,601 | $ 208,056,053 |
| Collateral under securities lending agreement | $ 2,905,846 | $ 2,905,846 | $ - | $ - |

Level 1 classifications consist of U.S. Treasuries and commercial paper with quoted market prices in active markets. Unsettled trade receivable and payable valuations are reflective of cash settlements subsequent to year-end. Fixed-income, U.S. equity securities, foreign equity securities, and certain exchange traded derivatives have readily determinable fair market values based on quoted prices in active markets.

Level 2 classifications consist of agency and Federal Home Loan Bank securities and collateralized loan obligation fixed-income securities that are valued based on observable market-based inputs and unobservable inputs that are corroborated by market data. The fair value of the derivative investments is based on market prices from the financial institution that is the counterparty to the derivative.

Level 3 classifications consist of securities that do not have readily determinable market values or are not publicly traded. The valuation process for Level 3 investments involves the use of fair value as reported by third-party administrators, fund investment managers, and general partners and is completed on at least a quarterly basis. All valuations are reviewed by management. Fair value estimates for fixed income securities, equity securities, and real estate investments are based on other market data for the same or comparable instruments and transactions. Natural resource investments are based on inputs provided by the general partner, audited financial information, and K-1 capital account balances to determine overall reasonableness of the recorded value. Audited information is only available annually, based on the partnerships' year-end. Because of the inherent uncertainty of valuations, values may differ from the values that would have been used had a ready market existed.

Activity related to the Level 3 investment activity as of December 31, 2018 and 2017, is as follows:

| | 2018 | 2017 |
|---|---|---|
| Additions and purchases | $ 25,699,350 | $ 70,648,420 |
| Transfers into Level 3 | - | - |
| Transfers out of Level 3 | (84,693,701) | (5,273,353) |

The Foundation's policy related to fair value measurement hierarchy classification, including any level transfers, occurs as of the end of the reporting period. Transfers out of Level 3 in 2018 and 2017 were the result of changes in the valuation of securities that do not require disclosure in the fair value hierarchy. Realized and unrealized gains or losses related to Level 3 investment activity are included in net investment income on the statements of activities. Unrealized losses attributable to Level 3 investments held as of December 31, 2017 totaled approximately $(3,406,000).

As of December 31, 2018 and 2017, the Foundation had commitments to contribute approximately $806,383,000 and $807,716,000, respectively, in additional capital under the terms of various investment agreements over the next 7–10 years.

In accordance with ASC 820, *Fair Value Measurements and Disclosures*, the Foundation classifies such investments as Level 2 when there is the ability to redeem the investment in the near term; however, if the Foundation does not have the ability to redeem its investment in the near term, the Foundation classifies such investments as Level 3. The Foundation defines near term to be within 90 days of the measurement date.

The Foundation's investment in funds that are valued using a NAV (or its equivalent) or that are recorded under the equity method of accounting have a redemption notice period of daily to biannually and primarily consist of the following:

| | 2018 Redemption Period | | | | |
|---|---|---|---|---|---|
| | **90 Days or Fewer** | **91 to 180 Days** | **181 to 365 Days** | **Greater than 365 Days** | **Total** |
| Fixed-income | $ - | $ 15,232,425 | $ 29,897,644 | $ 64,682,724 | $ 109,812,793 |
| U.S. equity | - | 18,727,516 | 113,351,988 | 156,841,342 | 288,920,846 |
| Foreign equity | 72,189,713 | 114,961,648 | 239,951,404 | 181,351,135 | 608,453,900 |
| Hedge funds | 144,553,215 | 133,680,912 | 44,571,623 | 210,998,158 | 533,803,908 |
| Natural resources | - | - | - | 356,488,901 | 356,488,901 |
| Private equity | - | - | - | 1,023,883,982 | 1,023,883,982 |
| Real estate | - | - | - | 248,916,379 | 248,916,379 |
| Total | $ 216,742,928 | $ 282,602,501 | $ 427,772,659 | $ 2,243,162,621 | $ 3,170,280,709 |

| | 2017 Redemption Period | | | | |
|---|---|---|---|---|---|
| | 90 Days or Fewer | 91 to 180 Days | 181 to 365 Days | Greater than 365 Days | Total |
| Fixed-income | $ 20,000,000 | $ 15,677,987 | $ 79,513,503 | $ 4,643,030 | $ 119,834,520 |
| U.S. equity | - | 21,030,530 | 195,551,508 | 66,090,402 | 282,672,440 |
| Foreign equity | 96,347,394 | 65,831,817 | 452,935,059 | 178,026,956 | 793,141,226 |
| Hedge funds | 161,788,642 | 101,467,876 | 77,866,454 | 145,128,917 | 486,251,889 |
| Natural resources | - | - | - | 277,501,236 | 277,501,236 |
| Private equity | 1,159,523 | - | - | 977,413,521 | 978,573,044 |
| Real estate | 111,910 | - | - | 252,452,838 | 252,564,748 |
| Total | $ 279,407,469 | $ 204,008,210 | $ 805,866,524 | $ 1,901,256,900 | $ 3,190,539,103 |

## 4. DERIVATIVES

The Foundation accounts for derivative financial instruments in accordance with ASC 815, *Derivatives and Hedging*. The Foundation enters into derivative arrangements to manage a variety of market risks and to adjust asset class exposure. The Foundation recognizes all derivatives as either assets or liabilities measured at fair value. The Foundation has netted liability positions against the investment balance. For accounting purposes, the derivatives do not have hedge designation, and all gains and losses are reported in the net realized and unrealized gains on investments on the statements of activities.

In connection with its derivative activities, the Foundation enters into master netting agreements and collateral support agreements with its counterparties. These agreements provide the Foundation with the right, in the event of default by the counterparty, to net a counterparty's rights and obligations under the agreement and to liquidate and set off collateral against any net amount owed by the counterparty. The master netting agreement is taken into account in the Foundation's risk management practices and application of counterparty credit limits.

To determine the amount of exposure to each counterparty, the Foundation nets the exposure on transactions by individual counterparty against the value of any collateral posted by the counterparty (a) when both parties owe determinable amounts, (b) where a legal right of setoff exists, and (c) when the right to setoff is enforceable by law. The thresholds for collateral postings vary by counterparty.

The aggregate fair value of derivative instruments in asset positions on December 31, 2018 and 2017, is approximately $44,391,000 and $15,469,000, respectively. The exposure to counterparty credit risk on December 31, 2018, is reduced by $16,706,000 of collateral held and approximately $14,643,000 of liabilities included in netting arrangements with those counterparties. The exposure to counterparty credit risk on December 31, 2017, is reduced by $10,000,000 of collateral held and approximately $1,634,000 of liabilities included in netting arrangements with those counterparties. The Foundation has never failed to access collateral when required. The Foundation has posted collateral of $1,400,000 and $0 to counterparties as of December 31, 2018 and 2017, respectively.

The fair values of derivative instruments in the statements of financial position and information about the offsetting of derivative instruments and related collateral amounts as of December 31, 2018 and 2017, are as follows:

| | **2018—Assets** | | | |
|---|---|---|---|---|
| | **Balance Sheet Location** | **Gross Amounts of Recognized Assets** | **Gross Amounts Offset in the Statements of Financial Position** | **Net Amounts of Assets Presented in the Statements of Financial Position** |
| Equity contracts | Investments | $ 44,391,282 | $ 31,225,266 | $ 13,166,016 |
| Foreign exchange contracts | Investments | - | - | - |
| Other contracts | Investments | - | 123,717 | (123,717) |
| Total derivative instruments | | $ 44,391,282 | $ 31,348,983 | $ 13,042,299 |

| | **2018—Liabilities** | | | |
|---|---|---|---|---|
| | **Balance Sheet Location** | **Gross Amounts of Recognized Liabilities** | **Gross Amounts Offset in the Statements of Financial Position** | **Net Amounts of Liabilities Presented in the Statements of Financial Position** |
| Equity contracts | Investments | $ 19,205,213 | $ 15,919,474 | $ 3,285,739 |
| Foreign exchange contracts | Investments | 1,513,822 | - | 1,513,822 |
| Other contracts | Investments | 873,543 | 123,717 | 749,826 |
| Total derivative instruments | | $ 21,592,578 | $ 16,043,191 | $ 5,549,387 |

| | **2017—Assets** | | | |
|---|---|---|---|---|
| | **Balance Sheet Location** | **Gross Amounts of Recognized Assets** | **Gross Amounts Offset in the Statements of Financial Position** | **Net Amounts of Assets Presented in the Statements of Financial Position** |
| Equity contracts | Investments | $ 15,468,889 | $ 11,634,038 | $ 3,834,851 |
| Foreign exchange contracts | Investments | - | - | - |
| Total derivative instruments | | $ 15,468,889 | $ 11,634,038 | $ 3,834,851 |

| | **2017—Liabilities** | | | |
|---|---|---|---|---|
| | **Balance Sheet Location** | **Gross Amounts of Recognized Liabilities** | **Gross Amounts Offset in the Statements of Financial Position** | **Net Amounts of Liabilities Presented in the Statements of Financial Position** |
| Equity contracts | Investments | $ 1,702,977 | $ 1,634,038 | $ 68,939 |
| Foreign exchange contracts | Investments | 3,585,623 | - | 3,585,623 |
| Total derivative instruments | | $ 5,288,600 | $ 1,634,038 | $ 3,654,562 |

The Foundation does not have any gross amounts of financial instruments or cash collateral received or pledged not offset in the statements of financial position, except for $3,894,000 held related to two counterparties as of December 31, 2018.

The effect of derivative instruments on the statements of activities as of December 31, 2018 and 2017, is as follows:

| | | Gain (Loss) Recognized on Derivatives | |
|---|---|---|---|
| | **Location of Gains (Losses)** | **2018** | **2017** |
| Equity contracts | Net investment (loss) income | $ 33,103,685 | $ 9,263,102 |
| Interest rate contracts | Net investment (loss) income | - | (109,294) |
| Foreign exchange contracts | Net investment (loss) income | 2,071,801 | 2,264,552 |
| Other contracts | Net investment (loss) income | (2,225,015) | 3,713,230 |
| Total derivative instruments | | $ 32,950,471 | $ 15,131,590 |

The Foundation is not credit rated, and therefore, no credit rating contingent provisions are required by counterparties.

Counterparty credit risk is the risk that counterparties to derivative contracts will fail to perform according to the terms of the agreements. Nationally recognized statistical rating organizations, such as Standard & Poor's (S&P) and Moody's, assign credit ratings to security issuers that indicate a measure of potential credit risk to investors. The Foundation manages credit risk by reviewing the credit standing of each counterparty and limits exposure to credit risk by requiring that the minimum acceptable credit rating of the counterparty be BBB- and Baa3 for S&P and Moody's, respectively.

## 5. PROGRAM-RELATED INVESTMENTS

PRIs in the statements of financial position represent various below-market-rate loans, equity investments and linked deposits with outstanding principal totaling $78,237,586 and $66,898,016 as of December 31, 2018 and 2017, respectively. Interest rates range from 1% to 4% at December 31, 2018. Loans are individually monitored to determine net realizable value based on an evaluation of recoverability. Net realizable value approximates fair value. There was $6,316,497 and $4,915,604 received as return of principal for the years ended December 31, 2018 and 2017, respectively. The Foundation has PRI commitments of approximately $21,707,966 and $35,223,539 as of December 31, 2018 and 2017, respectively.

PRIs are scheduled for collection as of December 31, 2018, as follows:

| **Years Ending December 31,** | |
|---|---|
| 2019 | $ 7,500,553 |
| 2020 | 8,260,156 |
| 2021 | 8,218,176 |
| 2022 | 12,107,665 |
| 2023 | 2,135,958 |
| 2024 and beyond | 40,015,078 |
| | 78,237,586 |
| Less allowance | (4,322,495) |
| Net | $ 73,915,091 |

Management has reviewed the collectability of all PRIs and has recorded an allowance of $4,322,495 and $4,527,049 as of December 31, 2018 and 2017, respectively. The Foundation establishes a loan loss allowance in accordance with the risk rating assigned to the PRI. The risk rating is based on a combination of financial and organizational factors and is evaluated annually unless more frequent monitoring is required.

The Foundation has entered into 20 third party loan guarantee agreements totaling $55,988,000 and $30,929,000, of which loss exposure related to the guarantees is $19,655,000 and $19,392,000 as of December 31, 2018 and 2017, respectively. The Foundation has recorded a contingent liability at the larger of the net present value of the guarantees or the minimum amount of probable loss. The Foundation recorded a contingency of $737,764 and $523,211 as of December 31, 2018 and 2017, respectively.

## 6. GRANTS PAYABLE

Grants payable represent the present value of grants using a 1.87% and 0.85% discount rate, as of December 31, 2018 and 2017, respectively. The discount rate is a Level 2 input and is based on the present value of discounted cash flows using the three-month U.S. Treasury rate. The Foundation made grant payments of approximately $163,300,000 and $170,600,000 in 2018 and 2017, respectively.

The Foundation's future grant commitments, which are scheduled for payment in future years as of December 31, 2018, are as follows:

| **Years Ending December 31,** | |
|---|---|
| 2019 | $ 45,212,586 |
| 2020 | 9,179,107 |
| 2021 | 1,378,786 |
| 2022 | 1,100,000 |
| 2023 | 300,000 |
| 2024 and beyond | 1,050,000 |
| | 58,220,479 |
| Discount | (1,465,277) |
| Net | $ 56,755,202 |

## 7. EXCISE TAX REQUIREMENTS

The Foundation is exempt from federal income taxes under Section 501(c)(3) of the Code, but is subject to a 2% (1% if certain criteria are met) federal excise tax on net investment income, including realized gains, as defined in the Code. The current excise tax is provided at 1% for both 2018 and 2017. The deferred excise tax provision is calculated assuming a 2% rate and is based on projected gains that assume complete liquidation of all assets. The current and deferred portions of the excise tax provision for 2018 were approximately $1,949,000 and $(6,134,000), respectively. The current and deferred portions of the excise tax provision for 2017 were approximately $2,552,000 and $4,363,000, respectively. Cash payments for federal excise taxes were $4,900,000 and $3,500,000 for the years ended December 31, 2018 and 2017, respectively. Federal excise taxes payable were $0 as of December 31, 2018 and 2017. The unrelated business income tax expense for 2018 and 2017 was $0 and $777,000 for the years ended December 31, 2018 and 2017, respectively. The prepaid unrelated business taxes were $595,000 and $2,049,000 as of December 31, 2018 and 2017, respectively. The Foundation recorded a deferred tax asset of $1,431,000 and $1,226,000 related to unrelated business income net operating loss and alternative minimum tax credit carry forwards as of December 31, 2018 and 2017, respectively.

## 8. OTHER POSTEMPLOYMENT BENEFITS

The Foundation is subject to the provisions of FASB-issued ASC 715, *Compensation—Retirement Benefits*, which requires recognition of the overfunded or underfunded status of the other postemployment benefit plan as an asset or liability in the statements of financial position and recognition of changes in the funded status in the year in which the changes occur. The funded status of the plan is measured as the difference between the fair value of plan assets and the benefit obligation.

The Foundation provides certain health care and life insurance benefits for retired employees. The Foundation's employees may become eligible for these postemployment employee benefits. Actuarial assumptions and participant data changes are reported in other postemployment adjustments in the statement of activities.

The other postemployment benefit plan-funded status and amounts recognized in the Foundation's statements of financial position and statements of activities as of and for the years ended December 31, 2018 and 2017, are as follows:

| | **Postemployment Employee Benefits** | |
|---|---|---|
| | **2018** | **2017** |
| Fair value of plan assets | $ - | $ - |
| Benefit obligation | (7,606,091) | (8,777,196) |
| Funded status of the plan | $ (7,606,091) | $ (8,777,196) |
| Accrued benefit liability recognized in the statement of financial position—January 1 | $ (8,777,196) | $ (8,125,584) |
| Service cost | $ 392,776 | $ 343,451 |
| Interest cost | 307,716 | 314,317 |
| Prior-service cost amortization | (899,207) | (899,207) |
| Benefit cost recognized in the statements of activities | $ (198,715) | $ (241,439) |
| Actuarial (gain) loss recognized in the statements of activities | $ (779,542) | $ 1,032,459 |
| Employer contributions | $ 192,848 | $ 139,408 |
| Benefits paid | $ (192,848) | $ (139,408) |
| Benefit obligation—December 31 | $ (7,606,091) | $ (8,777,196) |

The actuarial gain of approximately $800,000 for December 31, 2018 can be attributed to a $1,100,000 gain due to a change in the assumptions used to calculate life insurance benefits, a $700,000 gain due to the change in the discount rate from 3.56% at December 31, 2017 to 4.15% at December 31, 2018, a gain of $20,000 due to mortality assumptions, and a gain of $80,000 due to changes in the benefit accrual offset by losses of $900,000 due to amortization of prior service costs and $200,000 of life insurance administrative costs.

The actuarial loss of approximately $1,000,000 for December 31, 2017 can be attributed to a $700,000 loss due to the change in the discount rate from 4.10% at December 31, 2016 to 3.56% at December 31, 2017, a $900,000 loss in amortization of prior service costs offset by gains of $200,000 due to updated mortality assumptions, $300,000 due to updated census data and $100,000 due to changes in the benefit accrual.

The plan amendment resulted in the stabilization of the Foundation's other postretirement benefit obligation through the implementation of health reimbursement accounts which allows participants greater flexibility with multiple plan options.

| | Postemployment Employee Benefits | |
|---|---|---|
| **Assumptions and Dates Used for Liability** | **2018** | **2017** |
| Discount rate | 4.15 % | 3.56 % |
| Compensation increase rate | 4.00 | 4.00 |
| Measurement date | December 31 | |
| **Assumptions Used to Determine Expense** | | |
| Discount rate | 3.56 % | 4.10 % |
| Compensation increase rate | 4.00 | 4.00 |
| Health care cost trend rate assumptions: | | |
| Initial trend rate: Pre/Post Medicare | N/A | N/A |
| Ultimate trend rate: Pre/Post Medicare | N/A | N/A |
| Year ultimate trend is reached: Pre/Post Medicare | N/A | N/A |

A one-percentage-point change in assumed health care cost trends rates as of December 31, 2018, would not have any effect on postemployment benefit obligations.

Expected amortization during 2019 for amortization of net prior service credit and amortization of net loss are $781,494 and $138,066, respectively.

**Future Expected Benefit Payments**

| | |
|---|---|
| 2019 | $ 280,650 |
| 2020 | 311,633 |
| 2021 | 334,274 |
| 2022 | 354,277 |
| 2023 | 368,398 |
| 2024–2028 | 2,004,737 |

## 9. ANALYSIS OF EXPENSES

The Foundation's grant and administrative expenses have been allocated between program and supporting activities. Grantmaking activities of the Foundation involving reviewing proposals, awarding, monitoring and evaluating grants as well as the actual payment of grants have been allocated to the program function. All other administrative expenses related to managing the operations of the foundation have been allocated to the supporting activities function. Certain categories of expenses that are incurred for the Foundation as a whole and are attributable to one or more functions are allocated based on either management estimates of time and effort or building occupancy square footage.

The Foundation's functional expenses, displayed by natural expense classification, for the year ended December 31, 2018 and 2017 are as follows:

| | 2018—Allocation of Expenses | | |
|---|---|---|---|
| | Program Activities | Supporting Activities | Total Expenses |
| Grants—net | $114,829,604 | $ - | $114,829,604 |
| Salary, benefits and payroll taxes | 13,957,303 | 4,528,576 | 18,485,879 |
| Professional service fees | 3,223,888 | 367,180 | 3,591,068 |
| Travel, conferences and meetings | 1,848,076 | 279,450 | 2,127,526 |
| Sponsored convenings | 1,724,725 | 24,532 | 1,749,257 |
| Depreciation | 984,853 | 664,392 | 1,649,245 |
| Occupancy | 552,097 | 277,460 | 829,557 |
| Legal, accounting and tax fees | 394,055 | 187,100 | 581,155 |
| PRI loan loss allowance | (65,049) | - | (65,049) |
| Other expenses | 1,134,409 | 1,000,747 | 2,135,156 |
| | $138,583,961 | $7,329,437 | $145,913,398 |

| | 2017—Allocation of Expenses | | |
|---|---|---|---|
| | Program Activities | Supporting Activities | Total Expenses |
| Grants—net | $149,311,048 | $ - | $149,311,048 |
| Salary, benefits and payroll taxes | 12,687,199 | 3,548,891 | 16,236,090 |
| Professional service fees | 4,075,995 | 318,584 | 4,394,579 |
| Travel, conferences and meetings | 1,631,121 | 222,376 | 1,853,497 |
| Sponsored convenings | 954,057 | 29,879 | 983,936 |
| Depreciation | 1,018,349 | 686,989 | 1,705,338 |
| Occupancy | 536,412 | 283,461 | 819,873 |
| Legal, accounting and tax fees | 425,853 | 246,248 | 672,101 |
| PRI loan loss allowance | 1,655,834 | - | 1,655,834 |
| Other expenses | 903,664 | 797,920 | 1,701,584 |
| | $173,199,532 | $6,134,348 | $179,333,880 |

## 10. LIQUIDITY AND AVAILABILITY OF RESOURCES

The Foundation's financial assets that are readily available within one year of December 31, 2018 to meet general expenditures include:

| | 2018 |
|---|---|
| Cash | $ 1,768,211 |
| Actively traded investments | 248,922,713 |
| Investments measured at NAV | 927,118,088 |
| Total financial assets | $ 1,177,809,012 |

The Foundation must annually pay out a minimum amount of 5% of the average fair value of its investment assets for the preceding year for charitable and administrative purposes in accordance with private foundation Internal Revenue Service requirements. The Foundation structures its financial assets to manage liquidity in a manner to meet this distribution requirement. The Foundation invests in various short-term investments, securities and alternatives which are available and liquid within one year. Additionally, as more fully described in Note 2, the Foundation has a line of credit available for immediate or unanticipated liquidity needs.

## 11. SUBSEQUENT EVENTS

There have been no subsequent events through June 6, 2019, the date these financial statements were issued, requiring adjustment to, or disclosure in, the financial statements.

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