

The Kresge Foundation

(A Michigan Trustee Corporation)

Financial Statements as of and for the
Years Ended December 31, 2017 and 2016, 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, 2017 and 2016, 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, 2017 and 2016, 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.

Deloitte + Touche LLP

June 6, 2018

THE KRESGE FOUNDATION
(A Michigan Trustee Corporation)

STATEMENTS OF FINANCIAL POSITION
AS OF DECEMBER 31, 2017 AND 2016

	2017	2016
ASSETS		
CASH	\$ 1,764,857	\$ 740,342
INVESTMENTS—At fair market value	3,860,906,367	3,577,575,196
PROGRAM-RELATED INVESTMENTS—Net of allowance of \$4,527,049 and \$2,871,215, respectively	62,370,967	43,993,190
COLLATERAL UNDER SECURITIES LENDING AGREEMENT	2,905,846	2,728,233
ACCRUED INTEREST AND DIVIDENDS	1,502,881	2,333,532
PROPERTY AND EQUIPMENT—Net of accumulated depreciation of \$10,752,186 and \$9,524,215, respectively	19,101,169	20,483,791
OTHER	<u>6,084,838</u>	<u>4,102,991</u>
TOTAL	<u>\$3,954,636,925</u>	<u>\$3,651,957,275</u>
 LIABILITIES AND UNRESTRICTED NET ASSETS		
LIABILITIES:		
Grants payable—net of discount of \$997,732 and \$389,690, respectively	\$ 89,753,579	\$ 88,073,289
Accounts payable and other liabilities	6,237,260	5,559,499
Other postemployment benefit liability	8,777,196	8,125,584
Borrowings under revolving line of credit	25,776,663	27,709,850
Payable under securities lending agreement	2,905,846	2,728,233
Deferred federal excise taxes	<u>19,016,682</u>	<u>14,654,044</u>
Total liabilities	152,467,226	146,850,499
UNRESTRICTED NET ASSETS	<u>3,802,169,699</u>	<u>3,505,106,776</u>
TOTAL	<u>\$3,954,636,925</u>	<u>\$3,651,957,275</u>

See notes to financial statements.

THE KRESGE FOUNDATION
(A Michigan Trustee Corporation)

STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
INVESTMENT INCOME AND LOSS:		
Interest, dividends, and other income	\$ 14,003,395	\$ 21,552,066
Net realized and unrealized gains on investments	479,866,469	128,413,231
Investment management fees	(2,740,956)	(2,370,867)
Federal excise tax expense and other	<u>(8,965,230)</u>	<u>(5,452,069)</u>
Net investment income	<u>482,163,678</u>	<u>142,142,361</u>
EXPENSES:		
Grants approved—net of change in discount of \$608,042 and \$324,926, respectively	149,311,048	149,190,444
Administrative expenses	<u>34,757,248</u>	<u>35,936,308</u>
Total expenses	<u>184,068,296</u>	<u>185,126,752</u>
OTHER POSTEMPLOYMENT ADJUSTMENTS	<u>(1,032,459)</u>	<u>4,549,802</u>
CHANGE IN UNRESTRICTED NET ASSETS	297,062,923	(38,434,589)
UNRESTRICTED NET ASSETS:		
Beginning of year	<u>3,505,106,776</u>	<u>3,543,541,365</u>
End of year	<u>\$3,802,169,699</u>	<u>\$3,505,106,776</u>

See notes to financial statements.

THE KRESGE FOUNDATION
(A Michigan Trustee Corporation)

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Change in unrestricted net assets	\$ 297,062,923	\$ (38,434,589)
Adjustments to reconcile change in unrestricted net assets to net cash used in operating activities:		
Depreciation	1,705,338	1,770,896
Loss on disposals of property and equipment	6,375	358
Increase in program-related investments provision	1,655,834	921,463
Change in value of grants payable	(608,042)	(324,926)
Net realized and unrealized gains on investments	(479,866,469)	(128,413,231)
Net unrealized loss on program related investments	40,000	-
Changes in assets and liabilities:		
Accrued interest and dividends	830,651	(435,248)
Other assets	(1,981,847)	972,821
Approved grants payable	2,288,332	781,042
Accounts payable and other liabilities	677,761	(68,167)
Other postemployment benefit liability	651,612	(3,921,133)
Deferred federal excise taxes	4,362,638	1,118,402
	<u>(173,174,894)</u>	<u>(166,032,312)</u>
Net cash used in operating activities		
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales of investments	1,270,637,933	1,285,740,717
Purchases of investments	(1,074,102,635)	(1,100,033,063)
Returns of principal for program-related investments	4,915,604	4,027,261
Disbursements for program-related investments	(24,989,215)	(12,115,346)
Purchases of property and equipment	(329,091)	(866,440)
	<u>176,132,596</u>	<u>176,753,129</u>
Net cash provided by investing activities		
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from revolving line of credit	25,776,663	38,486,695
Repayments of revolving line of credit	(27,709,850)	(49,135,721)
	<u>(1,933,187)</u>	<u>(10,649,026)</u>
Net cash used in financing activities		
NET INCREASE IN CASH	1,024,515	71,791
CASH:		
Beginning of year	<u>740,342</u>	<u>668,551</u>
End of year	<u>\$ 1,764,857</u>	<u>\$ 740,342</u>

See notes to financial statements.

THE KRESGE FOUNDATION
(A Michigan Trustee Corporation)

NOTES TO FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

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 \$1,705,338 and \$1,770,896 as of December 31, 2017 and 2016, 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, 2017 and 2016, consists of the following:

	2017	2016
Building and improvements	\$ 24,154,705	\$ 24,053,945
Furniture and fixtures	1,995,019	1,994,525
Computer and office equipment	<u>3,048,491</u>	<u>3,331,040</u>
	29,198,215	29,379,510
Less accumulated depreciation and amortization	<u>(10,752,186)</u>	<u>(9,524,215)</u>
Subtotal depreciable assets—net	<u>18,446,029</u>	<u>19,855,295</u>
Land	500,000	500,000
Art	140,466	128,496
Construction in progress	<u>14,674</u>	<u>-</u>
Subtotal nondepreciable assets	<u>655,140</u>	<u>628,496</u>
Total property and equipment—net	<u>\$ 19,101,169</u>	<u>\$ 20,483,791</u>

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 \$85,100,000 and \$89,400,000 in conditional grants as of December 31, 2017 and 2016, respectively. At December 31, 2017, conditional grants included \$80,000,000 to the Foundation for Detroit’s Future (FDF), payable in equal installments over a 16 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, 2017 and 2016. 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 2.14% and 1.45% and contains a commitment fee on the unused available balance of 0.17% as of December 31, 2017 and 2016. As of December 31, 2017 and 2016, the outstanding borrowings were \$25,776,663 and \$27,709,850, respectively. The aggregate outstanding principal, interest, and related fees are due in full on the commitment termination date August 31, 2018. Interest and related fees payable at year-end are included in accounts payable and other liabilities.

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, 2014. The Foundation evaluates uncertain tax positions for more-likely than-not sustainability. The Foundation has concluded that as of December 31, 2017 and 2016, 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 percent to 21 percent; (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 May 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standard Update (ASU) No. 2015-07, *Fair Value Measurement: Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share*. The new guidance has removed, from the fair value hierarchy, investments for which the practical expedient is used to measure fair value at net asset value (NAV). The adoption of this pronouncement has removed, from the fair value hierarchy in Note 3, investment balances of \$3,190,539,103 and \$2,995,515,805 in 2017 and 2016, respectively. The Foundation has included these investments as a reconciling line item so that the total investments presented in the fair value hierarchy is consistent with the amount presented in the Statements of Financial Position. The guidance has been adopted as of January 1, 2017 and has been retrospectively applied for all comparative periods presented. ASU No. 2015-07 did not impact the Statements of Financial Position or the Statements of Activities as of and for the years ended December 31, 2017 and December 31, 2016.

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 is effective for the Foundation for years beginning after December 15, 2017, with retrospective application required for all comparative periods presented with certain disclosure exceptions. At this time, the Foundation is evaluating the implications of ASU No. 2016-14 and its effects on the financial statements.

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 addresses how certain cash receipts and cash payments are presented and classified in the Statements of Cash Flows. The guidance is effective for the Foundation for years beginning after December 15, 2017, with early adoption permitted. We are currently assessing the impact that this standard will have on the financial statements.

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 \$1,107,000 and \$1,673,000 as of December 31, 2017 and 2016, respectively. The Foundation had unsettled trade sales of approximately \$21,215,000 and \$31,461,000 as of December 31, 2017 and 2016, 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 and exchange traded securities. 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, 2017 and 2016, the Foundation had loaned securities with a total market value of approximately \$3,940,000 and \$6,011,000, respectively, and received related cash collateral of approximately \$2,906,000 and \$2,728,000, 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 \$17,000 and \$96,000 for the years ended December 31, 2017 and 2016, respectively.

The changes in security lending collateral of approximately \$178,000 and \$(14,504,000) as of December 31, 2017 and 2016, 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, 2017 and 2016, consist of the following:

	2017	2016
Net realized gains	\$ 261,734,575	\$ 72,492,355
Net unrealized gains	<u>218,131,894</u>	<u>55,920,876</u>
Net realized and unrealized gains on investments	<u>\$ 479,866,469</u>	<u>\$ 128,413,231</u>

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, 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	<u>13,953,207</u>	<u>-</u>	<u>-</u>	<u>13,953,207</u>
Total fair value measurements	670,367,264	396,640,610	65,670,601	208,056,053
Investments measured at net asset value	<u>3,190,539,103</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total investments	<u>\$3,860,906,367</u>	<u>\$396,640,610</u>	<u>\$65,670,601</u>	<u>\$208,056,053</u>
Collateral under securities lending agreement	<u>\$ 2,905,846</u>	<u>\$ 2,905,846</u>	<u>\$ -</u>	<u>\$ -</u>

The financial assets and liabilities recorded at fair value on a recurring basis within the fair value hierarchy as of December 31, 2016, are as follows:

	2016	Level 1	Level 2	Level 3
Temporary investments	\$ 53,082,983	\$ 53,082,983	\$ -	\$ -
Fixed-income securities:				
U.S. treasury securities	37,400,593	37,400,593	-	-
Credit and other	41,804,205	35,879	31,057,600	10,710,726
U.S. equity securities	88,361,724	86,711,604	-	1,650,120
Foreign equity securities	120,823,326	120,823,326	-	-
Derivative contracts:				
Equity	32,981,358	-	32,981,358	-
Interest rate	(103,296)	-	(103,296)	-
Foreign exchange	33,596,731	-	33,596,731	-
Other	1,517,861	-	1,517,861	-
Natural resources	82,703,414	-	-	82,703,414
Private equity	69,577,207	-	-	69,577,207
Real estate	<u>20,313,285</u>	<u>-</u>	<u>-</u>	<u>20,313,285</u>
Total fair value measurements	582,059,391	298,054,385	99,050,254	184,954,752
Investments measured at net asset value	<u>2,995,515,805</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total investments	<u>\$3,577,575,196</u>	<u>\$298,054,385</u>	<u>\$99,050,254</u>	<u>\$184,954,752</u>
Collateral under securities lending agreement	<u>\$ 2,728,233</u>	<u>\$ 2,728,233</u>	<u>\$ -</u>	<u>\$ -</u>

The negative asset balances as of December 31, 2017 and 2016 represent liability positions on derivative contracts.

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.

A reconciliation of the beginning and ending balance of the Level 3 investment activity that is measured at fair value using unobservable inputs as of December 31, 2017 and 2016, is as follows:

	2017	2016
Balance—beginning of year	\$ 184,954,752	\$ 129,202,755
Total realized and unrealized (losses)/gains included in change in net assets	(4,308,214)	9,000,927
Additions and purchases	70,648,420	57,669,628
Sales and maturities	(37,965,552)	(11,046,138)
Transfers into Level 3	-	127,580
Transfers out of Level 3	<u>(5,273,353)</u>	<u>-</u>
Balance—end of year	<u>\$ 208,056,053</u>	<u>\$ 184,954,752</u>

The 2016 beginning balance has been restated to reflect the adoption of ASU 2015-07, Fair Value Measurement: Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share and the removal of \$2,827,753,112 from the Level 3 fair value hierarchy.

Unrealized (loss)/gains attributable to Level 3 investments held at year end totaled approximately \$(3,406,000) and \$21,469,000 as of December 31, 2017 and 2016, respectively.

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 2017 were the result of changes in the valuation of securities that do not require disclosure in the fair value hierarchy. Transfers into Level 3 in 2016 are recorded in accordance with the near-term guidance of ASC 820, *Fair Value Measurements and Disclosures*. There were no transfers between Level 1 and Level 2 for the years ended December 31, 2017 and 2016.

Gains (realized and unrealized) as reported above are included in net investment income on the statements of activities.

As of December 31, 2017 and 2016, the Foundation had commitments to contribute approximately \$807,716,000 and \$751,417,000, 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:

2017 Redemption Period					
	90 Days or Fewer	91 to 180 Days	181 to 400 Days	Greater than 400 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	<u>111,910</u>	<u>-</u>	<u>-</u>	<u>252,452,838</u>	<u>252,564,748</u>
Total	<u>\$ 279,407,469</u>	<u>\$ 204,008,210</u>	<u>\$ 805,866,524</u>	<u>\$ 1,901,256,900</u>	<u>\$ 3,190,539,103</u>

2016 Redemption Period					
	90 Days or Fewer	91 to 180 Days	181 to 400 Days	Greater than 400 Days	Total
Fixed-income	\$ -	\$ 59,043,383	\$ 65,189,919	\$ -	\$ 124,233,302
U.S. equity	-	-	135,744,193	114,516,579	250,260,772
Foreign equity	97,678,437	76,303,107	405,930,490	134,904,915	714,816,949
Hedge funds	96,737,842	183,725,349	135,676,416	30,863,077	447,002,684
Natural resources	-	-	-	288,324,799	288,324,799
Private equity	-	-	-	931,463,547	931,463,547
Real estate	<u>-</u>	<u>-</u>	<u>-</u>	<u>239,413,752</u>	<u>239,413,752</u>
Total	<u>\$ 194,416,279</u>	<u>\$ 319,071,839</u>	<u>\$ 742,541,018</u>	<u>\$ 1,739,486,669</u>	<u>\$ 2,995,515,805</u>

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, 2017 and 2016, is approximately \$15,469,000 and \$76,949,000, respectively. 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 exposure to counterparty credit risk on December 31, 2016, is reduced by \$50,982,000 of collateral held and approximately \$8,957,000 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 \$0 and \$2,100,000 to counterparties as of December 31, 2017 and 2016, 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, 2017 and 2016, are as follows:

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		<u>\$ 15,468,889</u>	<u>\$ 11,634,038</u>	<u>\$ 3,834,851</u>

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	<u>3,585,623</u>	-	<u>3,585,623</u>
Total derivative instruments		<u>\$ 5,288,600</u>	<u>\$ 1,634,038</u>	<u>\$ 3,654,562</u>

2016—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	\$ 37,084,634	\$ 21,344,735	\$ 15,739,899
Interest rate contracts	Investments	499,960	890,175	(390,215)
Foreign exchange contracts	Investments	37,846,869	37,703,942	142,927
Other contracts	Investments	<u>1,517,861</u>	-	<u>1,517,861</u>
Total derivative instruments		<u>\$ 76,949,324</u>	<u>\$ 59,938,852</u>	<u>\$ 17,010,472</u>

2016—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	\$ 4,103,276	\$ 4,103,276	\$ -
Interest rate contracts	Investments	603,256	603,256	-
Foreign exchange contracts	Investments	4,250,138	4,250,138	-
Other contracts	Investments	<u>-</u>	<u>-</u>	<u>-</u>
Total derivative instruments		<u>\$ 8,956,670</u>	<u>\$ 8,956,670</u>	<u>\$ -</u>

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 as of December 31, 2017.

The effect of derivative instruments on the statements of activities as of December 31, 2017 and 2016, is as follows:

		Gain (Loss) Recognized on Derivatives	
		2017	2016
Location of Gains (Losses)			
Equity contracts	Net realized and unrealized gains on investments	\$ 9,263,102	\$ 9,616,014
Interest rate contracts	Net realized and unrealized gains on investments	(109,294)	164,391
Foreign exchange contracts	Net realized and unrealized gains on investments	2,264,552	654,860
Other contracts	Net realized and unrealized gains on investments	<u>3,713,230</u>	<u>6,660,340</u>
Total derivative instruments		<u>\$ 15,131,590</u>	<u>\$ 17,095,605</u>

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 \$66,898,016 and \$46,864,405 as of December 31, 2017 and 2016, respectively. Interest rates range from 1.0% to 4.0% at December 31, 2017. Loans are individually monitored to determine net realizable value based on an evaluation of recoverability. Net realizable value approximates fair value. There was \$4,915,604 and \$4,027,261 received as return of principal for the years ended December 31, 2017 and 2016, respectively. The Foundation has PRI commitments of approximately \$35,223,539 and \$54,043,000 as of December 31, 2017 and 2016, respectively.

PRI's are scheduled for collection as of December 31, 2017, as follows:

Years Ending December 31,	
2018	\$ 2,751,185
2019	7,400,553
2020	9,064,973
2021	8,468,176
2022	11,881,499
2023 and beyond	<u>27,331,630</u>
	66,898,016
Less allowance	<u>(4,527,049)</u>
Net	<u>\$62,370,967</u>

Management has reviewed the collectability of all PRI's and has recorded an allowance of \$4,527,049 and \$2,871,215 as of December 31, 2017 and 2016, 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 16 third party loan guarantee agreements totaling \$30,929,000 and \$27,734,000, of which loss exposure related to the guarantees is \$19,392,000 and \$13,839,000 as of December 31, 2017 and 2016, 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 \$523,211 and \$483,331 as of December 31, 2017 and 2016, respectively.

6. GRANTS PAYABLE

Grants payable represent the present value of grants using a 0.85% and 0.32% discount rate, as of December 31, 2017 and 2016, 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 \$170,600,000 and \$158,800,000 in 2017 and 2016, respectively.

The Foundation's future grant commitments, which are scheduled for payment in future years as of December 31, 2017, are as follows:

Years Ending December 31,	
2018	\$ 69,369,524
2019	17,896,787
2020	2,360,000
2021	225,000
2022	450,000
2023 and beyond	<u>450,000</u>
	90,751,311
Discount	<u>(997,732)</u>
Net	<u>\$ 89,753,579</u>

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 2017 and 2016. 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 2017 were approximately \$2,552,000 and \$4,363,000, respectively. The current and deferred portions of the excise tax provision for 2016 were approximately \$983,000 and \$1,118,000, respectively. Cash payments for federal excise taxes were \$3,500,000 and \$500,000 for the years ended December 31, 2017 and 2016, respectively. Federal excise taxes payable were \$0 as of December 31, 2017 and 2016. The unrelated business income tax expense for 2017 and 2016 was \$777,000 and \$1,187,000 for the years ended December 31, 2017 and 2016, respectively. The prepaid unrelated business taxes were \$2,049,000 and \$1,188,000 as of December 31, 2017 and 2016, respectively. The Foundation recorded a deferred tax asset of \$1,226,000 and \$1,123,000 related to unrelated business income net operating loss and alternative minimum tax credit carry forwards as of December 31, 2017 and 2016, 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, 2017 and 2016, are as follows:

	Postemployment Employee Benefits	
	2017	2016
Fair value of plan assets	\$ -	\$ -
Benefit obligation	<u>(8,777,196)</u>	<u>(8,125,584)</u>
Funded status of the plan	<u>\$ (8,777,196)</u>	<u>\$ (8,125,584)</u>
Accrued benefit liability recognized in the statement of financial position—January 1	<u>\$ (8,125,584)</u>	<u>\$ (12,046,717)</u>
Service cost	\$ 343,451	\$ 778,053
Interest cost	314,317	463,401
Prior-service cost amortization	(899,207)	(320,447)
Net amortization loss	<u>-</u>	<u>-</u>
Benefit cost recognized in the statements of activities	<u>\$ (241,439)</u>	<u>\$ 921,007</u>
Actuarial loss (gain) recognized in the statements of activities	<u>\$ 1,032,459</u>	<u>\$ (4,549,802)</u>
Employer contributions	<u>\$ 139,408</u>	<u>\$ 292,338</u>
Benefits paid	<u>\$ (139,408)</u>	<u>\$ (292,338)</u>
Benefit obligation—December 31	<u>\$ (8,777,196)</u>	<u>\$ (8,125,584)</u>

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 actuarial gain of approximately \$4,500,000 for December 31, 2016 can be attributed to a \$5,600,000 gain due to a plan amendment, a \$900,000 loss due to the change in the discount rate from 4.32% at December 31, 2015 to 4.10% at December 31, 2016, a \$100,000 gain due to updated mortality assumptions offset by approximately \$300,000 in amortization of prior service cost.

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.

Assumptions and Dates Used for Liability	Postemployment Employee Benefits	
	2017	2016
Discount rate	3.56 %	4.10 %
Compensation increase rate	4.00	4.00
Measurement date	December 31	
 Assumptions Used to Determine Expense		
Discount rate	4.10 %	4.32 %
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, 2017, would not have any effect on postemployment benefit obligations.

Expected amortization during 2018 for amortization of net prior service credit and amortization of net loss are \$899,207 and \$0, respectively.

Future Expected Benefit Payments

2018	\$ 269,356
2019	275,729
2020	307,345
2021	330,415
2022	350,445
2023–2027	1,939,829

9. SUBSEQUENT EVENTS

There have been no subsequent events through June 6, 2018, the date these financial statements were issued, requiring adjustment to, or disclosure in, the financial statements.

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