Financial Statements

Cleveland Institute of Music
Years Ended June 30, 2016 and 2015
With Report of Independent Auditors

Ernst & Young LLP

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Cleveland Institute of Music

Financial Statements

Years Ended June 30, 2016 and 2015

Contents

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Report of Independent Auditors

The Board of Trustees
Cleveland Institute of Music

We have audited the accompanying financial statements of Cleveland Institute of Music, which comprise the statements of financial position as of June 30, 2016 and 2015, 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 conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Cleveland Institute of Music as of June 30, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

December 6, 2016

Cleveland Institute of Music

Statements of Financial Position

June 30, 2016 With Comparative
Totals for June 30, 2015

				June 30	
		Temporarily	Permanently	2016	2015
	Unrestricted	Restricted	Restricted	Total	Total
Assets					
Cash and cash equivalents	**$ 1,247,593**	**$ 159,630**	**$ –**	**$ 1,407,223**	$ 1,946,718
Accounts receivable:					
Tuition – less allowance of $8,528	**1,496**	–	–	**1,496**	14,417
Pledges – less allowance of $19,000	**19,990**	**708,709**	**324**	**729,023**	44,627
Other – less allowance of $2,034	**55,911**	**368,943**	–	**424,854**	451,857
Student notes – less allowance of $329,781	**1,849,864**	–	–	**1,849,864**	1,897,513
Inventories	**138,445**	–	–	**138,445**	139,226
Deposits and prepaids	**152,908**	–	–	**152,908**	66,954
Bond financing costs	**103,765**	–	–	**103,765**	94,811
Investments:					
Board-designated and restricted funds	**27,175,545**	**–**	**19,911,153**	**47,086,698**	49,406,237
Charitable perpetual trusts	–	–	**4,887,371**	**4,887,371**	4,798,853
Land, buildings, and equipment – net	**29,644,151**	–	–	**29,644,151**	30,753,347
Total assets	**$ 60,389,668**	**$ 1,237,282**	**$ 24,798,848**	**$ 86,425,798**	$ 89,614,560
Liabilities and net assets					
Liabilities:					
Accounts payable and other liabilities	**$ 229,298**	**$ –**	**$ –**	**$ 229,298**	$ 205,541
Accrued salaries and related payroll taxes	**249,418**	**–**	**–**	**249,418**	224,690
Tuition and fees paid in advance	**224,373**	**–**	**–**	**224,373**	188,066
Split interest agreements payable	**150,950**	**–**	**–**	**150,950**	186,801
Bonds payable	**15,125,000**	**–**	**–**	**15,125,000**	15,950,000
Note payable	**128,117**	**–**	**–**	**128,117**	188,015
U.S. government grants refundable	**1,480,161**	**–**	**–**	**1,480,161**	1,503,450
Total liabilities	**17,587,317**	**–**	**–**	**17,587,317**	18,446,563
Net assets:					
Unrestricted	**42,802,351**	**–**	**–**	**42,802,351**	46,679,866
Temporarily restricted	–	**1,237,282**	**–**	**1,237,282**	524,254
Permanently restricted	–	**–**	**24,798,848**	**24,798,848**	23,963,877
Total net assets	**42,802,351**	**1,237,282**	**24,798,848**	**68,838,481**	71,167,997
Total liabilities and net assets	**$ 60,389,668**	**$ 1,237,282**	**$ 24,798,848**	**$ 86,425,798**	$ 89,614,560

See accompanying notes.

Cleveland Institute of Music

Statement of Financial Position

June 30, 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Assets				
Cash and cash equivalents	$ 1,802,202	$ 144,516	$ –	$ 1,946,718
Accounts receivable:				
Tuition – less allowance of $7,566	14,417	–	–	14,417
Pledges – less allowance of $3,000	33,832	10,795	–	44,627
Other – less allowance of $2,034	82,914	368,943	–	451,857
Student notes – less allowance of $286,512	1,897,513	–	–	1,897,513
Inventories	139,226	–	–	139,226
Deposits and prepaids	66,954	–	–	66,954
Bond financing costs	94,811	–	–	94,811
Investments:				
Board-designated and restricted funds	30,241,213	–	19,165,024	49,406,237
Charitable perpetual trusts	–	–	4,798,853	4,798,853
Land, buildings, and equipment – net	30,753,347	–	–	30,753,347
Total assets	$ 65,126,429	$ 524,254	$ 23,963,877	$ 89,614,560
Liabilities and net assets				
Liabilities:				
Accounts payable and other liabilities	$ 205,541	$ –	$ –	$ 205,541
Accrued salaries and related payroll taxes	224,690	–	–	224,690
Tuition and fees paid in advance	188,066	–	–	188,066
Split interest agreements payable	186,801	–	–	186,801
Bonds payable	15,950,000	–	–	15,950,000
Note payable	188,015	–	–	188,015
U.S. government grants refundable	1,503,450	–	–	1,503,450
Total liabilities	18,446,563	–	–	18,446,563
Net assets:				
Unrestricted	46,679,866	–	–	46,679,866
Temporarily restricted	–	524,254	–	524,254
Permanently restricted	–	–	23,963,877	23,963,877
Total net assets	46,679,866	524,254	23,963,877	71,167,997
Total liabilities and net assets	$ 65,126,429	$ 524,254	$ 23,963,877	$ 89,614,560

See accompanying notes.

Cleveland Institute of Music

Statements of Activities

Year Ended June 30, 2016 With Comparative Totals for June 30, 2015

				Year Ended June 30	
		Temporarily	Permanently	2016	2015
	Unrestricted	Restricted	Restricted	Total	Total
Revenues, gains, and support					
Gross tuition and fees	**$ 22,849,886**	$ –	$ –	**$ 22,849,886**	$ 22,941,859
Less financial aid and tuition discount	**11,364,818**	–	–	**11,364,818**	10,847,990
Net tuition and fees	**11,485,068**	**–**	**–**	**11,485,068**	12,093,869
Contributions	**3,179,799**	**848,707**	**746,453**	**4,774,959**	2,701,048
Contributions of fixed assets	**26,180**	–	–	**26,180**	31,097
Investment income	**1,035,718**	–	–	**1,035,718**	927,602
Net realized and unrealized (losses) gains	**(1,621,358)**	**–**	–	**(1,621,358)**	910,924
Government assistance	**511,345**	**368,943**	–	**880,288**	864,909
Sales and services:					
Auxiliary enterprises	**988,219**	–	–	**988,219**	985,896
Educational activities	**146,055**	–	–	**146,055**	339,550
Other income	**189,344**	**7,766**	–	**197,110**	133,774
Net assets released from restrictions	**512,388**	**(512,388)**	–	**–**	–
Total revenues, gains, and support	**16,452,758**	**713,028**	**746,453**	**17,912,239**	18,988,669
Expenses and other deductions					
Educational and general:					
Instruction	**11,361,613**	–	–	**11,361,613**	11,362,224
Academic support	**1,679,860**	–	–	**1,679,860**	1,556,502
Student services	**711,225**	–	–	**711,225**	697,420
Auxiliary enterprises	**598,081**	–	–	**598,081**	590,297
Total educational and general	**14,350,779**	**–**	**–**	**14,350,779**	14,206,443
Institutional support	**5,979,494**	–	–	**5,979,494**	5,413,173
Total expenses and other deductions	**20,330,273**	**–**	**–**	**20,330,273**	19,619,616
Change in charitable perpetual trust	**–**	**–**	**88,518**	**88,518**	(342,236)
Net (decrease) increase in net assets	**(3,877,515)**	**713,028**	**834,971**	**(2,329,516)**	(973,183)
Net assets at beginning of year	**46,679,866**	**524,254**	**23,963,877**	**71,167,997**	72,141,180
Net assets at end of year	**$ 42,802,351**	**$ 1,237,282**	**$ 24,798,848**	**$ 68,838,481**	$ 71,167,997

See accompanying notes.

Cleveland Institute of Music

Statement of Activities

Year Ended June 30, 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains, and support				
Gross tuition and fees	$ 22,941,859	$ –	$ –	$ 22,941,859
Less financial aid and tuition discount	10,847,990	–	–	10,847,990
Net tuition and fees	12,093,869	–	–	12,093,869
Contributions	1,791,886	126,020	783,142	2,701,048
Contributions of fixed assets	31,097	–	–	31,097
Investment income	927,602	–	–	927,602
Net realized and unrealized gains	910,924	–	–	910,924
Government assistance	495,966	368,943	–	864,909
Sales and services:				
Auxiliary enterprises	985,896	–	–	985,896
Educational activities	339,550	–	–	339,550
Other income	133,774	–	–	133,774
Net assets released from restrictions	569,923	(569,923)	–	–
Total revenues, gains, and support	18,280,487	(74,960)	783,142	18,988,669
Expenses and other deductions				
Educational and general:				
Instruction	11,362,224	–	–	11,362,224
Academic support	1,556,502	–	–	1,556,502
Student services	697,420	–	–	697,420
Auxiliary enterprises	590,297	–	–	590,297
Total educational and general	14,206,443	–	–	14,206,443
Institutional support	5,413,173	–	–	5,413,173
Total expenses and other deductions	19,619,616	–	–	19,619,616
Change in charitable perpetual trust	–	–	(342,236)	(342,236)
Net (decrease) increase in net assets	(1,339,129)	(74,960)	440,906	(973,183)
Net assets at beginning of year	48,018,995	599,214	23,522,971	72,141,180
Net assets at end of year	$ 46,679,866	$ 524,254	$ 23,963,877	$ 71,167,997

See accompanying notes.

Cleveland Institute of Music

Statements of Cash Flows

	Year Ended June 30	
	2016	**2015**
Operating activities		
Decrease in net assets	**$ (2,329,516)**	$ (973,183)
Adjustments to reconcile decrease in net assets to net cash provided by operating activities:		
Change in charitable perpetual trust	**(88,518)**	342,236
Net unrealized losses	**2,731,452**	746,122
Depreciation and amortization	**1,616,713**	1,582,093
Write-off of deferred financing costs	**92,148**	–
Contributions of fixed assets	**(26,180)**	(31,097)
Restricted contributions for long-term purposes	**(746,453)**	(783,142)
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable	**(596,823)**	132,132
Decrease (increase) in inventories	**781**	(2,646)
(Increase) decrease in deposits and prepaids	**(85,954)**	22,414
Decrease in accounts payable and other liabilities	**(35,383)**	(24,950)
Increase in accrued salaries and related payroll taxes	**24,728**	17,081
Increase in tuition and fees paid in advance	**36,307**	18,734
Net cash provided by operating activities	**593,302**	1,045,794
Investing activities		
Purchase of investments	**(17,588,181)**	(26,539,213)
Proceeds from sale of investments	**17,176,268**	25,991,613
Purchase of land, buildings, and equipment	**(472,245)**	(207,850)
Net cash used in investing activities	**(884,158)**	(755,450)
Financing activities		
Restricted contributions for long-term purposes	**746,453**	783,142
Principal payments on bonds payable	**(825,000)**	(795,000)
Proceeds from issuance of bonds	**15,540,000**	–
Repayments on bonds	**(15,540,000)**	–
Bond financing costs	**(110,194)**	–
Principal payments on note payable	**(59,898)**	(57,275)
Net cash used in financing activities	**(248,639)**	(69,133)
Net (decrease) increase in cash and cash equivalents	**(539,495)**	221,211
Cash and cash equivalents at beginning of year	**1,946,718**	1,725,507
Cash and cash equivalents at end of year	**$ 1,407,223**	$ 1,946,718

See accompanying notes.

1. Significant Accounting Policies

Nature of Organization

The mission of Cleveland Institute of Music (the Institute) is to be a leading international conservatory that is distinguished by an exceptional degree of collaboration between students and teachers. This same stimulating environment extends to the Institute’s community education programs, which help people of all ages realize their musical potential. The Institute is a not-for-profit corporation located in Cleveland, Ohio, operating under the laws of the state of Ohio and is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

Accrual Basis

The financial statements of the Institute are prepared on the accrual basis in accordance with U.S. generally accepted accounting principles.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported and disclosures in the financial statements. Actual results could differ from those estimates.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are used to differentiate resources, the use of which is restricted by donors or grantors to a specific time period or purpose, from resources on which no restrictions have been placed, or that arise from the general operations of the Institute. Temporarily restricted gifts, grants, and bequests are recorded as an addition to temporarily restricted net assets in the period received. Resources restricted by donors or grantors for specific operating purposes are reported in unrestricted revenues, gains, and other support to the extent expended within the same period. Earnings on investments of temporarily restricted net assets, including investment income, realized, and unrealized appreciation and depreciation on temporarily restricted net assets, are included in other unrestricted revenues, gains, and support unless restricted by donors.

1. Significant Accounting Policies (continued)

Permanently restricted net assets consist of amounts held in perpetuity as designated by the donors. Investment income and net appreciation (depreciation) on investments of permanently restricted net assets are included in temporarily restricted revenues, gains, and support until board appropriation. In those cases where a donor has placed specific restrictions on the use of income, any related net appreciation is also subject to the same restriction and is reported as a part of temporarily restricted net assets until such time as the restriction has been met.

Contributions of land, buildings, and equipment without donor stipulations concerning the use of such long-lived assets are reported as revenues in unrestricted net assets when received. Contributions of cash or other assets to be used to acquire land, building, and equipment with donor stipulations are reported as revenues in temporarily restricted net assets when received. The restrictions are considered to be released at the time of acquisition of such long-lived assets.

Tuition and Fees Revenue and Tuition and Fees Paid in Advance

Tuition and fees revenue is recognized at the beginning of each session based on approved fees. Tuition and fees paid in advance represent payments received related to summer and fall sessions. The summer session is conducted over two different fiscal years and is recognized in the fiscal year in which the session is predominantly conducted.

Auxiliary Enterprises Revenue

Auxiliary enterprises revenue primarily represents revenue generated by dormitory rentals and bookstore sales. Revenue received from dormitory rental arrangements is recognized ratably over the lease term.

Financial Aid and Tuition Discounts

Financial aid and tuition discounts represent the portion of aid provided to the student in the form of reduced tuition. Certain aid such as loans, funds provided to students as awarded by third parties, Federal Direct Lending, Pell, and state grants is accounted for as a third-party payment and not included in the financial aid and tuition discount line on the accompanying statements of activities.

1. Significant Accounting Policies (continued)

Contributed Services

No amounts have been reflected in the financial statements for contributed services. The Institute pays for most services requiring specific expertise. However, many individuals volunteer their time and perform a variety of tasks that assist the Institute. These volunteers include the members of the Board of Trustees and other committees of the Institute.

Cash and Cash Equivalents

Cash and cash equivalents include investments in highly liquid debt instruments with a maturity when purchased of three months or less. Cash and cash equivalents are stated at cost, which approximates fair value and excludes amounts board designated or restricted.

Pledges Receivable

Pledges receivable represent unconditional promises of donors to give cash and other assets which are recognized by the Institute at net present value in the period the promise is made. Conditional promises to give are recognized when the conditions are met.

Student Notes Receivable

Student notes receivable consist primarily of loans made to students under a United States government loan program.

Inventories

Inventories of books and supplies are carried at the lower of cost (first-in-first-out method) or net realizable value.

Bond Financing Costs

The costs related to the issuance of bonds are capitalized and amortized over the period the obligation is outstanding using the bonds outstanding method.

1. Significant Accounting Policies (continued)

Investments and Investment Income

Investments in equity securities with readily determinable market values and all investments in debt securities are measured at fair value.

Alternative investments include hedge funds, hedged fund of funds, and private equity funds (collectively, alternative funds) and are measured at fair value.

Investment income or loss (including interest and dividends) and net realized and unrealized gains and losses are reflected in the accompanying statements of activities. Realized investment gains or losses are determined by comparison of the carrying value to net proceeds received on the settlement date. Unrealized gains or losses are determined by the differences between carrying value and fair value. These amounts are reported in the accompanying statements of activities as net realized and unrealized gains.

Land, Buildings, and Equipment

Land, buildings, and equipment are recorded at cost or fair value at the date of donation. The costs of repairs and maintenance are expensed as incurred. Depreciation is recorded using the straight-line method for buildings and equipment over their estimated useful lives of 30 years and 5 to 40 years, respectively.

Split Interest Agreements

The Institute is an income beneficiary of several charitable perpetual trusts. The Institute records its interest in charitable perpetual trusts, which is included in investments on the accompanying statements of financial position, at its pro rata share of the fair value of the perpetual trust assets. Because the assets of the trusts are not controlled by the Institute, they are recorded as permanently restricted net assets. Income distributed to the Institute by the trusts of $257,489 and $266,408 in 2016 and 2015, respectively, was recorded as unrestricted investment income on the accompanying statements of activities.

The Institute has entered into charitable gift annuity agreements, which include provisions requiring the Institute to pay periodic fixed payments to beneficiaries during their lifetimes. The obligation is reflected as split interest agreements payable on the accompanying statements of financial position. Charitable gift annuities differ from other charitable giving options in that the annuity is a general obligation of the Institute. Accordingly, if the assets of the gift are exhausted as a result of required payments to beneficiaries, unrestricted assets of the Institute will be utilized to fund future payments.

1. Significant Accounting Policies (continued)

Recent Accounting Pronouncement

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers*, which outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance, and requires significantly expanded disclosures about revenue recognition. The core principle of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance is effective for the Institute for reporting periods beginning after December 15, 2017. The Institute is currently evaluating the impact on the financial statements and the options of adopting using either a full retrospective or a modified approach.

In April 2015, the FASB issued ASU 2015-03, *Imputation of Interest*, *Simplifying the Presentation of Debt Issuance Costs*. This ASU requires debt issuance costs to be presented in the balance sheet as a direct deduction from the associated debt liability, consistent with the presentation of a debt discount. This amends current guidance that requires debt issuance costs to be presented as assets on the balance sheet. ASU 2015-03 is effective for the Institute for reporting periods beginning after December 15, 2015 with early adoption permitted. Upon adoption, the Institute is required to apply the new guidance retrospectively to all periods presented in the financial statements. The Institute has $104,000 and $95,000 of debt issuance costs at June 30, 2016 and 2015, respectively, which would be reclassified under the new guidance. The Institute will adopt the provisions of ASU 2015-03 upon the effective date.

In February 2016, the FASB issued ASU 2016-02, *Leases*. This ASU requires lessees to recognize assets and liabilities on the balance sheet for leases with lease terms greater than 12 months. The recognition, measurement and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a finance or operating lease. This amends current guidance that requires only capital leases to be recognized on the lessee balance sheet. ASU 2016-02 will also require additional disclosures on the amount, timing and uncertainty of cash flows arising from leases. The guidance is effective for the Institute for reporting periods beginning after December 15, 2018 with early adoption permitted. The Institute is currently evaluating the impact that ASU 2016-02 will have on its financial statements and will adopt the provisions upon the effective date.

1. Significant Accounting Policies (continued)

In August 2016, the FASB issued ASU 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. This standard intends to make certain improvements to the current reporting requirements for not-for-profit entities including; (1) the presentation for two classes of net assets at the end of the period, rather than the currently required three classes, as well as the annual change in each of the two classes; (2) the removal of the requirement to present or disclose the indirect method (reconciliation) when using the direct method for the statement of cash flows; and (3) the requirement to provide various enhanced disclosures relating to various not-for-profit specific topics. The new standard is effective for annual financial statements beginning after December 15, 2017. The Institute is currently evaluating the impact that ASU 2016-02 will have on its financial statements and will adopt the provisions upon the effective date.

2. Pledges Receivable and Contributions

Pledges receivable are recorded net of an allowance for uncollectible pledges of $19,000 and $3,000 as of June 30, 2016 and 2015, respectively. Pledges are restricted by donors for scholarships, expansion of facilities, and general operating support purposes, and are due as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
2016				
Less than one year	**$ 19,990**	**$ –**	**$ 324**	**$ 20,314**
One to five years	**–**	**708,709**	**–**	**708,709**
	$ 19,990	**$ 708,709**	**$ 324**	**$ 729,023**
2015				
Less than one year	$ 33,832	$ –	$ –	$ 33,832
One to five years	–	10,795	–	10,795
	$ 33,832	$ 10,795	$ –	$ 44,627

Pledges receivable, net are comprised of the following categories:

	2016	2015
Annual fund	**$ 728,699**	$ 44,627
Endowment	**324**	–
	$ 729,023	$ 44,627

2. Pledges Receivable and Contributions (continued)

The composition of contributions on the accompanying statements of activities for the years ended June 30 is as follows:

	2016	2015
Annual fund and other operating	**$ 3,778,506**	$ 1,392,906
Endowment	**746,453**	783,142
Bequests	**250,000**	525,000
	$ 4,774,959	$ 2,701,048

The Institute has $2,431,902 and $4,206,902 of deferred gifts with various conditions that are not recorded as of June 30, 2016 and 2015, respectively.

3. Investments

The composition of investments is as follows:

	June 30	
	2016	**2015**
Cash and cash equivalents	**$ 18,119**	$ 443,937
Money markets	**612,218**	2,589,305
Fixed income securities:		
U.S. government agencies	–	78,002
U.S. corporate fixed income	**90,052**	199,353
Common and preferred stocks:		
International	**713,237**	1,232,788
Mutual funds:		
U.S. corporate fixed income	**6,452,498**	6,513,122
U.S. common and preferred stock	**22,173,122**	20,158,118
International common and preferred stock	**4,140,227**	5,413,133
Alternative investments:		
Hedge funds	**9,286,347**	9,211,587
Private equity and other	**3,600,878**	3,566,892
Charitable perpetual trusts	**4,887,371**	4,798,853
	$ 51,974,069	$ 54,205,090

3. Investments (continued)

The fair value of investments is allocated as of June 30, 2016 and 2015, as follows: $36,440,042 and $38,728,399, respectively, for endowment and board-designated endowments; $982,740 and $1,239,972, respectively, for board-designated funds; $9,573,864 and $9,160,511, respectively, for the Expansion Project (expansion of facilities which included the addition of a concert hall, practice studios, teaching studios, classrooms, and offices); $90,052 and $277,355, respectively, for operations; and $4,887,371 and $4,798,853, respectively, related to charitable perpetual trusts.

The Institute invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the accompanying statements of financial position.

Alternative investments represent investments in separate accounts, and commingled vehicles some of which employ traditional strategies (long only) in readily marketable securities (liquid equities or bonds) and others of which employ less traditional strategies (long and short equity or fixed income, event driven, macro, relative value, and arbitrage strategies) that may include the use of options, futures, and other derivative instruments.

At June 30, 2016, the Institute's alternative investments are subject to various liquidity restrictions as follows:

Available for redemption:	
Monthly	$ 946,708
Quarterly	4,089,620
Semiannual	2,026,355
Annually	2,223,664
	9,286,347
Subject to distribution and lock-up provisions	3,600,878
Total alternative investments	$ 12,887,225

3. Investments (continued)

Investments that are available for redemption may be redeemed by the Institute generally with 30- to 60-day advance notice on a monthly, quarterly, semiannual, or annual basis subject to the terms of the investment agreement.

Investments subject to distribution cannot be redeemed by the Institute but rather will be distributed by the fund upon the liquidation of the underlying assets of the fund or limited partnership. Distributions are generally expected (but not guaranteed) over the next 12 years.

At June 30, 2016, the Institute is committed to invest an additional $2,424,319 in its current alternative investments over the next six years.

Total investment return is comprised of the following for the years ended June 30, 2016 and 2015:

	2016	2015
Interest income and dividends	**$ 1,035,718**	$ 927,602
Net realized gains on sales of investments	**1,110,094**	1,657,046
Net unrealized losses on investments	**(2,731,452)**	(746,122)
Net unrealized gains on charitable perpetual trusts	**88,518**	(342,236)
Total investment return	**$ (497,122)**	$ 1,496,290

4. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 – Inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

- Level 2 – Inputs to the valuation methodology include quoted prices for similar assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

- Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement. The inputs into the determination of fair value require significant management judgment or estimation.

To measure fair value, a hierarchy has been established that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs. As such, the hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets and liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

The carrying value of cash and cash equivalents, accounts receivable, inventories, deposits and prepaid, accounts payable, accrued salaries, and tuition and fees paid in advance reported in the accompanying statements of financial position represents a reasonable estimate of fair value due to their short-term nature. Student notes receivable are subject to significant restrictions with respect to interest rates and repayment terms. Accordingly, it is not practicable to measure the fair values of these notes. Investments are recorded at their fair value. The carrying value of the bonds payable is a reasonable estimate of its fair value as the interest rate on the bonds is variable. Bonds payable would be classified as Level 2 in the fair value hierarchy.

4. Fair Value Measurements (continued)

The following tables present the financial instruments carried at fair value on a recurring basis as of June 30, respectively, in accordance with the valuation hierarchy defined above:

	June 30, 2016			
	Total	**Level 1**	**Level 2**	**Level 3**
Cash and cash equivalents	**$ 18,119**	**$ 18,119**	**$ –**	**$ –**
Money markets	**612,218**	**612,218**	**–**	**–**
Fixed income securities:				
U.S. corporate fixed income	**90,052**	**90,052**	**–**	**–**
Common and preferred stocks:				
International	**713,237**	**713,237**	**–**	**–**
Mutual funds:				
U.S. corporate fixed income	**6,452,498**	**6,452,498**	**–**	**–**
U.S. common and preferred stocks	**22,173,122**	**22,173,122**	**–**	**–**
International common and preferred stocks	**4,140,227**	**4,140,227**	**–**	**–**
Alternative investments:				
Hedge funds*	**9,286,347**[(a)]	**–**	**–**	**–**
Private equity and other*	**3,600,878**[(b)]	**–**	**–**	**–**
Charitable perpetual trust	**4,887,371**	**–**	**–**	**4,887,371**[(c)]
Total assets at fair value	**$ 51,974,069**	**$ 34,199,473**	**$ –**	**$ 4,887,371**

4. Fair Value Measurements (continued)

	June 30, 2015			
	Total	Level 1	Level 2	Level 3
Cash and cash equivalents	$ 443,937	$ 443,937	$ –	$ –
Money markets	2,589,305	–	2,589,305	–
Fixed income securities:				
U.S. government agencies	78,002	–	78,002	–
U.S. corporate fixed income	199,353	199,353	–	–
Common and preferred stocks:				
International	1,232,788	1,232,788	–	–
Mutual funds:				
U.S. corporate fixed income	6,513,122	6,513,122	–	–
U.S. common and preferred stocks	20,158,118	20,158,118	–	–
International common and preferred stocks	5,413,133	5,413,133	–	–
Alternative investments:				
Hedge funds*	9,211,587[a]	–	–	–
Private equity and other*	3,566,892[b]	–	–	–
Charitable perpetual trust	4,798,853	–	–	4,798,853[c]
Total assets at fair value	$ 54,205,090	$ 33,960,451	$ 2,667,307	$ 4,798,853

* In accordance with ASC 820-10, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statements of financial position.

[a] The investment objective of this class of hedged funds is to reduce volatility and risk in the portfolio while preserving capital and delivering positive returns under all market conditions.

[b] The investment objective of this class of funds seeks long-term capital appreciation and superior risk-adjusted net returns through private equity investments.

[c] This investment represents charitable perpetual trusts held by others in which the Institute is a partial beneficiary. The investment portfolio includes domestic common stocks, corporate bonds, mutual funds, and money market funds designed to achieve high total returns through capital appreciation and dividend income.

4. Fair Value Measurements (continued)

The Institute's Investment Committee is responsible for determining the valuation policies and analyzing information provided by the investment custodians and issuers that is used to determine the fair value of investments.

The following is a description of the Institute's valuation methodologies for assets measured at fair value.

Money markets – valued at daily closing price as reported by the fund. These funds are required to publish their daily net asset value and to transact at that price. Additionally, these money market funds are deemed to be actively traded.

U.S. corporate fixed income securities and common and preferred stocks – valued based upon quoted market prices. Investments in securities traded on a national securities exchange are valued at the last reported sales price each day as reported by a recognized pricing service. Securities traded in the over-the-counter market and listed securities, for which no sale was reported on that date, are valued at fair value, based on the mean of the most recent bid and ask price and other market information available.

Mutual funds – valued at daily closing price as reported by the fund. Mutual funds are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily NAV and to transact at that price. Closed-end mutual funds trade at the market price throughout the day. These mutual funds are deemed to be actively traded.

Alternative investments – valued based on inputs which reflect the Institute's own assumptions about the valuation that are significant to the fair value measurement market participants would use in pricing the asset and include the best information available. The transaction price is initially used as the best estimate of fair value. This valuation is adjusted when changes to inputs and assumptions are corroborated by evidence. The Institute has implemented a process in which the valuation of each alternative investment is supported by the collection and review of the latest available audited financial statements of the alternative investment. The Institute utilizes NAV, or its equivalent, as a practical expedient to determine fair value for alternative investments. Because alternative investments are not readily marketable, their estimated fair value is subject to uncertainty and therefore may differ from the value that would have been used had a ready market for such investments existed. Such differences could be material.

4. Fair Value Measurements (continued)

Charitable perpetual trusts – valued based on the Institute's beneficial interest in the investments held in the trust, which is measured at fair value. Since the Institute has no right to the underlying investments, the trusts have been classified as Level 3.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Institute believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

The following table presents the changes in investments measured at fair value as of June 30, 2016, within Level 3 of the fair value hierarchy. This classification is based upon the use of significant unobservable inputs to the overall fair value measurement.

	Charitable Perpetual Trust
Balance as of June 30, 2014	$ 5,141,089
Unrealized losses related to instruments still held at the reporting date	(342,236)
Balance as of June 30, 2015	4,798,853
Unrealized gains related to instruments still held at the reporting date	**88,518**
Balance as of June 30, 2016	**$ 4,887,371**

5. Land, Buildings, and Equipment

The following is a summary of land, buildings, and equipment:

	June 30	
	2016	**2015**
Land and improvements	**$ 1,818,406**	$ 1,818,406
Buildings	**39,074,618**	39,074,618
Leasehold improvements	**592,769**	592,769
Musical instruments	**2,660,197**	2,571,733
Library books	**1,206,371**	1,167,687
Equipment	**2,102,799**	1,825,531
Furniture and fixtures	**719,010**	712,369
Automobile	**23,860**	23,860
	48,198,030	47,786,973
Less accumulated depreciation	**18,803,477**	17,211,748
	29,394,553	30,575,225
Artwork and collections	**79,978**	74,978
Construction-in-progress	**169,620**	103,144
Land, buildings, and equipment – net	**$ 29,644,151**	$ 30,753,347

6. Bonds Payable

In December 2010, pursuant to certain agreements between the Institute and the Ohio Higher Educational Facility Commission (the Commission), the Institute issued $19,320,000 of tax-exempt State of Ohio Higher Educational Facility Variable Rate Bonds (Series 2010 Bonds). The proceeds from the Series 2010 Bonds were used to refinance the Series 2005 Bonds. The variable interest rate is equal to 65.01% of the one-month London Interbank Offered Rate plus 2.75% not to exceed the maximum rate of 10%. In connection with the issuance of the Series 2010 Bonds, the Institute entered into a Guaranty Agreement with U.S. Bank National Association. In addition, the Institute entered into a Bond Purchase Agreement under a private placement bond with PNC Bank, National Association ($9,660,000) and Key Bank ($9,660,000) which had an initial term of five years, through December 2015.

On November 30, 2015, the Institute refinanced the Series 2010 Bonds and issued $15,540,000 of tax-exempt State of Ohio Higher Educational Facility Variable Rate Bonds (Series 2015 Bonds). The proceeds from the Series 2015 Bonds were used to refinance the Series 2010 Bonds.

6. Bonds Payable (continued)

Additionally, as a result of the refinancing, the Institute incurred a loss due to the write-off of bond financing costs of $92,000 which is included in institutional support on the statement of activities.

The variable interest rate is equal to 65.01% of the one-month London Interbank Offered Rate plus 2%. In connection with the issuance of the Series 2015 Bonds, the Institute entered into a Bond Purchase Agreement under a private placement bond with FirstMerit Bank N.A. recently acquired by Huntington National Bank which has an initial term of ten years, through November 2025. Bond debt service for the Series 2015 Bonds is calculated over 15 years with semiannual payments each May and November. The Institute is required to make specified deposits with the Trustee (U.S. Bank National Association) to fund principal and interest payments due and continues to be subject to certain restrictive covenants, including provisions relating to certain debt ratios and other matters. The Series 2015 Bonds are secured by the Institute’s unrestricted gross revenues. From July 1, 2015 to November 30, 2016, the Institute’s variable interest rate ranged from 1.91% to 1.92% for the Series 2010 Bonds. From December 1, 2015 to June 30, 2016, the variable interest rate ranged from 1.45% to 1.60% for the Series 2015 Bonds.

Annual principal payments on long-term obligations for the five-year period beginning in 2016 are as follows: 2017 – $855,000; 2018 –$885,000; 2019 – $915,000: 2020 – $945,000; 2021 – $980,000; and thereafter – $10,545,000.

The Institute did not capitalize interest in 2016 and 2015. Interest paid was $272,509 and $315,446 in 2016 and 2015, respectively.

7. Operating Leases

The Institute entered into an operating lease agreement with Case Western University (the University) on July 1, 1987, to lease a building to be used as a dormitory. The Institute signed an amendment to the original lease agreement on November 25, 2008, which extends the term of the lease for ten years until June 30, 2018, with the option to renew for one additional five-year period. Rent for the 2015–2016 academic year was $201,270 and will increase annually by one-half of the rate of increase of the University double-room rate.

7. Operating Leases (continued)

The University completed certain leasehold improvements and renovations of the building. Upon completion of the improvements, the Institute recorded a note payable to the University of $540,000 for the cost of the improvements. The interest on the note is 4.5% per annum. The note will be repaid in 40 consecutive equal quarterly installments starting September 30, 2009, of $16,839, which includes both principal and interest. The note payable balance at June 30, 2016, is $128,117. Interest paid on the note payable was $7,459 and $10,081 in 2016 and 2015, respectively.

The Institute has various operating lease agreements for buildings and equipment. Future minimum payments under these leases with initial or remaining terms of one year or more consisted of the following at June 30, 2016:

	Operating Leases
2017	$ 311,446
2018	281,284
2019	79,446
2020	61,199
2021	57,537
Total minimum lease payments	$ 790,912

Rent expense was $472,200 and $468,422 for 2016 and 2015, respectively.

8. Retirement Plan

The Institute sponsors a defined contribution plan through Teachers Insurance and Annuity Association/College Retirement Equities Fund (TIAA/CREF), a national organization used to fund retirement benefits for educational institutions. This plan is available to all eligible employees who, at their discretion, may invest from 1% to 4% of their base salary with TIAA/CREF. The Institute matches the employee contribution on a two-for-one basis up to 8% of base salary. The Institute contributed $465,744 and $456,269 in 2016 and 2015, respectively, which is recorded as an expense in the accompanying statements of activities.

9. Nature of Temporarily Restricted Net Assets

Temporarily restricted net assets are available for the following purposes:

	June 30 2016	June 30 2015
Scholarship support	**$ 42,725**	$ 91,569
Institutional support	**786,982**	32,876
Special projects	**407,575**	399,809
	$ 1,237,282	$ 524,254

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purpose or by occurrence of events specified by the donors or by the change of restriction specified by the donors. In 2016 and 2015, the Institute released temporarily restricted net assets as follows:

	2016	2015
Scholarship support	**$ 86,569**	$ 87,676
Institutional support	**31,876**	57,217
Special projects	**393,943**	383,385
Expansion project	**–**	41,645
	$ 512,388	$ 569,923

10. Nature of Permanently Restricted Net Assets

Permanently restricted net assets are amounts held in perpetuity, the income from which is expendable for the following purposes:

	June 30 2016	June 30 2015
Scholarship support	**$ 9,857,265**	$ 9,420,663
Institutional support	**11,259,036**	10,828,516
Faculty support	**3,328,915**	3,365,041
Instructional support	**353,632**	349,657
	$ 24,798,848	$ 23,963,877

11. Endowment

The Institute's endowment consists of 195 individual donor-restricted funds established for a variety of purposes. Net assets associated with endowment funds are classified and reported based on donor-imposed restrictions.

Interpretation of Relevant Law

Effective June 1, 2009, Ohio's version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) became law. The Institute's Board of Trustees has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Institute classifies as permanently restricted net assets (1) the original value of gifts donated to the permanent endowment, (2) the original value of subsequent gifts to the permanent endowment, and (3) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Institute in a manner consistent with the standard for expenditure prescribed by UPMIFA. In accordance with UPMIFA, the Institute considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund.
2. The purposes of the donor-restricted endowment fund.
3. General economic conditions.
4. The possible effect of inflation and deflation.
5. The expected total return from income and the appreciation of investments.
6. Other resources of the Institute.
7. The investment policies of the Institute.

11. Endowment (continued)

Funds With Deficiencies

From time-to-time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Institute to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were $153,168 and $5,860 as of June 30, 2016 and 2015, respectively.

Return Objectives and Risk Parameters

The Institute has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity. Under this policy, the endowment assets are invested in a manner that is intended to produce results that equal or exceed a broad mix of financial market indices. The Institute expects its endowment funds, over time, to provide an average rate of return of 5% above the rate of inflation as defined by the Consumer Price Index annually. Actual returns in any given year may, and have, varied from this amount.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the Institute relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Institute targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

Distributions from endowments are based on a spending policy set by the Institute’s Board of Trustees. Under this spending policy, appropriated income is calculated at 5.90% for 2016 and 5.95% for 2015, of the average market value of endowment investments for the prior three years. In establishing this policy, the Institute considered the long-term expected return on its endowment. Accordingly, over the long term, the Institute expects the current spending policy to allow its endowment to grow at an average of 8% annually. This is consistent with the Institute’s

11. Endowment (continued)

objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return. Unappropriated earnings by the Board of Trustees are recorded as temporarily restricted net assets.

Endowment Net Asset Composition by Type of Fund at June 30

	2016			
	Unrestricted	**Temporarily Restricted**	**Permanently Restricted**	**Total**
Donor restricted	**$ (153,168)**	**$ –**	**$ 19,911,477**	**$ 19,758,309**
Charitable perpetual trust	**–**	**–**	**4,887,371**	**4,887,371**
Board designated	**17,460,369**	**–**	**–**	**17,460,369**
Total endowment	**$ 17,307,201**	**$ –**	**$ 24,798,848**	**$ 42,106,049**

	2015			
	Unrestricted	**Temporarily Restricted**	**Permanently Restricted**	**Total**
Donor restricted	$ (5,860)	$ –	$ 19,165,024	$ 19,159,164
Charitable perpetual trust	–	–	4,798,853	4,798,853
Board designated	20,403,382	–	–	20,403,382
Total endowment	$ 20,397,522	$ –	$ 23,963,877	$ 44,361,399

11. Endowment (continued)

Changes in Endowment Net Assets

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, June 30, 2014	$ 20,658,876	$ –	$ 23,522,971	$ 44,181,847
Investment income	524,357	–	–	524,357
Net depreciation	(625,276)	–	–	(625,276)
Change in charitable perpetual trust	–	–	(342,236)	(342,236)
Contributions	–	–	783,142	783,142
Appropriation of endowment assets for expenditure	(160,435)	–	–	(160,435)
Endowment net assets, June 30, 2015	20,397,522	–	23,963,877	44,361,399
Investment income	**646,502**	–	–	**646,502**
Net depreciation	**(3,469,881)**	–	–	**(3,469,881)**
Change in charitable perpetual trust	–	–	**88,518**	**88,518**
Contributions	–	–	**746,453**	**746,453**
Appropriation of endowment assets for expenditure	**(266,942)**	–	–	**(266,942)**
Endowment net assets, June 30, 2016	**$ 17,307,201**	**$** –	**$ 24,798,848**	**$ 42,106,049**

12. Subsequent Events

The Institute has evaluated and disclosed any subsequent events through December 6, 2016, which is the date the financial statements were issued and made available.