



Financial Statements

Naval War College Foundation, Inc.

December 31, 2019 and 2018



NAVAL WAR COLLEGE FOUNDATION, INC.

Financial Statements

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Mayer Hoffman McCann P.C.

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Independent Auditors' Report

The Board of Trustees
Naval War College Foundation, Inc.
Newport, Rhode Island

We have audited the accompanying financial statements of Naval War College Foundation, Inc. (the "Foundation"), which comprise the statements of financial position as of December 31, 2019 and 2018, 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 audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' 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.



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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Naval War College Foundation, Inc. as of December 31, 2019 and 2018, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As disclosed in Note 1 to the financial statements, during the year ended December 31, 2019, the Foundation adopted Accounting Standards Update (“ASU”) No. 2014-19, *Revenue from Contracts with Customers* and ASU No. 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. Our opinion is not modified with respect to these matters.

Mayer Hoffman McCann P.C.

June 8, 2020
Providence, Rhode Island

NAVAL WAR COLLEGE FOUNDATION, INC.

Statements of Financial Position

	<i>December 31,</i>	
	<i>2019</i>	<i>2018</i>
Assets		
Cash	\$ 367,151	\$ 461,336
Interest receivable	62,292	60,187
Contributions receivable, net	1,305,047	1,617,161
Life memberships receivable, net	19,835	19,325
Investments	47,245,775	31,799,830
Inventory	87,544	95,164
Prepaid expenses	3,136	34,762
Furniture and equipment, net	19,523	8,899
Vehicle, net	23,513	-
Historical collections	67,598	67,598
 Total assets	\$ 49,201,414	\$ 34,164,262
 Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses	\$ 350,558	\$ 126,700
Obligation under split-interest agreements	128,552	74,499
 Total liabilities	479,110	201,199
Net assets:		
Without donor restrictions	12,970,765	11,207,734
With donor restrictions	35,751,539	22,755,329
 Total net assets	48,722,304	33,963,063
 Total liabilities and net assets	\$ 49,201,414	\$ 34,164,262

NAVAL WAR COLLEGE FOUNDATION, INC.

Statement of Activities

Year Ended December 31, 2019
(with comparative totals for 2018)

	<i>Without Donor Restrictions</i>	<i>With Donor Restrictions</i>	<i>2019 Total</i>	<i>2018 Total</i>
Operating revenues:				
Contributions	\$ 1,398,369	\$ -	\$ 1,398,369	\$ 1,361,672
Corporate members	63,500	-	63,500	113,000
Individual members	91,651	-	91,651	113,765
Graduate members	22,611	-	22,611	33,740
Total support	1,576,131	-	1,576,131	1,622,177
Investment income (loss), net	1,969,316	-	1,969,316	(263,551)
Special events, gross	87,565	-	87,565	87,960
Museum store sales, net	37,860	-	37,860	32,677
Publication royalties	83	-	83	268
Endowment return utilized in operations	685,338	(685,338)	-	-
Net assets released from restriction	562,719	(562,719)	-	-
Total operating revenues	4,919,012	(1,248,057)	3,670,955	1,479,531
Operating expenses:				
Foundation grants	1,601,362	-	1,601,362	1,539,019
Program services	690,125	-	690,125	614,840
Management and resource development	861,692	-	861,692	862,374
Total operating expenses	3,153,179	-	3,153,179	3,016,233
Increase (decrease) in net assets from operations	1,765,833	(1,248,057)	517,776	(1,536,702)
Non-operating activities:				
Contributions	-	11,626,942	11,626,942	2,576,405
Investment income (loss), net	-	2,617,325	2,617,325	(318,608)
Change in value of split-interest agreements	(2,802)	-	(2,802)	(13,641)
Change in net assets from non-operating activities	(2,802)	14,244,267	14,241,465	2,244,156
Change in net assets	1,763,031	12,996,210	14,759,241	707,454
Net assets, beginning of year	11,207,734	22,755,329	33,963,063	33,255,609
Net assets, end of year	\$ 12,970,765	\$ 35,751,539	\$ 48,722,304	\$ 33,963,063

NAVAL WAR COLLEGE FOUNDATION, INC.

Statement of Activities

Year Ended December 31, 2018

	<i>Without Donor Restrictions</i>	<i>With Donor Restrictions</i>	<i>Total</i>
Operating revenues:			
Contributions	\$ 1,361,672	\$ -	\$ 1,361,672
Corporate members	113,000	-	113,000
Individual members	113,765	-	113,765
Graduate members	<u>33,740</u>	<u>-</u>	<u>33,740</u>
Total support	<u>1,622,177</u>	<u>-</u>	<u>1,622,177</u>
Investment loss, net	(263,551)	-	(263,551)
Special events, gross	87,960	-	87,960
Museum store sales, net	32,677	-	32,677
Publication royalties	268	-	268
Endowment return utilized in operations	374,732	(374,732)	-
Net assets released from restriction	<u>701,017</u>	<u>(701,017)</u>	<u>-</u>
Total operating revenues	<u>2,555,280</u>	<u>(1,075,749)</u>	<u>1,479,531</u>
Operating expenses:			
Foundation grants	1,539,019	-	1,539,019
Program services	614,840	-	614,840
Management and resource development	<u>862,374</u>	<u>-</u>	<u>862,374</u>
Total operating expenses	<u>3,016,233</u>	<u>-</u>	<u>3,016,233</u>
Decrease in net assets from operations	<u>(460,953)</u>	<u>(1,075,749)</u>	<u>(1,536,702)</u>
Non-operating activities:			
Contributions	-	2,576,405	2,576,405
Investment loss, net	-	(318,608)	(318,608)
Change in value of split-interest agreements	<u>(13,641)</u>	<u>-</u>	<u>(13,641)</u>
Change in net assets from non-operating activities	<u>(13,641)</u>	<u>2,257,797</u>	<u>2,244,156</u>
Change in net assets	<u>(474,594)</u>	<u>1,182,048</u>	<u>707,454</u>
Net assets, beginning of year	<u>11,682,328</u>	<u>21,573,281</u>	<u>33,255,609</u>
Net assets, end of year	<u>\$ 11,207,734</u>	<u>\$ 22,755,329</u>	<u>\$ 33,963,063</u>

NAVAL WAR COLLEGE FOUNDATION, INC.

Statements of Cash Flows

	<i>Years Ended December 31,</i>	
	<i>2019</i>	<i>2018</i>
Cash flows from operating activities:		
Changes in net assets	\$ 14,759,241	\$ 707,454
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation	3,884	2,823
Loss on disposal of furniture and equipment	1,482	1,683
Bad debt expense	100	8,150
Net realized and unrealized loss (gain) on investments	(3,721,437)	1,296,587
Change in contributions receivable discount	22,776	33,336
Contributions restricted for long-term investment	(11,626,942)	(2,576,405)
Changes in:		
Interest receivable	(2,105)	(11,455)
Contributions receivable	53,809	(299,699)
Life memberships receivable	(610)	(1,065)
Inventory	7,620	(1,147)
Prepaid expenses	31,626	(16,327)
Accounts payable and accrued expenses	223,858	51,881
Obligation under split-interest agreements	54,053	5,358
Total adjustments	(14,951,886)	(1,506,280)
Net cash used in operating activities	(192,645)	(798,826)
Cash flows from investing activities:		
Acquisition of vehicle, furniture and equipment	(39,503)	(2,760)
Purchase of investments	(14,929,078)	(6,350,715)
Proceeds from sale/maturities of investments	3,204,570	3,522,279
Net cash used in investing activities	(11,764,011)	(2,831,196)
Cash flows from financing activities:		
Proceeds restricted for long-term investment	11,862,471	2,025,607
Net cash provided by financing activities	11,862,471	2,025,607
Decrease in cash	(94,185)	(1,604,415)
Cash, beginning of year	461,336	2,065,751
Cash, end of year	\$ 367,151	\$ 461,336

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies

The Naval War College Foundation, Inc. (the “Foundation”), organized in 1969, is a charitable organization whose purpose is to provide a source of support to assist the Naval War College in carrying out its mission to enhance the professional capabilities of its students and conduct research in the development of advanced strategic and tactical concepts. The Internal Revenue Service has determined that the Foundation is a non-profit organization exempt from income taxes under Sections 501(c)(3) of the Internal Revenue Code.

Basis of Presentation

The financial statements of the Foundation have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the U.S. which requires that information regarding its financial position and activities are reported based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Foundation and changes therein are classified and reported as follows:

Net Assets Without Donor Restrictions

Net assets available for general use and not subject to donor-imposed restrictions. Included in net assets without donor restrictions at December 31, 2019 and 2018 are \$54,679 and \$50,199, respectively, of assets directed by the Board of Trustees to be segregated from the general operating assets and to be known as the Strasser Board Restricted Fund.

Net Assets With Donor Restrictions

Net assets subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature that may or will be met, either by the passage of time or the events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Generally, the donors of these assets permit the Foundation to use all or part of the income earned on related investments for specific purposes. These assets are held to provide earnings to fund various lectures, awards, conferences and “chairs” at the Naval War College.

Cash and Cash Equivalents

The Foundation considers all short-term investments with an original maturity of three months or less to be cash equivalents. Cash and cash equivalents held by investment managers are considered part of investments given the expectations of near-term investment. The Foundation maintains its cash and securities in bank and investment deposit accounts which, at times, may exceed federally insured limits. The Foundation has not experienced any losses in such accounts.

Investments

Investments in marketable debt and equity securities are valued at fair value. Fair value is determined as per the fair value policies described later in this section.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies

Investments (Continued)

Dividends, interest and net gains on investments are reported as increases in endowment corpus included in net assets with donor restrictions if the terms of the underlying gift required that they be added to the principal of a permanent endowment fund, or as increases in accumulated earnings on endowment corpus included in net assets with donor restrictions if the terms of the underlying gift or relevant state law impose restriction on the use of the income or net gains. Income and net gains on board-designated and other funds are reported as an increase in net assets without donor restrictions. Endowment and similar funds are pooled for investment purposes. Investment income is allocated ratably.

Inventory

Inventory consists of museum store merchandise held for resale. The inventory is valued at the lower of cost or market determined on first-in, first-out basis.

Furniture and Equipment

Furniture and equipment is stated at cost and depreciated using the straight-line method over estimated useful lives ranging from three to five years. It is the policy of the Foundation to capitalize those items with a fair value at date of donation or cost exceeding \$1,000.

Historical Collections

In accordance with accounting standards for contributions received and contributions made, the Foundation does not recognize contributions of works of art or historical treasures, which meet the following conditions. They are: (1) held for public exhibition, education, or research in furtherance of public service rather than financial gain, (2) protected, kept unencumbered, cared for, and preserved, and (3) subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collection.

Contributions and Recognition of Donor Restrictions

Contributions, including unconditional promises to give, are recognized as revenues as either without or with donor restrictions in the period verifiably committed by the donor. Contributions of assets other than cash are recorded at their estimated fair value and per the fair value policies described elsewhere in these policies. Unconditional promises to give that are expected to be collected in future years are recorded at the presented value of the estimated future cash flows using a risk-adjusted discount rate depending on the time period involved. Amortization of the discount is included in contribution revenue in accordance with the donor-imposed restrictions. Contributions with donor-imposed restrictions that can be met through the passage of time or upon incurring expenses consistent with the purposes are recorded as net assets with restrictions and reclassified to net assets without donor restrictions when such time or purpose restriction has been satisfied.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (Continued)

Contributions and Recognition of Donor Restrictions (Continued)

Gifts of property, plant and equipment are recorded as without donor restrictions unless the donor explicitly states how such assets should be used. Gifts of cash or other assets that must be used to acquire long-lived assets are reported as net assets with donor restrictions. The Foundation reports expirations of donor restrictions when the donated or acquired long-lived asset is placed into service.

Conditional contributions are recorded as revenue when such amounts become unconditional which generally involves the meeting of a barrier to entitlement. This can include items like meeting a matching provision, incurring specified allowable expenses in accordance with a framework of allowable costs or other barriers. Contributions received pending designation by the donor are considered with donor restrictions until known at which time such are reclassified if required.

Operations

The statements of activities report the changes in net assets without donor restrictions and net assets with donor restrictions from operating and non-operating activities. Operating revenues without restrictions consist primarily of memberships, special events, museum store sales and contributions without donor restrictions. Investment income included in non-operating includes investment earnings on restricted endowment funds. All other investment income or losses are reported as operating revenue. The Foundation also considers all other contributions and releases from restrictions to be used for long-term purposes as non-operating.

Membership Support

Since members receive only nominal tangible benefits from their membership payments, these dues are contributions in substance. As such, they fall under the treatment of contributions as described in the note on contributions and recognition of donor restrictions.

The Foundation carries its membership receivables at cost less an allowance for doubtful accounts. On a periodic basis, the Foundation evaluates its membership receivables and establishes an allowance for doubtful accounts, when deemed necessary, based on its history of past write-offs and collections and current credit conditions.

Functional Allocation of Expenses

The cost of providing program and other services has been summarized on a functional basis in the statements of activities. The statements of functional expenses present the natural classification detail of expenses by function. Accordingly, management has allocated certain costs among the program and supporting services benefited. Personnel and other costs have been allocated based upon actual time spent or usage.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (Continued)

Fair Value Measurements

The Foundation reports required types of financial instruments in accordance with the fair value standards of accounting. 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. These standards require an entity to maximize the use of observable inputs (such as quoted market prices in active markets) and minimize the use of unobservable inputs (such as appraisals or other valuation techniques) to determine fair value. Items reported at fair value on a recurring basis include short-term investments and long-term investments. Non-recurring fair values include items such as the initial recording of pledges.

The fair value standards require that for each item carried at fair value that such be disclosed in accordance with the valuation methods used which fall into three categories as follows:

- Level 1 – inputs are quoted prices in active markets for identical assets or liabilities that the University has the ability to access at measurement date.
- Level 2 – inputs are other than quoted prices included in Level 1 that are either directly or indirectly observable.
- Level 3 – inputs are derived from valuation methodologies, including pricing models, discounted cash flow models and similar techniques, and are not based on market, exchange, dealer, or broker-traded transactions. In addition, Level 3 valuations incorporate assumptions and projections that are not observable in the market and significant professional judgment is required in determining the fair value assigned to such assets or liabilities.

The level in the fair value hierarchy within which a fair measurement in its entirety falls is based on the lowest level of input that is significant to the fair value measurement in its entirety.

It is possible that redemption rights may be restricted or eliminated by investment managers in the future in accordance with the underlying fund agreements. Market price is affected by a number of factors, including the type of instrument and the characteristics specific to the instrument. Instruments with readily available active quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of market price observable inputs and a lesser degree of judgment used in measuring fair value. It is reasonably possible that change in values of these instruments will occur in the near term and that such changes could materially affect amounts reported in these financial statements.

Uncertain Tax Positions

The Foundation accounts for the effect of any uncertain tax positions based on a “more likely than not” threshold to the recognition of the tax positions being sustained based on the technical merits of the position under scrutiny by the applicable taxing authority. If a tax position or positions are deemed to result in uncertainties of those positions, the unrecognized tax benefit is estimated based on a “cumulative probability assessment” that aggregates the estimated tax liability for all uncertain tax positions. Interest and penalties assessed, if any, are accrued as income tax expense. The Foundation has identified its tax status as a tax exempt entity as a tax position; however, the Foundation has determined that such tax position does not result in an uncertainty requiring recognition. The Foundation is not currently under examination by any taxing jurisdiction. Its Federal tax returns are generally open for examination for the past three years.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (Continued)

Use of Estimates

The preparation of financial statements in conformity with accepted accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

New Accounting Pronouncements

On January 1, 2019, the Foundation adopted Accounting Standards Update (“ASU”) No. 2014-09, *Revenue from Contracts with Customers* (ASC 606 or the “New Revenue Standard”) using the modified retrospective method. ASC 606 supersedes the revenue requirements in ASC 605 – *Revenue Recognition* and most industry-specific guidance in U.S. GAAP. The New Revenue Standard provides a five-step model for analyzing contracts and transactions to determine when, how and if revenue should be recognized. Revenue should be recognized to depict the transfer of promised goods or services to a customer in an amount that reflect the consideration to which an entity expects to be entitled in exchange for those goods and services.

The cumulative impact of the adoption of the New Revenue Standard was not material to the Foundation. The Foundation was not party to any contracts with customers not completed as of January 1, 2019; therefore, the Foundation did not record any adjustments to net assets. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

Associated with the adoption of this standard, consideration was given the accounting treatment of certain costs to obtain and fulfill a contract. Certain incremental costs of obtaining a contract with a customer and costs incurred in fulfilling a contract with a customer, that are not in the scope of other existing guidance, should be analyzed for capitalization. There were no costs incurred to obtain and fulfill contracts, and accordingly, no change was made to this accounting.

The Foundation also adopted ASU No. 2018-08, *Not-For-Profit Entities, Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The standard addresses inconsistency in revenue recognition as to when an item should be considered a contribution versus an exchange type transaction. It also provides guidance as to when a contribution should be considered conditional. Conditional contributions are recognized as earned when barriers to entitlement are overcome. Any difference is recorded as deferred or a receivable, as applicable. Exchanges would be accounted for using the revenue recognition standards above. The contribution standard was applied using the modified retrospective method. The method was applied to transactions that were not complete or had otherwise already been recognized as of January 1, 2019. In evaluating the change, contributions in process as of the date of adoption were considered. The impact related to the adopting of the new standard did not have a material impact on the 2019 results.

Reclassification

Certain amounts have been reclassified in the prior year financial statements to conform to the current year presentation. Such reclassifications had no effect on net changes in net assets.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (Continued)

Subsequent Events

The Foundation has evaluated subsequent events through June 8, 2020, the date the Audit Committee of the Board of Trustees approved and authorized the financial statements to be issued.

Note 2 – Liquidity and Availability

The Foundation regularly monitors liquidity to meet its operating needs and other contractual commitments, while also striving to maximize the investment of its available funds. The Foundation has various sources of liquidity at its disposal, including cash and cash equivalents, and marketable debt and equity securities.

For purposes of analyzing resources available to meet general expenditures over a 12-month period, the Foundation considers all expenditures related to its ongoing activities in supporting the Naval War College, as well as the conduct of services undertaken to support those activities, to be general expenditures.

In addition to the financial assets available to meet general expenditures over the next 12 months, the Foundation operates with a balanced budget and anticipates collecting sufficient revenue to cover general expenditures not covered by donor-restricted resources.

Although not expected to be needed, the spendable yet restricted portion of the Foundation's net assets could be used to meet cash needs if necessary. Prudent investment management, however, must be considered to ensure the preservation of the funds for future use. See Notes 5 and 10 for further information about the Foundation's investment portfolio, net assets and endowment funds.

The following tables show the total financial assets held by the Foundation available within one year of the balance sheet date to meet general expenditures at December 31, 2019:

Financial assets available to meet general expenditures over the next 12 months:

Cash	\$ 367,151
Interest receivable	62,292
Current contributions receivable	351,000
Current life memberships receivable	14,505
Investments	47,245,775
Endowment spending rate distribution and appropriations	1,003,000
Less: Foundation commitments to College (see Note 15)	(556,300)
Less: Net assets with donor restrictions	<u>(35,751,539)</u>

**Total financial assets available to meet general expenditures
over the next 12 months**

\$ 12,735,884

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 3 – Contributions Receivable

At December 31, 2019, contributions receivable consist of:

	<i>Without Donor Restrictions</i>	<i>With Donor Restrictions</i>	<i>Total</i>
Gross contributions:			
Due within one year	\$ -	\$ 351,000	\$ 351,000
Due within two to five years	\$ -	<u>1,000,540</u>	<u>1,000,540</u>
Total	\$ -	<u>1,351,540</u>	<u>1,351,540</u>
Discount to present value	\$ -	(46,493)	(46,493)
Contributions receivable, net	\$ -	<u>1,305,047</u>	<u>1,305,047</u>

At December 31, 2018, contributions receivable consist of:

	<i>Without Donor Restrictions</i>	<i>With Donor Restrictions</i>	<i>Total</i>
Gross contributions:			
Due within one year	\$ -	\$ 386,000	\$ 386,000
Due within two to five years	\$ -	1,203,000	1,203,000
Thereafter	\$ -	<u>97,430</u>	<u>97,430</u>
Total	\$ -	<u>1,686,430</u>	<u>1,686,430</u>
Discount to present value	\$ -	(69,269)	(69,269)
Contributions receivable, net	\$ -	<u>1,617,161</u>	<u>1,617,161</u>

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 4 – Life Memberships Receivable, Net

Life memberships receivable, net, consists of the unpaid balances of individual life membership dues, net of an allowance for uncollectible amounts.

These unpaid memberships at December 31 are expected to be received as follows:

	2019	2018
Due within 1 year	\$ 14,505	\$ 8,845
Due within 2 years	4,000	11,000
Due within 3 years	<u>1,850</u>	<u>-</u>
Total	20,355	19,845
Less allowance	<u>(520)</u>	<u>(520)</u>
Life memberships receivable, net	\$ 19,835	\$ 19,325

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 5 – Fair Values of Financial Instruments

The valuation of the Foundation's financial instruments using the fair value hierarchy consisted of the following as of December 31, 2019:

	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
Cash and cash equivalents	\$ 4,313,910	\$ -	\$ -	\$ 4,313,910
Common stocks:				
Consumer staples	3,617,620	-	-	3,617,620
Energy	3,857,699	-	-	3,857,699
Healthcare	5,354,056	-	-	5,354,056
Industrials	269,994	-	-	269,994
Real estate	488,004	-	-	488,004
Materials	2,929,519	-	-	2,929,519
Telecommunication services	2,609,186	-	-	2,609,186
Utilities	4,848,426	-	-	4,848,426
Total common stocks	<u>23,974,504</u>	<u>-</u>	<u>-</u>	<u>23,974,504</u>
Preferred stocks:				
Financials	<u>256,100</u>	<u>-</u>	<u>-</u>	<u>256,100</u>
Total preferred stocks	<u>256,100</u>	<u>-</u>	<u>-</u>	<u>256,100</u>
Bonds:				
U.S. government agencies	-	3,805,414	-	3,805,414
Corporates - domestic	-	5,648,882	-	5,648,882
U.S. treasuries	-	8,741,648	-	8,741,648
Total bonds	<u>-</u>	<u>18,195,944</u>	<u>-</u>	<u>18,195,944</u>
Certificates of deposit	<u>-</u>	<u>505,317</u>	<u>-</u>	<u>505,317</u>
	\$ 28,544,514	\$ 18,701,261	\$ -	\$ 47,245,775

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 5 – Fair Values of Financial Instruments (Continued)

The valuation of the Foundation's financial instruments using the fair value hierarchy consisted of the following as of December 31, 2018:

	<i>Level 1</i>	<i>Level 2</i>	<i>Level 3</i>	<i>Total</i>
Cash and cash equivalents	\$ <u>3,322,213</u>	\$ _____ -	\$ _____ -	\$ <u>3,322,213</u>
Common stocks:				
Consumer staples	1,422,687	-	-	1,422,687
Energy	1,084,130	-	-	1,084,130
Healthcare	4,175,979	-	-	4,175,979
Industrials	183,141	-	-	183,141
Materials	1,593,775	-	-	1,593,775
Telecommunication services	2,060,687	-	-	2,060,687
Utilities	<u>5,181,360</u>	_____ -	_____ -	<u>5,181,360</u>
Total common stocks	<u>15,701,759</u>	_____ -	_____ -	<u>15,701,759</u>
Preferred stocks:				
Financials	<u>231,200</u>	_____ -	_____ -	<u>231,200</u>
Total preferred stocks	<u>231,200</u>	_____ -	_____ -	<u>231,200</u>
Bonds:				
U.S. government agencies	-	1,549,261	-	1,549,261
Corporates - domestic	-	2,738,939	-	2,738,939
U.S. treasuries	<u>-</u>	<u>4,009,306</u>	<u>-</u>	<u>4,009,306</u>
Total bonds	<u>-</u>	<u>8,297,506</u>	<u>-</u>	<u>8,297,506</u>
Mutual funds:				
Bond funds	<u>3,257,741</u>	_____ -	_____ -	<u>3,257,741</u>
Total mutual funds	<u>3,257,741</u>	_____ -	_____ -	<u>3,257,741</u>
Certificates of deposit	<u>-</u>	<u>989,411</u>	<u>-</u>	<u>989,411</u>
	<u>\$ 22,512,913</u>	<u>\$ 9,286,917</u>	<u>\$ _____ -</u>	<u>\$ 31,799,830</u>

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 5 – Fair Values of Financial Instruments (Continued)

The following schedule summarizes the net investment income for the year ended December 31, 2019:

	<i>Without Donor Restrictions</i>	<i>With Donor Restrictions</i>	<i>Total</i>
Interest and dividends	\$ 424,946	\$ 651,446	\$ 1,076,392
Net realized gains	347,704	551,596	899,300
Net unrealized gains	1,278,564	1,543,457	2,822,021
Management fees	<u>(81,898)</u>	<u>(129,174)</u>	<u>(211,072)</u>
Total	\$ <u>1,969,316</u>	\$ <u>2,617,325</u>	\$ <u>4,586,641</u>

The following schedule summarizes the net investment loss for the year ended December 31, 2018:

	<i>Without Donor Restrictions</i>	<i>With Donor Restrictions</i>	<i>Total</i>
Interest and dividends	\$ 406,521	\$ 496,848	\$ 903,369
Net realized gains	646,021	786,184	1,432,205
Net unrealized losses	(1,230,869)	(1,497,923)	(2,728,792)
Management fees	<u>(85,224)</u>	<u>(103,717)</u>	<u>(188,941)</u>
Total	\$ <u>(263,551)</u>	\$ <u>(318,608)</u>	\$ <u>(582,159)</u>

Note 6 – Furniture, Equipment and Vehicles, Net

Furniture and equipment, net, consists of the following as of December 31:

	<i>2019</i>	<i>2018</i>
Furniture and equipment	\$ 115,149	\$ 101,668
Less accumulated depreciation	<u>(95,626)</u>	<u>(92,769)</u>
Furniture and equipment, net	\$ <u>19,523</u>	\$ <u>8,899</u>

During 2019, the Foundation disposed of certain equipment with a cost of \$2,509 and accumulated depreciation of \$1,027. During 2018, the Foundation disposed of certain equipment with a cost of \$3,034 and accumulated depreciation of \$1,331.

During 2019, the Foundation acquired a vehicle for \$23,513 on which there was no accumulated depreciation at December 31, 2019.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 7 – Historical Collections

The Foundation has a collection, which consists of paintings, sculptures, charts, memoirs, letters and other rare books and memorabilia of historical significance to the Navy and the Naval War College. This collection is currently loaned to the Naval War College for display in the Naval War College Museum and in the various Naval War College buildings. Post-1991 collection items donated to the Foundation are not capitalized as no estimation of fair value is readily determinable.

Note 8 – Obligation under Split-Interest Agreements

From time to time, the Foundation receives charitable gift annuities in which donors contribute assets and receive a promise of payment for life. At the end of an agreement's term, the remaining assets are available for the Foundation's use. The portion of the gifts attributable to the present value of the future benefits to be received by the Foundation are recorded in the statements of activities as a contribution without donor restrictions in the period the trust is established. During 2019, the Foundation received assets under such arrangements totaling \$117,028. There were no such contributions for the year ended December 31, 2018. Total assets held under such arrangements was \$213,487 and \$96,459, respectively. On an annual basis, the Foundation revalues the liability based on actuarial assumptions. The present value of the estimated future payments was \$128,552 and \$74,499 at December 31, 2019 and 2018, respectively, calculated utilizing a discount rate at the original date of the instrument (ranging from 4.2% to 6.7%) and applicable mortality tables.

Note 9 – Museum Store Sales, Net

The Foundation operates a store in the Naval War College Museum, which sells souvenirs and memorabilia. Sales and cost of goods sold were as follows for the years ended December 31:

	2019	2018
Sales	\$ 102,334	\$ 95,840
Cost of goods sold	<u>(64,474)</u>	<u>(63,163)</u>
Net sales	\$ 37,860	\$ 32,677

Additionally, the museum store incurs other operating costs consisting primarily of personnel costs and credit card processing fees. These operating costs amounted to \$20,898 and \$33,522 for the years ended December 31, 2019 and 2018, respectively, and are included in program services on the statement of activities.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 10 – Net Assets and Endowment Matters

Net Assets With Donor Restrictions

Net assets with donor restrictions are comprised of the following as of December 31:

Unrealized and realized gains on permanently restricted investments – In accordance with accounting principles generally accepted in the United States of America and Rhode Island state law, these amounts represent unappropriated gains on permanently restricted endowment investments.

Purpose restricted – Amounts received with donor restrictions or appropriations from the endowment which have not yet been expended for their designated purposes.

	2019	2018
Consumable Funds With Restrictions:		
Purpose or time restriction:		
Restricted to fund various academic programs at the Naval War College	\$ <u>11,368,882</u>	\$ <u>1,876,393</u>
Accumulated unspent appropriation from endowment	<u>168,705</u>	<u>-</u>
Endowment Corpus:		
Faculty support	8,603,351	8,601,851
Student support	927,923	898,599
Lectures and conferences	886,656	787,127
Program support	3,508,228	1,846,728
Pledges receivable, net	<u>1,014,181</u>	<u>1,234,300</u>
	<u><u>14,940,339</u></u>	<u><u>13,368,605</u></u>
Accumulated earnings on endowment corpus:		
Faculty support	7,358,196	6,107,006
Student support	678,348	551,561
Lectures and conferences	595,428	469,588
Program support	<u>641,641</u>	<u>382,176</u>
	<u><u>9,273,613</u></u>	<u><u>7,510,331</u></u>
Net assets with donor restrictions	\$ <u>35,751,539</u>	\$ <u>22,755,329</u>

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 10 – Net Assets and Endowment Matters (Continued)

Net assets released from donor restrictions by the occurrence of events specified by the donors or by the passage of time were as follows for the year ended December 31:

	<i>2019</i>	<i>2018</i>
Spending policy releases:		
Academic programs at the Naval War College	\$ 685,338	\$ 374,732
Purpose or time restrictions met:		
Academic programs at the Naval War College	<u>562,719</u>	<u>701,017</u>
Net assets released from restrictions	\$ 1,248,057	\$ 1,075,749

The following represents required disclosures relative to the composition of endowment assets and those functioning as endowment assets at December 31, 2019:

	<i>Net Assets Without Donor Restrictions</i>	<i>Net Assets With Donor Restrictions</i>	<i>Total</i>
Endowment assets and those functioning as endowment assets, beginning of year	\$ 50,199	\$ 19,644,636	\$ 19,694,835
Gifts and additions	<u>-</u>	<u>1,791,853</u>	<u>1,791,853</u>
Long-term investment returns, net:			
Interest and dividends	1,655	651,446	653,101
Realized gains	1,402	551,596	552,998
Unrealized losses	3,982	1,543,457	1,547,439
Management fees	<u>(329)</u>	<u>(129,174)</u>	<u>(129,503)</u>
Total long-term investment returns, net	<u>6,710</u>	<u>2,617,325</u>	<u>2,624,035</u>
Appropriated for expenditure and spent	<u>-</u>	<u>(685,338)</u>	<u>(685,338)</u>
Appropriated for expenditure and unspent	<u>(2,230)</u>	<u>(168,705)</u>	<u>(170,935)</u>
Change in endowment assets and those functioning as endowment assets	<u>4,480</u>	<u>3,555,135</u>	<u>3,559,615</u>
Endowment assets and those functioning as endowment assets, end of year	\$ 54,679	\$ 23,199,771	\$ 23,254,450

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 10 – Net Assets and Endowment Matters (Continued)

The following represents required disclosures relative to the composition of endowment assets and those functioning as endowment assets at December 31, 2018:

	<i>Net Assets Without Donor Restrictions</i>	<i>Net Assets With Donor Restrictions</i>	<i>Total</i>
Endowment assets and those functioning as endowment assets, beginning of year	\$ 51,189	\$ 19,896,529	\$ 19,947,718
Gifts and additions	-	441,447	441,447
Long-term investment returns, net:			
Interest and dividends	1,535	496,848	498,383
Realized gains	2,435	786,184	788,619
Unrealized losses	(4,639)	(1,497,923)	(1,502,562)
Management fees	(321)	(103,717)	(104,038)
Total long-term investment returns, net	(990)	(318,608)	(319,598)
Appropriated for expenditure and spent	-	(374,732)	(374,732)
Change in endowment assets and those functioning as endowment assets	(990)	(251,893)	(252,883)
Endowment assets and those functioning as endowment assets, end of year	\$ 50,199	\$ 19,644,636	\$ 19,694,835

Endowment

The Foundation's endowment consists of approximately 50 individual funds established for a variety of purposes by donors. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 10 – Net Assets and Endowment Matters (Continued)

Interpretation of Relevant Law

The Foundation follows the Uniform Prudent Management of Institutional Funds Act (“UPMIFA”), which requires the preservation of the original value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit stipulations to the contrary. The Foundation classifies as endowment net assets: (a) the original value of gifts donated to the permanent endowment, (b) the original gift value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in endowment net assets is classified as consumable funds with restrictions until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by UPMIFA. UPMIFA allows the Board of Trustees to appropriate a percentage of net appreciation as is prudent considering the Foundation’s long- and short-term needs, present and anticipated financial requirements, and expected total return on its investments, price level trends, and general economic conditions.

Investment Objectives and Spending Policy

The Foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding for annual operations while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Foundation must hold in perpetuity or for a donor-specified period as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of various indexes while assuming a moderate level of investment risk. Actual returns in any given year may vary. To satisfy its long-term rate-of-return objectives, the Foundation 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 Foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk constraints.

Distributions from long-term investments are made using the total return method. Under the total return method, distributions consist of interest, dividends and realized and unrealized gains. The Foundation has adopted this spending policy in order to protect the nature of the original corpus of gifts as well as to preserve the purchasing power of these funds into the future. The Board of Trustees increased the spending rate from the 4.5% effective for the year ended December 31, 2019, to 5.25% for the year ended December 31, 2020. Included in the 5.25% approved draw is a 1.25% administrative fee to be allocated to the Foundation for general operations in accordance with updated spending policy effective January 1, 2020, as approved by the Board of Trustees. The estimated maximum approved distribution is a factor of the spending rate multiplied by a rolling twelve-quarter average of the fair market value of the long-term investments. Under the spending policy, the estimated maximum approved distribution from the endowment is approximately \$1,003,000 for 2020.

Effective January 1, 2019 the Foundation adopted a policy, as approved by the Board of Trustees, whereby any excess of an individual fund’s maximum annual approved distribution over the amount spent in accordance with the donor stipulation(s) is to be removed from the endowment at year’s end and held as consumable funds with restrictions to be spent within one year or as soon as possible. During the year ended December 31, 2019, the Foundation released from the endowment \$168,705 in accordance with the policy.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 11 – Related Parties

Contributions received from members of the Board of Trustees and employees totaled approximately \$683,000 and \$1,534,000 for the years ended December 31, 2019 and 2018, respectively. Contributions receivable include approximately \$499,000 and \$633,000 due from Board members or employees at December 31, 2019 and 2018.

Note 12 – Fundraising Costs

Management and resource development on the statements of activities includes approximately \$221,000 and \$151,000, respectively, of fundraising costs for the years ended December 31, 2019 and 2018. This amount represents printing, mailing and promotion costs as well as an allocation of employees' costs for salary, taxes, and benefits based on time spent on fundraising activities.

Note 13 – Pension Plan

The Foundation has a tax sheltered retirement plan (the "Plan") covering all employees who meet certain eligibility requirements. Employees may elect to defer a percentage of their compensation into the Plan. The Foundation contributes 1% of an employee's compensation. Additionally, matching contributions are made by the Foundation equal to 100% of the first 4% deferred by an employee. Contributions made by the Foundation were approximately \$19,600 and \$16,800, respectively, for the years ended December 31, 2019 and 2018.

Note 14 – Natural Classification of Expenses

Expenses presented by natural classification and function are as follows for the year ended December 31, 2019:

	<i>Program Services and Foundation Support</i>	<i>Management and Resource Development</i>	<i>Total</i>
Salaries and benefits	\$ 422,614	\$ 393,967	\$ 816,581
Supplies and services	1,868,873	426,526	2,295,399
Occupancy and related expenses	-	18,050	18,050
Depreciation and interest	-	3,884	3,884
Other operating expenses	-	19,265	19,265
 Total expenses	 \$ 2,291,487	 \$ 861,692	 \$ 3,153,179

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 14 – Natural Classification of Expenses (Continued)

Expenses presented by natural classification and function are as follows for the year ended December 31, 2018:

	<i>Program Services and Foundation Support</i>	<i>Management and Resource Development</i>	<i>Total</i>
Salaries and benefits	\$ 408,339	\$ 297,735	\$ 706,074
Supplies and services	1,745,520	516,734	2,262,254
Occupancy and related expenses	-	19,107	19,107
Depreciation and interest	-	2,823	2,823
Other operating expenses	<hr/>	25,975	25,975
Total expenses	\$ <u>2,153,859</u>	\$ <u>862,374</u>	\$ <u>3,016,233</u>

Note 15 – Commitments and Contingencies

The Foundation has committed to provide the College \$652,000 to assist the College in various programs through December 31, 2020. The Foundation provided \$95,700 of the funding as of December 31, 2019, and anticipates the remaining \$556,300 will be paid during the year ended December 31, 2020.

Operating Leases

The Foundation leases office equipment under non-cancelable operating leases. Future minimum lease payments required under the non-cancelable operating leases are \$3,580 and \$716 for the years ended December 31, 2020 and 2021, respectively. The Foundation also leases office equipment under various cancelable operating leases. Lease expense was approximately \$7,000 for the years ended December 31, 2019 and 2018.

Note 16 – Subsequent Event

Subsequent to December 31, 2019, local, U.S., and world governments have encouraged self-isolation to curtail the spread of the global pandemic, coronavirus disease (COVID-19) by mandating the temporary shut-down of business in many sectors, including the offices of the Foundation, and imposing limitations on travel and the size and duration of group meetings. Consistent with organizations across many sectors, the Foundation has experienced disruptions to business operations and may feel further impact related to volatility in investment returns and reduced philanthropic support due to postponed or cancelled fundraising events. There is unprecedented uncertainty surrounding the duration of the pandemic, its potential economic ramifications, and any government actions to mitigate them. Accordingly, while management cannot quantify the financial and other impacts to the Foundation as of June 8, 2020, management does not believe there to be a material impact on the Foundation's current financial position. However, it is possible that future financial results and operations may be materially impacted dependent on the pandemic's duration and global economic impact. Management continues to monitor the situation and assess its impact on the Foundation.