

# EARLHAM COLLEGE

Consolidated Financial Statements  
With Independent Auditors' Report

June 30, 2017 and 2016

# EARLHAM COLLEGE

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## **INDEPENDENT AUDITORS' REPORT**

Board of Trustees, Earlham College  
Board of Directors, Earlham Foundation  
Richmond, Indiana

We have audited the accompanying consolidated financial statements of Earlham College, including Earlham Foundation, which comprise the consolidated statements of financial position as of June 30, 2017 and 2016, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### ***Management's Responsibility for the Consolidated Financial Statements***

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

Board of Trustees, Earlham College  
Board of Directors, Earlham Foundation  
Richmond, Indiana

***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Earlham College, including Earlham Foundation, as of June 30, 2017 and 2016, and the changes in their consolidated net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Capin Crouse LLP*

Greenwood, Indiana  
October 16, 2017

# EARLHAM COLLEGE

## Consolidated Statements of Financial Position

	June 30,	
	2017	2016
<b>ASSETS:</b>		
Cash and cash equivalents	\$ 7,473,231	\$ 8,022,083
Cash—restricted	745,633	847,037
Cash—restricted for endowment	14,314,340	4,669,477
Cash—restricted by bond trustee	812	489
	22,534,016	13,539,086
Accounts and other receivables, net allowance of \$175,471 and \$193,353 for the years ended June 30, 2017 and 2016, respectively	1,206,401	2,077,188
Contributions receivable, net allowance of \$45,484 and \$78,421 for the years ended June 30, 2017 and 2016, respectively	1,780,655	2,033,886
Students notes receivable, net allowance of \$429,870 and \$407,497 for the years ended June 30, 2017 and 2016, respectively	3,525,156	3,938,466
Prepaid expenses and other assets	1,022,460	1,008,152
Property and equipment	147,417,861	145,988,240
Interest in charitable trusts	1,628,263	1,486,908
Investments—endowment and general institutional	417,507,933	384,735,733
Investments—restricted by bond trustee	7,511,653	8,803,075
<b>Total Assets</b>	<b>\$ 604,134,398</b>	<b>\$ 563,610,734</b>
<b>LIABILITIES AND NET ASSETS:</b>		
Liabilities:		
Accounts payable and accrued expenses	\$ 3,002,533	\$ 3,928,407
Construction accounts payable	273,223	872,570
Deposits, amounts held for others, and deferred income	2,303,754	2,253,107
Fair value of swap agreement	775,438	2,070,388
Loan payable, net of debt issuance costs of \$156,217 and \$175,950	24,843,783	16,824,050
Bonds payable, net of bond issuance costs of \$675,719 and \$714,370	82,310,874	84,407,818
Annuities payable	2,437,465	2,561,669
Capital lease obligations	981,494	660,754
Advances from federal agencies for student loans	3,701,253	3,992,051
<b>Total liabilities</b>	<b>120,629,817</b>	<b>117,570,814</b>
Net assets:		
Unrestricted		
Undesignated	33,795,530	41,812,563
Board and management designated (quasi-endowment)	34,980,767	32,010,743
<b>Total unrestricted</b>	<b>68,776,297</b>	<b>73,823,306</b>
Temporarily restricted	326,283,251	287,065,286
Permanently restricted	88,445,033	85,151,328
<b>Total net assets</b>	<b>483,504,581</b>	<b>446,039,920</b>
<b>Total Liabilities and Net Assets</b>	<b>\$ 604,134,398</b>	<b>\$ 563,610,734</b>

See notes to consolidated financial statements

# EARLHAM COLLEGE

## Consolidated Statement of Activities

Year Ended June 30, 2017

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>SUPPORT, REVENUE, AND RECLASSIFICATIONS:</b>				
Education and general:				
Tuition and fees	\$ 46,008,181	\$ -	\$ -	\$ 46,008,181
Less: Scholarships and student aid	(31,866,648)	-	-	(31,866,648)
Tuition and fees, net	14,141,533	-	-	14,141,533
Contributions	2,174,040	11,088,560	3,208,057	16,470,657
Investment return designated for current operations	8,914,554	8,209,283	-	17,123,837
Other investment income	82,115	-	-	82,115
Federal and state grants	1,044,611	-	-	1,044,611
Auxiliary income	9,626,345	-	-	9,626,345
Change in value of split-interest agreements	454,212	32,886	85,648	572,746
Other income	1,048,536	2,958,865	-	4,007,401
	37,485,946	22,289,594	3,293,705	63,069,245
Net assets released from purpose restrictions	22,288,335	(22,288,335)	-	-
<b>Total Support, Revenue, and Reclassifications</b>	<b>59,774,281</b>	<b>1,259</b>	<b>3,293,705</b>	<b>63,069,245</b>
<b>OPERATING EXPENSES:</b>				
Instruction	25,213,661	-	-	25,213,661
Research	450,274	-	-	450,274
Public service	330,756	-	-	330,756
Academic support	3,343,976	-	-	3,343,976
Student services	6,498,003	-	-	6,498,003
Administrative and general	11,531,997	-	-	11,531,997
Physical plant operation and maintenance	6,734,281	-	-	6,734,281
Auxiliary services	7,342,922	-	-	7,342,922
<b>Total Expenses</b>	<b>61,445,870</b>	<b>-</b>	<b>-</b>	<b>61,445,870</b>
<b>Change in Net Assets from Operations</b>	<b>(1,671,589)</b>	<b>1,259</b>	<b>3,293,705</b>	<b>1,623,375</b>
<b>NONOPERATING ACTIVITIES:</b>				
Investment return in excess of (less than) amounts designated for current operations	(4,670,370)	39,216,706	-	34,546,336
Change in value of interest rate swap	1,294,950	-	-	1,294,950
<b>Total Nonoperating Activities</b>	<b>(3,375,420)</b>	<b>39,216,706</b>	<b>-</b>	<b>35,841,286</b>
<b>Change in Net Assets</b>	<b>(5,047,009)</b>	<b>39,217,965</b>	<b>3,293,705</b>	<b>37,464,661</b>
<b>Net Assets, Beginning of Year</b>	<b>73,823,306</b>	<b>287,065,286</b>	<b>85,151,328</b>	<b>446,039,920</b>
<b>Net Assets, End of Year</b>	<b>\$ 68,776,297</b>	<b>\$ 326,283,251</b>	<b>\$ 88,445,033</b>	<b>\$ 483,504,581</b>

See notes to consolidated financial statements

# EARLHAM COLLEGE

## Consolidated Statement of Activities

Year Ended June 30, 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>SUPPORT, REVENUE, AND RECLASSIFICATIONS:</b>				
Education and general:				
Tuition and fees	\$ 42,557,600	\$ -	\$ -	\$ 42,557,600
Less: Scholarships and student aid	(27,201,217)	-	-	(27,201,217)
Tuition and fees, net	15,356,383	-	-	15,356,383
Contributions	884,166	4,606,797	1,494,224	6,985,187
Investment return designated for current operations	9,292,570	7,406,741	-	16,699,311
Other investment income	80,479	-	-	80,479
Federal and state grants	958,679	-	-	958,679
Auxiliary income	8,873,644	-	-	8,873,644
Change in value of split-interest agreements	103,010	126,832	(187,517)	42,325
Other income	298,441	778,859	-	1,077,300
	<u>35,847,372</u>	<u>12,919,229</u>	<u>1,306,707</u>	<u>50,073,308</u>
Net assets released from purpose restrictions	19,409,286	(19,409,286)	-	-
Total Support, Revenue, and Reclassifications	<u>55,256,658</u>	<u>(6,490,057)</u>	<u>1,306,707</u>	<u>50,073,308</u>
<b>OPERATING EXPENSES:</b>				
Instruction	24,101,210	-	-	24,101,210
Research	374,197	-	-	374,197
Public service	341,625	-	-	341,625
Academic support	2,774,946	-	-	2,774,946
Student services	5,518,357	-	-	5,518,357
Administrative and general	11,800,134	-	-	11,800,134
Physical plant operation and maintenance	7,868,038	-	-	7,868,038
Auxiliary services	7,026,244	-	-	7,026,244
Total Expenses	<u>59,804,751</u>	<u>-</u>	<u>-</u>	<u>59,804,751</u>
Change in Net Assets from Operations	(4,548,093)	(6,490,057)	1,306,707	(9,731,443)
<b>NONOPERATING ACTIVITIES:</b>				
Investment return in excess of (less than) amounts designated for current operations	(9,681,984)	(14,659,257)	-	(24,341,241)
Change in value of interest rate swap	(1,962,062)	-	-	(1,962,062)
Total Nonoperating Activities	<u>(11,644,046)</u>	<u>(14,659,257)</u>	<u>-</u>	<u>(26,303,303)</u>
Change in Net Assets	(16,192,139)	(21,149,314)	1,306,707	(36,034,746)
Net Assets, Beginning of Year	<u>90,015,445</u>	<u>308,214,600</u>	<u>83,844,621</u>	<u>482,074,666</u>
Net Assets, End of Year	<u>\$ 73,823,306</u>	<u>\$ 287,065,286</u>	<u>\$ 85,151,328</u>	<u>\$ 446,039,920</u>

See notes to consolidated financial statements

# EARLHAM COLLEGE

## Consolidated Statements of Cash Flows

	Year Ended June 30,	
	2017	2016
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Change in net assets	\$ 37,464,661	\$ (36,034,746)
Items not requiring (providing) cash:		
Depreciation and amortization	7,124,482	6,412,008
Net realized and unrealized (gains) losses	(50,127,862)	11,010,956
Net realized (gain) loss on sale of property and equipment	13,465	(55,725)
Contributions, restricted for long-term investment	(3,154,374)	(2,106,574)
Change in value of interest rate swap	(1,294,950)	1,962,062
Changes in:		
Accounts and notes receivable	870,787	147,059
Contributions receivable	253,231	2,103,149
Student notes receivable	413,310	165,053
Prepaid expenses and other assets	(14,308)	93,637
Interest in charitable trusts	(141,355)	201,361
Accounts payable and accrued expenses	(1,525,221)	(1,507,529)
Deposits, amounts held for others, and deferred income	50,647	243,311
Annuities payable	(124,204)	(142,913)
Advances from federal agencies for student loans	(290,798)	(123,427)
Net Cash Used by Operating Activities	(10,482,489)	(17,632,318)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(7,876,003)	(10,236,757)
Proceeds from sale of investments	72,705,648	47,366,252
Proceeds from sales or property and equipment	22,000	122,223
Purchases of investments	(54,007,143)	(36,740,823)
Purchase of investments restricted by bond trustee	(51,421)	(56,275)
Net Cash Provided by Investing Activities	10,793,081	454,620
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Proceeds from issuance of loan payable and bonds payable	8,000,000	8,000,000
Proceeds from contributions restricted for investment in endowment	3,154,374	2,106,574
Reduction of bond payable	(2,135,595)	(1,715,593)
Payments on capital lease obligations	(334,441)	(261,553)
Net Cash Provided by Financing Activities	8,684,338	8,129,428
Change in Cash and Cash Equivalents	8,994,930	(9,048,270)
Cash and Cash Equivalents, Beginning of Year	13,539,086	22,587,356
Cash and Cash Equivalents, End of Year	\$ 22,534,016	\$ 13,539,086
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>		
Cash paid for interest (\$-0- capitalized as of June 30, 2017 and 2016)	\$ 3,569,249	\$ 3,407,584
Property and equipment purchases in accounts payable	\$ 273,223	\$ 872,570
Property and equipment acquired through capital lease	\$ 655,181	\$ 337,512

See notes to consolidated financial statements



# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

1. NATURE OF ORGANIZATION:

Earlham College (College) was incorporated in 1881 as a not-for-profit organization under the laws of the State of Indiana. Earlham College is organized and operated for educational purposes and its primary sources of revenue are tuition, contributions and investment return. Earlham Foundation (Foundation) was incorporated in 1931 under the terms of a 1921 Indiana Act concerning foundations and holding companies. The Foundation's purpose is to receive and hold endowed gifts and bequests for the use and benefit of Earlham College and Earlham School of Religion. The Earlham School of Religion was created in 1960 as a Christian theological seminary to provide graduate-level training in the Quaker tradition. It operates as a separate fund within the financial structure of Earlham College.

2. SIGNIFICANT ACCOUNTING POLICIES:

**BASIS OF PRESENTATION**

The College prepares its financial statements using the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America (GAAP). The following are the more significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements.

**PRINCIPLES OF CONSOLIDATION**

The consolidated financial statements include the accounts of Earlham College and Earlham Foundation (the consolidated organization being referred to herein as "Earlham" or "Organization"). All material inter-organization accounts and transactions have been eliminated in consolidation.

**CLASSES OF NET ASSETS**

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

*Unrestricted net assets* consist of resources not subject to donor-imposed restrictions. Unrestricted net assets also include those net assets that are restricted as to their use by action of Earlham's Board of Trustees.

*Temporarily restricted net assets* consist of amounts restricted by donors and grantors for specific activities of Earlham or to be used at some future date. When a donor restriction expires, that is, when a time restriction ends or a purpose restriction is fulfilled, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions.

*Permanently restricted net assets* represent those resources subject to donor-imposed restrictions that they be maintained permanently by Earlham. The donors of these assets permit Earlham to use all or part of the income and gains on related investments for either general or specific purposes. Permanently restricted net assets include endowment funds, charitable remainder unitrusts, and contributions receivable.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES, continued:

#### USE OF ESTIMATES

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect (i) the reported amounts of assets and liabilities and disclosures of contingencies at the date of the consolidated financial statements and (ii) the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### CASH AND CASH EQUIVALENTS

Earlham considers all liquid investments with an original maturity of three months or less to be cash equivalents. Cash equivalents consist of money market funds and certificates of deposit. While Earlham's cash and cash equivalents balances may exceed federally insured limits, Earlham has not experienced any losses on such accounts. Earlham believes it is not exposed to any significant credit risk on these accounts.

#### ACCOUNTS RECEIVABLE

Accounts receivable are stated at the amount of tuition, housing and fees billed to students as well as amounts billed to outside organizations plus any accrued and unpaid service charges. Earlham provides an allowance for doubtful accounts, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions. Accounts receivable are ordinarily due 30 days after the issuance of the invoice unless a monthly electronic funds transfer plan election is made in advance. Accounts that are unpaid after the due date are subject to service charges at 1% per month. Accounts past due more than 120 days are considered delinquent. Service charges continue to accrue on delinquent accounts until the account is past due more than one year, at which time the service charge accrual ceases and does not resume until the account is no longer classified as delinquent. Delinquent receivables are written off based on individual credit evaluation and specific circumstances of the account. The total of accounts with balances over 120 days past due and still accruing service charges was approximately \$308,000 and \$371,000 at June 30, 2017 and 2016, respectively.

#### STUDENT NOTES RECEIVABLE

The majority of student notes receivable are under the Federal Perkins Loan Program and are reported at the outstanding principal balances. The repayment period begins after an initial grace period of either six or nine months after the student ceases to be at least a half-time student. At June 30, 2017 and 2016, the net Perkins receivable (included in the "students notes receivable" line on the consolidated statements of financial position) was \$3,432,653 and \$3,822,346 and the Perkins liability (the amount funded with federal funds and repayable upon program termination) was \$3,701,253 and \$3,992,051, respectively. The allowance for doubtful accounts is maintained at a level which, in management's judgment, is adequate to absorb potential losses inherent in the receivable portfolio. The amount of the allowance is based on management's evaluation of the collectability of the receivable portfolio, including the nature of the portfolio, credit concentrations, trends in historical loss experience, and economic conditions.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES, continued:

#### INVESTMENTS AND INVESTMENT RETURN

Investments in equity securities having a readily determinable fair value and in all debt securities are carried at fair value. Other investments are also carried at fair value. For those investments without readily determinable fair values, values used were those provided by the managers of the investment funds. These estimated values are subject to uncertainty and, therefore, may differ significantly from the value that would have been used had a market for such investments existed. Such differences could be material.

Investment return includes dividend, interest and other investment income; and realized and unrealized gains and losses on investments carried at fair value. Investment return is included in the consolidated statements of activities as unrestricted or temporarily restricted based upon the existence and nature of any donor or legally imposed restrictions.

All long-term investments have been pooled into the Earlham pooled endowment fund. This fund is managed by professional investment managers and net investment income is allocated quarterly on a unitized basis.

Earlham has significant investments in stocks, bonds, mutual funds and alternative investments and is therefore subject to various risks such as interest rate, market and credit risks. Investments are made by investment managers engaged by Earlham and the investments are monitored for Earlham by an investment advisor. Although the fair value of investments is subject to fluctuations on a year-to-year basis, management believes the investment policy is prudent for the long-term welfare of Earlham.

#### PROPERTY AND EQUIPMENT

Expenditures for property and equipment and items which substantially increase the useful lives of existing assets are capitalized at cost. Depreciation is calculated on the straight-line method at rates designed to depreciate the costs of assets over estimated useful lives as follows:

	<u>Years</u>
Buildings, grounds and improvements	20-50
Furniture and equipment	5
Transportation equipment	5
Computer equipment	4

The College capitalizes interest costs as a component of construction in progress, based on interest costs of borrowing specifically for the project, net of interest earned on investments acquired with the proceeds of the borrowing. Total interest capitalized was \$-0- for both years ended June 30, 2017 and 2016.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES, continued:

#### LONG-LIVED ASSET IMPAIRMENT

The College evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value. No asset impairment was recognized during the years ended June 30, 2017 and 2016.

#### CONTRIBUTIONS

Gifts of cash and other assets received without donor stipulations are reported as unrestricted revenue and net assets. Gifts received with a donor stipulation that limits their use are reported as temporarily or permanently restricted revenue and net assets. When a donor stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions. Gifts and investment income that are originally restricted by the donor and for which the restriction is met in the same time period are recorded as temporarily restricted and then released from restrictions.

Gifts of land, buildings, and equipment and other long-lived assets are reported as unrestricted revenue and net assets unless explicit donor stipulations specify how such assets must be used, in which case the gifts are reported as temporarily or permanently restricted revenue and net assets. Absent explicit donor stipulations for the time long-lived assets must be held, expirations of restrictions resulting in reclassification of temporarily restricted net assets as unrestricted net assets are reported when the long-lived assets are placed in service.

Unconditional gifts expected to be collected within one year are reported at their net realizable value. Unconditional gifts expected to be collected in future years are reported at the present value of estimated future cash flows. The resulting discount is amortized using the level-yield method and is reported as contribution revenue.

Conditional gifts depend on the occurrence of a specified future and uncertain event to bind the potential donor and are recognized as assets and revenue when the conditions are substantially met and the gift becomes unconditional.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES, continued:

#### GOVERNMENT GRANTS AND FEDERAL FINANCIAL AID

Support funded by grants is recognized as Earlham performs the contracted services under grant agreements. Grant revenue is recognized as earned as the eligible expenses are incurred. Grant expenditures and federal financial aid are subject to audit and acceptance by the granting agency and, as a result of such audit, adjustments could be required.

#### STUDENT FINANCIAL ASSISTANCE PROGRAMS

The College participates in various programs administered by the Department of Education (DOE) and state boards, and the College acts as an agent for the respective agencies. The governmental grant amounts reported exclude funds directly awarded and credited to students under the various federal and state programs; however, substantial portions of the tuition and fees revenue and collection of accounts receivable as of June 30, 2017 and 2016, are dependent upon the College's continued participation in the various programs.

#### INCOME TAXES

The College is exempt from federal income taxes under Section 501(c)(3) of the U.S. Internal Revenue Code and a similar provision of state law. During November 2016, the Foundation became exempt from federal income taxes under Section 501(c)(3) of the U.S. Internal Revenue Code and a similar provision of state law. The Foundation has been classified as a public organization, which is not a private foundation under Section 509(a) of the code. This exemption has a retrospective effective date of June 11, 2014. The Foundation was previously exempt under Section 501(c)(2) of the U.S. Internal Revenue Code as a title holding company and a similar provision of state law. However, the College and Foundation are subject to federal income tax on any unrelated business taxable income. The College and Foundation are not considered to be private foundations.

#### EXPENSE ALLOCATION

The costs of supporting the various programs and other activities have been summarized on a functional basis in the notes to the consolidated financial statements. Physical plant operations and maintenance costs have been classified as program, management and general, and fundraising based on the actual direct expenditures and cost allocations based upon square footage of space occupied.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 2. SIGNIFICANT ACCOUNTING POLICIES, continued:

#### FAIR VALUE OF FINANCIAL INSTRUMENTS

Earlham's financial instruments include cash and cash equivalents, accrued investment income receivable, contributions receivable, student notes receivable, investments, interest in charitable trusts, amounts held for others, liabilities under split-interest agreements and bonds payable.

For cash and cash equivalents and accrued investment income receivable, the carrying amounts approximate fair value because of the short maturity of these items. Investments and interest in charitable trusts are reflected at their estimated fair values using methodologies described in Note 15. The carrying amount of the contributions receivable, student notes receivable, amounts held for others, and liabilities under split-interest agreements are a reasonable estimate of the corresponding fair value.

The carrying value of the outstanding bonds payable was \$79,140,000 and \$81,115,000 with fair value of \$82,986,593 and \$85,122,188 as of June 30, 2017 and 2016, respectively. The fair value of the bonds payable is based on a discounted cash flow analysis using current yield rates offered for debt of the same remaining maturities.

#### RECLASSIFICATIONS

Certain amounts from the prior year have been reclassified to conform with current year presentation.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 3. CONTRIBUTIONS RECEIVABLE:

	Temporarily Restricted	Permanently Restricted	Total
As of June 30, 2017:			
Due within one year	\$ 274,730	\$ -	\$ 274,730
Due in one to five years	894,450	10,000	904,450
Due in more than five years	1,095,000	-	1,095,000
	2,264,180	10,000	2,274,180
Allowance for uncollectible contributions	(45,284)	(200)	(45,484)
Discount	(447,720)	(321)	(448,041)
	\$ 1,771,176	\$ 9,479	\$ 1,780,655
As of June 30, 2016:			
Due within one year	\$ 389,795	\$ 20,900	\$ 410,695
Due in one to five years	928,347	35,000	963,347
Due in more than five years	1,240,000	-	1,240,000
	2,558,142	55,900	2,614,042
Allowance for uncollectible contributions	(76,744)	(1,677)	(78,421)
Discount	(500,123)	(1,612)	(501,735)
	\$ 1,981,275	\$ 52,611	\$ 2,033,886

The discount rate ranged from 0.45% to 4.09% for both years ended June 30, 2017 and 2016.

Contributions receivable are designated for specific purposes as follows:

	June 30,	
	2017	2016
Time restrictions	\$ 49,807	\$ 107,286
Building renovations	126,194	170,684
Scholarship awards and instructional programs	289,352	219,774
Institutional support	1,305,823	1,483,531
Investment in perpetuity, the income of which is expendable to support:		
Scholarship awards	9,479	48,856
Instructional programs and research	-	3,755
	\$ 1,780,655	\$ 2,033,886

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

4. INVESTMENTS:

Earlham's investments are as follows:

	June 30,	
	2017	2016
Endowment and quasi-endowment funds:		
Domestic equities	\$ 57,355,369	\$ 48,355,834
International equities	74,018,867	65,092,854
Emerging markets	19,214,136	16,422,360
Fixed income debt securities	55,606,785	38,794,880
Alternative investments:		
Real estate	8,641,893	11,464,079
Private equity:		
Buyout and growth equity	42,371,276	49,923,854
Venture capital	26,426,971	28,639,522
Distressed debt	4,156,772	5,046,775
Natural resources	23,986,130	18,416,153
Hedge:		
Long/short funds	73,630,953	62,320,854
Fund of funds	8,887,011	10,675,021
Event-driven funds	16,033,180	23,100,376
Real estate	200,000	200,000
	410,529,343	378,452,562
Trust and annuity funds:		
Equity securities	3,889,535	3,380,966
Fixed income debt securities	1,689,292	1,615,682
Pooled income fund	529,949	498,064
Real estate and other	354,793	351,748
	6,463,569	5,846,460
Current fund:		
Real estate	506,791	436,711
Equity securities	8,230	-
	515,021	436,711
Restricted by bond trustee:		
Fixed income debt securities	7,511,653	8,803,075
	7,511,653	8,803,075
Total investments	\$ 425,019,586	\$ 393,538,808



# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

4. INVESTMENTS, continued:

The endowment investment portfolio balance included 48% and 56% of investments whose value is determined by fund managers' estimates or appraisals at June 30, 2017 and 2016, respectively.

Because certain investment managers do not provide fair values until late in the following quarter, Earlham's policy is to use the prior quarter's fair value, adjusted for cash receipts and cash disbursements, to determine the value of its endowment internally on a quarterly basis. The fair value used for the endowment investments under Earlham's endowment policy was \$406,786,288 and \$375,358,487 at June 30, 2017 and 2016, respectively. An adjustment of \$3,508,176 and \$2,858,874 represents the difference between the fair value used to compute the endowment at June 30, 2017 and 2016, respectively, for internal purposes and fair values provided by the investment managers received subsequent to year-end, which has been recorded in investments in the consolidated statements of financial position.

Total investment return is comprised of the following:

	June 30,	
	2017	2016
Dividends and interest (net of investment fees of \$612,786 and \$538,835 for the years ended June 30, 2017 and 2016, respectively)	\$ 2,347,786	\$ 2,807,600
Net realized and unrealized gains (losses) on investments	49,404,502	(10,369,051)
Total return on investments	51,752,288	(7,561,451)
Investment return designated for current operations	(17,123,837)	(16,699,311)
Other investment income	(82,115)	(80,479)
Investment return in excess of amounts designated for current operations	<u>\$ 34,546,336</u>	<u>\$ (24,341,241)</u>

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

5. PROPERTY AND EQUIPMENT:

Earlham's property and equipment are as follows:

	June 30,	
	2017	2016
Buildings, grounds and improvements	\$ 192,922,915	\$ 187,565,454
Furniture and equipment	13,941,894	12,778,739
Transportation equipment	729,419	679,432
Computer equipment	9,383,319	9,102,952
	<u>216,977,547</u>	<u>210,126,577</u>
Accumulated depreciation	<u>(75,032,671)</u>	<u>(67,982,165)</u>
	141,944,876	142,144,412
Land	2,812,143	2,744,236
Construction in progress	<u>2,660,842</u>	<u>1,099,592</u>
	<u>\$ 147,417,861</u>	<u>\$ 145,988,240</u>

6. EMPLOYEE GROUP MEDICAL INSURANCE:

Earlham has adopted a plan of self-insuring employee group medical insurance. Expenses are recorded as incurred. Insurance policies in force at both June 30, 2017 and 2016, limit Earlham's annual liability generally to \$125,000 per individual. Earlham's portion of the predetermined funding provision is charged to expense each month. The estimate of claims incurred but not paid (based on claims reported and an estimate of claims incurred but not reported) was \$250,000 for both the years ended June 30, 2017 and 2016.

7. LOAN PAYABLE:

In May 2015, Earlham College entered into a loan agreement with Huntington National Bank to borrow up to a maximum of \$25,000,000 under a five year draw facility that converts to a term loan for the purpose of financing operations and strategic initiatives. The loan bears interest at the rate of LIBOR plus 1.35%. During the five year commitment period, which began May 19, 2015, and ends May 19, 2020, Earlham College may request advances under the draw facility up to the maximum amount. During the commitment period interest is payable monthly. At the conclusion of the five year commitment period, the loan converts to a fixed term loan with a 120 month amortization of principal and interest. The final maturity date of the loan is May 19, 2025.

As of June 30, 2017 and 2016, the outstanding amount drawn under this loan agreement was \$25,000,000 and \$17,000,000, respectively. The outstanding balance on the consolidated statements of financial position is reported net of unamortized debt issuance costs of \$156,217 and \$175,950, respectively, for the years ended June 30, 2017 and 2016.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

8. BONDS PAYABLE:

Bonds payable consisted of the following:

	June 30,	
	2017	2016
Indiana Finance Authority, Educational Facilities Revenue Bonds, Series 2007 (A)	\$ 8,690,000	\$ 9,790,000
Indiana Finance Authority, Educational Facilities Revenue and Refunding Bonds, Series 2013 (B)	57,370,000	57,605,000
Indiana Finance Authority, Educational Facilities Revenue Bonds, Series 2015 (C)	13,080,000	13,720,000
	79,140,000	81,115,000
Unamortized premium	3,846,593	4,007,188
Less: unamortized bond issuance costs	(675,719)	(714,370)
	\$ 82,310,874	\$ 84,407,818

- (A) In June 2007, Earlham College entered into a loan agreement with the Indiana Finance Authority to finance the construction, renovation and equipping of certain educational facilities. The loan was financed by the sale of \$15,255,000 principal amount of Educational Facilities Revenue Bonds. These bonds are dated June 20, 2007, and bear various interest rates ranging from 4.25% to 5.00% depending on the maturity date. Interest is payable semi-annually on April 1 and October 1. The principal amount of the bonds is payable annually on October 1 from 2009 through 2028. In April 2015, Earlham advance refunded approximately 85% of the outstanding balance of these bonds. The principal balance of this portion of the bonds will be paid off on October 1, 2017, from funds currently held in escrow by the bond trustee.
- (B) In January 2013, Earlham College entered into a loan agreement with the Indiana Finance Authority to finance the construction, renovation and equipment of certain educational facilities. The loan was financed by the sale of \$58,500,000 principal amount of bonds. The bonds bear various interest rates ranging from 0.5% to 5.0% depending on the maturity date. Interest is payable semi-annually on April 1 and October 1. The principal amount of the bonds is payable annually on October 1 from 2013 through 2042.
- (C) In April 2015, Earlham College entered into a loan agreement with the Indiana Finance Authority to finance the renovation of certain educational facilities and to advance refund a substantial portion of the series 2007 bonds. The loan was financed by the sale of \$14,000,000 principal amount of bonds. The bonds bear interest at the rate of 2.92% until October 1, 2025, at which time it may change. Interest is payable semi-annually on April 1 and October 1. The principal amount of the bonds is payable annually on October 1 from 2015 through 2028. The bonds may be redeemed prior to maturity under specific circumstances and may be subject to redemption provisions as defined in the agreement.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

8. BONDS PAYABLE, continued:

The future maturities of bonds payable are as follows:

2018	\$ 8,490,000
2019	1,630,000
2020	2,110,000
2021	2,205,000
2022	2,300,000
Thereafter	<u>62,405,000</u>
	79,140,000
Plus unamortized premium	3,846,593
Less unamortized bond issuance costs	<u>(675,719)</u>
	<u><u>\$ 82,310,874</u></u>

The \$8,490,000 payment scheduled in fiscal year 2018 includes a payoff of the escrow for the series 2007 bonds. The principal balance for this series is \$8,690,000 at June 30, 2017. The proceeds for this payoff are escrowed with the bond trustee as of June 30, 2017, and are included in investments—restricted by bond trustee on the consolidated statements of financial position.

Under the terms of the bonds payable, Earlham is subject to certain covenants. Earlham was in compliance with these financial covenants as of June 30, 2017 and 2016, respectively.

Interest expense for the years ended June 30, 2017 and 2016, was \$3,563,099 and \$3,437,755, respectively.

9. ANNUITIES PAYABLE:

Earlham has been the recipient of several gift annuities, which require future payments to the contributors or their named beneficiaries. The assets received from the donors are recorded at fair market value. Earlham recorded a liability at June 30, 2017 and 2016, of \$2,437,465 and \$2,561,669, respectively, which represents the present value of the future annuity obligations discounted at a rate ranging from 1.2% to 10.0% for the years ended June 30, 2017 and 2016, respectively. Contribution revenue recognized under such agreements was \$11,808 and \$77,360 for the years ended June 30, 2017 and 2016, respectively.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 10. CAPITAL LEASE OBLIGATIONS:

Earlham leases equipment through various capital lease arrangements. Amortization expense for the capital leases is included within depreciation expense. The net book value of the assets associated with the capital leases are as follows:

	June 30,	
	<u>2017</u>	<u>2016</u>
Equipment under capital leases	\$ 1,977,180	\$ 1,321,999
Less accumulated depreciation	<u>(980,609)</u>	<u>(640,400)</u>
	<u>\$ 996,571</u>	<u>\$ 681,599</u>

Minimum payments required under capital lease obligations are as follows:

2018	\$ 311,476
2019	272,142
2020	208,022
2021	114,148
2022	91,700
Thereafter	<u>101,039</u>
	1,098,527
Less: amount representing interest	<u>(117,033)</u>
	<u>\$ 981,494</u>

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 11. TEMPORARILY RESTRICTED NET ASSETS:

Temporarily restricted net assets are available for the following purposes at June 30, 2017:

	Endowed	Not Endowed	Totals
Earlham College:			
Unallocated endowment appreciation	\$ 167,165,152	\$ -	\$ 167,165,152
Scholarship awards	53,923,876	4,785,753	58,709,629
Instructional programs	19,758,106	3,719,999	23,478,105
Institutional support	9,957,858	1,849,588	11,807,446
Academic support programs	5,549,051	1,755,915	7,304,966
Research programs	7,027,626	559,948	7,587,574
Building renovations	1,718,460	612,272	2,330,732
Student services programs	1,150,090	5,730,369	6,880,459
Other	1,047,856	-	1,047,856
Public service	311,334	299,655	610,989
Time restricted	-	268,908	268,908
	267,609,409	19,582,407	287,191,816
Earlham School of Religion:			
Unallocated endowment appreciation	20,272,134	-	20,272,134
Scholarship awards	7,755,530	925,406	8,680,936
Instructional programs	8,226,304	1,912,061	10,138,365
	36,253,968	2,837,467	39,091,435
Total temporarily restricted net assets	\$ 303,863,377	\$ 22,419,874	\$ 326,283,251

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

11. TEMPORARILY RESTRICTED NET ASSETS, continued:

Temporarily restricted net assets are available for the following purposes at June 30, 2016:

	Endowed	Not Endowed	Totals
Earlham College:			
Unallocated endowment appreciation	\$ 151,345,937	\$ -	\$ 151,345,937
Scholarship awards	46,462,166	5,035,756	51,497,922
Instructional programs	14,600,345	4,313,187	18,913,532
Institutional support	9,224,955	1,848,204	11,073,159
Academic support programs	4,852,411	1,808,679	6,661,090
Research programs	6,235,598	358,402	6,594,000
Building renovations	1,480,364	764,309	2,244,673
Student services programs	891,812	1,049,075	1,940,887
Other	911,903	-	911,903
Public service	274,344	327,623	601,967
Time restricted	-	304,364	304,364
	236,279,835	15,809,599	252,089,434
Earlham School of Religion:			
Unallocated endowment appreciation	18,340,807	-	18,340,807
Scholarship awards	6,780,185	880,209	7,660,394
Instructional programs	7,224,449	1,750,202	8,974,651
	32,345,441	2,630,411	34,975,852
Total temporarily restricted net assets	\$ 268,625,276	\$ 18,440,010	\$ 287,065,286

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 12. PERMANENTLY RESTRICTED NET ASSETS:

Permanently restricted net assets (valued at original gift basis) at June 30, 2017, are restricted to:

	Endowed	Not Endowed	Totals
Investment in perpetuity, the income of which is expendable to support Earlham College:			
Scholarship awards	\$ 31,477,070	\$ 73,024	\$ 31,550,094
Any activity of the College	23,999,584	1,025,058	25,024,642
Instructional programs	10,214,562	-	10,214,562
Academic support programs	2,191,172	599,606	2,790,778
General institutional program activities	2,113,605	-	2,113,605
Research programs	2,110,343	-	2,110,343
Other activities	1,009,186	-	1,009,186
Student service programs	3,519,512	96,815	3,616,327
Public services programs	117,562	-	117,562
	76,752,596	1,794,503	78,547,099
Earlham School of Religion:			
Scholarship awards	3,529,904	-	3,529,904
Any activity of ESR	3,260,841	-	3,260,841
Instructional programs	3,107,189	-	3,107,189
	9,897,934	-	9,897,934
	\$ 86,650,530	\$ 1,794,503	\$ 88,445,033



# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

12. PERMANENTLY RESTRICTED NET ASSETS, continued:

Permanently restricted net assets (valued at original gift basis) at June 30, 2016, are restricted to:

	Endowed	Not Endowed	Totals
Investment in perpetuity, the income of which is expendable to support Earlham College:			
Scholarship awards	\$ 30,992,841	\$ 48,856	\$ 31,041,697
Any activity of the College	23,999,584	954,980	24,954,564
Instructional programs	10,070,317	3,755	10,074,072
Academic support programs	2,162,002	526,228	2,688,230
General institutional program activities	2,249,575	-	2,249,575
Research programs	2,092,768	-	2,092,768
Other activities	1,005,726	-	1,005,726
Student service programs	962,061	-	962,061
Public services programs	117,562	-	117,562
	73,652,436	1,533,819	75,186,255
Earlham School of Religion:			
Scholarship awards	3,529,429	121,353	3,650,782
Any activity of ESR	3,257,841	-	3,257,841
Instructional programs	3,056,450	-	3,056,450
	9,843,720	121,353	9,965,073
	\$ 83,496,156	\$ 1,655,172	\$ 85,151,328

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 13. NET ASSETS RELEASED FROM RESTRICTIONS:

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors.

	June 30,	
	2017	2016
Purpose restrictions accomplished:		
Scholarship awards	\$ 6,152,241	\$ 4,103,006
General institutional support	3,443,946	2,945,297
Instructional program expenses	1,765,462	1,600,404
Student services program expenses	765,197	574,694
Academic support program expenses	467,410	507,181
Public services program expenses	43,876	295,261
Research program expenses	274,622	264,349
Earlham School of Religion program expenses	250,430	192,606
Total purpose restrictions accomplished	<u>13,163,184</u>	<u>10,482,798</u>
Endowment appropriation	8,933,680	8,718,574
Time restriction expired	<u>191,471</u>	<u>207,914</u>
Total net assets released from restrictions	<u>\$ 22,288,335</u>	<u>\$ 19,409,286</u>

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 14. ENDOWMENT:

Earlham maintains an Endowment Fund, which includes both donor-restricted endowment funds and funds designated by the governing body to function as endowments (board-designated endowment funds). The Endowment Fund excludes contributions that have been pledged but not yet received by Earlham. While the contributions reported within the Endowment Fund disclosures only reflect cash received, the statements of activities report all contributions, including permanently restricted pledges, in conformity with GAAP. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions. Earlham's Board of Trustees has interpreted the State of Indiana Prudent Management of Institutional Funds Act (SPMIFA) as requiring 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, Earlham classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of donor-restricted endowment funds is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Earlham in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, Earlham considers the following factors in making a determination to appropriate or accumulate income on a total return basis from donor-restricted endowment funds:

1. Duration and preservation of the fund
2. Purposes of Earlham and the fund
3. General economic conditions
4. Possible effect of inflation and deflation
5. Expected total return from investment income and appreciation or depreciation of investments
6. Other resources of Earlham
7. Investment policies of Earlham

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

14. ENDOWMENT, continued:

The composition of net assets by type of endowment fund at June 30, 2017, was:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds— income is purpose restricted	\$ -	\$ 117,961,702	\$ 62,650,946	\$ 180,612,648
Donor-restricted endowment funds— income is time restricted	-	167,165,152	23,999,584	191,164,736
Donor-restricted quasi-endowment funds	-	18,736,523	-	18,736,523
Board-designated endowment funds	34,980,767	-	-	34,980,767
Total endowment funds	\$ 34,980,767	\$ 303,863,377	\$ 86,650,530	\$ 425,494,674

The composition of net assets by type of endowment fund at June 30, 2016, was:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds— income is purpose restricted	\$ -	\$ 102,532,397	\$ 59,496,572	\$ 162,028,969
Donor-restricted endowment funds— income is time restricted	(9,579)	151,345,937	23,999,584	175,335,942
Donor-restricted quasi-endowment funds	-	14,746,942	-	14,746,942
Board-designated endowment funds	32,020,322	-	-	32,020,322
Total endowment funds	\$ 32,010,743	\$ 268,625,276	\$ 83,496,156	\$ 384,132,175

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

14. ENDOWMENT, continued:

Changes in endowment net assets for the year ended June 30, 2017, were:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ 32,010,743	\$ 268,625,276	\$ 83,496,156	\$ 384,132,175
Investment return				
Investment income	179,717	2,085,953	-	2,265,670
Net appreciation	4,116,259	45,340,036	-	49,456,295
Total investment return	4,295,976	47,425,989	-	51,721,965
Contributions	1,161,265	2,457,570	3,154,374	6,773,209
Appropriation of endowment assets for expenditure	(2,487,217)	(14,645,458)	-	(17,132,675)
Endowment net assets, end of year	\$ 34,980,767	\$ 303,863,377	\$ 86,650,530	\$ 425,494,674

Amounts of donor-restricted endowment funds classified as permanently and temporarily restricted net assets at June 30, 2017, consisted of:

Permanently restricted net assets - portion of perpetual endowment funds required to be retained permanently by explicit donor stipulation or SPMIFA	\$ 86,650,530
Temporarily restricted net assets - portion of perpetual endowment funds subject to a restriction under SPMIFA:	
With purpose restrictions	\$ 295,637,073
With time restrictions	8,226,304
	\$ 303,863,377

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level Earlham is required to retain as a fund of perpetual duration pursuant to donor stipulations or SPMIFA. There were no deficiencies of this nature at June 30, 2017.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

14. ENDOWMENT, continued:

Changes in endowment net assets for the year ended June 30, 2016, were:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ 35,311,439	\$ 288,819,234	\$ 81,389,582	\$ 405,520,255
Investment return				
Investment income	244,418	2,482,703	-	2,727,121
Net appreciation	(963,817)	(9,735,219)	-	(10,699,036)
Total investment return	(719,399)	(7,252,516)	-	(7,971,915)
Contributions	156,163	1,122,590	2,106,574	3,385,327
Appropriation of endowment assets for expenditure	(2,737,460)	(14,064,032)	-	(16,801,492)
Endowment net assets, end of year	\$ 32,010,743	\$ 268,625,276	\$ 83,496,156	\$ 384,132,175

Amounts of donor-restricted endowment funds classified as permanently and temporarily restricted net assets at June 30, 2016, consisted of:

Permanently restricted net assets - portion of perpetual endowment funds required to be retained permanently by explicit donor stipulation or SPMIFA	\$ 83,496,156
Temporarily restricted net assets - portion of perpetual endowment funds subject to a restriction under SPMIFA:	
With purpose restrictions	\$ 261,400,827
With time restrictions	7,224,449
	\$ 268,625,276

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level Earlham is required to retain as a fund of perpetual duration pursuant to donor stipulations or SPMIFA. Deficiencies of this nature were \$9,579 at June 30, 2016.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 14. ENDOWMENT, continued:

#### INVESTMENT AND SPENDING POLICIES

Earlham has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs and other items supported by its endowment while seeking to maintain the purchasing power of the endowment. Endowment assets include those assets of donor-restricted endowment funds Earlham must hold in perpetuity or for donor specified periods, as well as those of board-designated endowment funds. Under Earlham's policies, endowment assets are invested in a manner that is intended to preserve inflation-adjusted values and provide annual budgetary support that is both stable and growing.

To satisfy its long-term rate of return objectives, Earlham relies on a total return strategy in which investment returns are achieved through both a current yield (investment income such as dividends and interest) and capital appreciation (both realized and unrealized). Earlham targets a diversified asset allocation, including, but not limited to, equity, fixed income and alternative investment instruments. The asset mix of the Endowment Funds is described in Note 4.

State law allows the Board to appropriate as much of the net appreciation as is prudent considering long and short-term needs, present and anticipated financial requirements, expected total return on its investments, price level trends and general economic conditions. The Board's current endowment spending policy is to adjust the previous year's endowment spending by the change in the all-items CPI index with the limitation that the adjusted endowment spending shall not exceed 5% nor be less than 4% of the twelve-quarter average market value of the endowment investments.

### 15. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES:

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

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

**Level 2** – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

**Level 3** – Unobservable inputs supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 15. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES, continued:

#### RECURRING MEASUREMENTS

The following tables present the fair value measurements of assets recognized in the accompanying consolidated statements of financial position measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall.

	Fair Value	Fair Value Measurements at Reporting Date Using		
		Level 1	Level 2	Level 3
As of June 30, 2017:				
Investments:				
Domestic equities	\$ 57,355,369	\$ 38,089,598	\$ 19,265,771	\$ -
International equities	24,842,883	24,842,883	-	-
Emerging markets	10,941,541	10,941,541	-	-
Fixed income debt securities	40,127,383	40,127,383	-	-
Investments in split-interest agreements and other:				
Equity securities	3,889,535	3,889,535	-	-
Fixed income debt securities	1,689,292	1,689,292	-	-
Pooled income fund	529,949	-	529,949	-
Real estate and other	354,793	354,793	-	-
Current fund investments:				
Equity securities	8,230	8,230	-	-
	<u>139,738,975</u>	<u>119,943,255</u>	<u>19,795,720</u>	<u>-</u>
Investments—restricted by bond trustee:				
Fixed income debt securities	<u>7,511,653</u>	<u>-</u>	<u>7,511,653</u>	<u>-</u>
	<u>\$ 147,250,628</u>	<u>\$ 119,943,255</u>	<u>\$ 27,307,373</u>	<u>\$ -</u>
Investments held at net asset value:				
International equities	49,175,984			
Emerging markets	8,272,595			
Fixed income debt securities	15,479,402			
Alternative investments:				
Real estate	8,641,893			
Private equity:				
Buyout and growth equity	42,371,276			
Venture capital	26,426,971			
Distressed debt	4,156,772			
Natural resources	23,986,130			
Hedge:				
Long/short funds	73,630,953			
Fund of funds	8,887,011			
Event-driven funds	16,033,180			
	<u>277,062,167</u>			
Investments not held at fair value:				
Real estate	<u>706,791</u>			
Total Investments	<u>\$ 425,019,586</u>			



# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 15. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES, continued:

#### RECURRING MEASUREMENTS, continued

	Fair Value	Fair Value Measurements at Reporting Date Using		
		Level 1	Level 2	Level 3
As of June 30, 2016:				
Investments:				
Domestic equities	\$ 48,355,834	\$ 36,757,480	\$ 11,598,354	\$ -
International equities	21,843,780	21,843,780	-	-
Emerging markets	9,263,072	9,263,072	-	-
Fixed income debt securities	27,037,725	27,037,725	-	-
Investments in split-interest agreements and other:				
Equity securities	3,380,966	3,380,966	-	-
Fixed income debt securities	1,615,682	1,615,682	-	-
Pooled income fund	498,064	-	498,064	-
Real estate and other	351,748	351,748	-	-
	<u>112,346,871</u>	<u>100,250,453</u>	<u>12,096,418</u>	<u>-</u>
Investments - restricted by bond trustee				
Fixed income debt securities	8,803,075	-	8,803,075	-
	<u>\$ 121,149,946</u>	<u>\$ 100,250,453</u>	<u>\$ 20,899,493</u>	<u>\$ -</u>
Investments held at net asset value:				
International equities	43,249,074			
Emerging markets	7,159,288			
Fixed income debt securities	11,757,155			
Alternative investments:				
Real estate	11,464,079			
Private equity:				
Buyout and growth equity	49,923,854			
Venture capital	28,639,522			
Distressed debt	5,046,775			
Natural resources	18,416,153			
Hedge:				
Long/short funds	62,320,854			
Fund of funds	10,675,021			
Event-driven funds	23,100,376			
	<u>271,752,151</u>			
Investments not held at fair value:				
Real estate	<u>636,711</u>			
Total Investments	<u>\$ 393,538,808</u>			

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 15. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES, continued:

Following is a description of the valuation methodologies and inputs used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying consolidated statements of financial position, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the years ended June 30, 2017 and 2016, respectively. For assets classified within Level 3 of the fair value hierarchy, the process used to develop the reported fair value is described below.

#### INVESTMENT STRATEGY

In addition to traditional stocks and fixed income securities, the College also holds shares, units or interests in institutional funds and alternative investment partnerships involving hedged strategies, private equity and real asset strategies. Hedged strategies involve funds whose managers have the authority to invest in various asset classes at their discretion, including the ability to invest long and short. Funds with hedged strategies generally hold securities or other financial instruments for which a ready market exists and may include stocks, bonds, put or call options, swaps, currency hedges and other instruments, and are valued accordingly. Private equity funds employ buyout, venture capital, and distressed credit strategies. Real asset and natural resources funds generally hold interests in private real estate, oil and gas partnerships and mineral holdings. Private equity and real asset strategies often require the estimation of fair values by the fund managers in the absence of readily determinable market values.

#### BASIS OF REPORTING

Investments are reported at estimated fair value. If an investment is held directly by the College and an active market with quoted prices exists, the market price of an identical security is used as reported fair value. The College's interests in alternative investment funds are generally reported at the net asset value (NAV) reported by the fund managers. Fair value determinations are the joint responsibility of the Investment office, the Controller's office, and the Investment Committee of the Board. The College contracts with an independent consultant to review fair value estimates on a quarterly basis. The Investment office and the Investment Committee challenge the reasonableness of the assumptions used and review the methodology, and the Controller's office ensures the estimated fair value complies with accounting standards generally accepted in the United States.

Because of inherent uncertainties in valuation assumptions, the estimated fair values for alternative investments such as private equity and private real estate may differ significantly from values that would have been used had a ready market existed, and the differences could be material. Such valuations are determined by fund managers and generally consider variables such as operating results, comparable earnings multiples, projected cash flows, recent sales prices, and other pertinent information.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 15. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES, continued:

#### BASIS OF REPORTING, continued

Registered mutual funds and securities are classified in Level 1 of the fair value hierarchy because their fair values are based on quoted prices for identical securities.

Most investments classified in Levels 2 and 3 consist of shares, units in funds or partnership interests as opposed to direct interests in the funds' underlying securities, which may be readily marketable and not difficult to value.

Many of these funds are not registered under the 1940 Securities and Exchange Act.

Certain hedge funds contain lock-up provisions. Under such provisions, share classes of the investment are available for redemption at various times in accordance with the management agreement with the fund.

#### MONEY MARKET FUNDS

Where quoted market prices are available in an active market, money market funds are classified within Level 1 of the hierarchy.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 15. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES, continued:

#### INVESTMENTS HELD AT NET ASSET VALUE

The following table presents information regarding funds with fair value that is determined using the net asset value (or its equivalent) provided by the fund as of June 30, 2017.

	Fair Value	Unfunded Commitments	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Investments:				
Real estate	\$ 8,641,893	\$ 12,355,973	Non-redeemable	Non-redeemable
Private equity	68,798,247	10,665,235	Non-redeemable	Non-redeemable
Distressed debt	4,156,772	6,911,992	Non-redeemable	Non-redeemable
Natural resources	23,986,130	8,116,421	Non-redeemable	Non-redeemable
Hedge funds	98,551,144	-	Quarterly/Annually	45 - 90 days
International equity	49,175,984	-	Daily	Daily
Emerging markets	8,272,595	-	Daily	15 days
Fixed income debt securities	15,479,402	-	Daily	30 days
	<u>\$ 277,062,167</u>	<u>\$ 38,049,621</u>		

The following table presents information regarding funds with fair value that is determined using the net asset value (or its equivalent) provided by the fund as of June 30, 2016.

	Fair Value	Unfunded Commitments	Redemption Frequency (if Currently Eligible)	Redemption Notice Period
Investments:				
Real estate	\$ 11,464,079	\$ 11,416,619	Non-redeemable	Non-redeemable
Private equity	78,563,376	13,249,665	Non-redeemable	Non-redeemable
Distressed debt	5,046,775	6,911,992	Non-redeemable	Non-redeemable
Natural resources	18,416,153	5,530,389	Non-redeemable	Non-redeemable
Hedge funds	96,096,251	-	Quarterly/Annually	45 - 90 days
International equity	43,249,074	-	Daily	Daily
Emerging markets	7,159,288	-	Daily	15 days
Fixed income debt securities	11,757,155	-	Daily	30 days
	<u>\$ 271,752,151</u>	<u>\$ 37,108,665</u>		

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 15. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES, continued:

#### INVESTMENTS HELD AT NET ASSET VALUE, continued

**Real estate** includes several real estate limited partnerships that invest primarily in U.S. commercial real estate. These investments can never be liquidated at the College's request. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the funds. It is estimated that the underlying assets of the funds will be liquidated over the next 1 to 15 years. The fair values of the investments in this category have been estimated using the net asset value of the College's ownership interest in partners' capital.

**Private equity** includes several private equity and venture capital limited partnerships that invest primarily in U.S. and international companies. These investments can never be liquidated at the College's request. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the fund. It is estimated that the underlying assets of the funds will be liquidated over the next 1 to 15 years. The fair values of the investments in this category have been estimated using the net asset value of the College's ownership interest in partners' capital. Approximately 36% of private equity funds are venture capital funds.

**Distressed debt** includes several distressed debt limited partnerships that invest primarily in the debt of U.S. companies. These investments can never be liquidated at Earlham's request. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the fund. It is estimated that the underlying assets of the funds will be liquidated over the next 1 to 15 years. The fair values of the investments in this category have been estimated using the net asset value of Earlham's ownership interest in partners' capital.

**Natural resources** include several limited partnerships that invest primarily in U.S. natural resource and energy companies. These investments can never be liquidated at Earlham's request. Instead, the nature of the investments in this category is that distributions are received through the liquidation of the underlying assets of the fund. It is estimated that the underlying assets of the funds will be liquidated over the next 1 to 15 years. The fair values of the investments in this category have been estimated using the net asset value of Earlham's ownership interest in partners' capital.

**Hedge funds** include investments in several different types of hedge fund limited partnerships: long/short funds, event-driven funds, and funds of hedge funds. The investments are generally subject to an initial lock-up period, which expires after 1 to 2 years. All funds are redeemable quarterly or annually with a notice period of between 45 and 90 days. The fair values of the investments in this category have been estimated using the net asset value per share of the investments. Approximately 65% of total hedge funds are long/short funds.

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 15. DISCLOSURES ABOUT FAIR VALUE OF ASSETS AND LIABILITIES, continued:

#### INVESTMENTS HELD AT NET ASSET VALUE, continued

*International equity* investments are in commingled funds. Their underlying assets are daily priced and traded public equities; however, trades in and out of the investment vehicle are executed at net asset value (NAV).

*Emerging markets* investments are in commingled funds. Their underlying assets are daily priced and traded public equities; however, trades in and out of the investment vehicle are executed at net asset value (NAV).

*Fixed income debt securities* investments are in commingled funds. Their underlying assets are daily priced and traded public equities; however, trades in and out of the investment vehicle are executed at net asset value (NAV).

### 16. RETIREMENT PLAN:

Full-time employees of Earlham are eligible to participate in a defined-contribution retirement plan administered by TIAA-CREF. Earlham contributions begin after the participants' second year of service. Under this plan, contributions are immediately vested for the benefit of the participants. Earlham's contributions amounted to approximately \$1,502,000 and \$1,506,000 for the years ended June 30, 2017 and 2016, respectively.

### 17. LEASE:

Earlham has leased land to Bethany Theological Seminary (Bethany). Bethany constructed a building on the leased real estate. The land lease has a 100-year initial term, requires annual rental payments which approximate the fair rental value of the land, and provides for renewal options. Bethany shares certain administrative costs with Earlham College and with the Earlham School of Religion.

### 18. FUNCTIONAL EXPENSES:

Expenses by functional classification are as follows:

	June 30,	
	2017	2016
Program services	\$ 49,913,872	\$ 48,004,617
Management and general	8,481,086	10,366,857
Fundraising	3,050,912	1,433,277
	<u>\$ 61,445,870</u>	<u>\$ 59,804,751</u>

# EARLHAM COLLEGE

## Notes to Consolidated Financial Statements

June 30, 2017 and 2016

### 19. CONTINGENCIES:

#### LEGAL MATTERS

The College is subject to claims and lawsuits that arose primarily in the ordinary course of its activities. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the financial position, change in net assets and cash flows of the College. Events could occur that would change this estimate materially.

#### STUDENT FINANCIAL ASSISTANCE PROGRAMS

Activity related to student financial assistance programs is subject to audit both by independent certified public accountants and by representatives of the administering agencies regarding compliance with applicable regulations. Any resultant findings of noncompliance could potentially result in the required return of related funds received and/or the assessment of fines or penalties, or the discontinuation of eligibility for participation. In the opinion of management, audit adjustments, if any, will not have a significant effect on the financial position or result of activities of the College.

### 20. SUBSEQUENT EVENTS:

Subsequent events have been evaluated through October 16, 2017, which represents the date the consolidated financial statements were available to be issued. Subsequent events after that date have not been evaluated.