

# **Kansas City Art Institute**

Independent Auditor's Report and Financial Statements

June 30, 2016 and 2015



# Kansas City Art Institute

June 30, 2016 and 2015

## Contents

Independent Auditor's Report.....	1
-----------------------------------	---

### Financial Statements

Statements of Financial Position .....	3
Statements of Activities.....	4
Statements of Cash Flows.....	5
Notes to Financial Statements .....	6

## Independent Auditor's Report

Board of Trustees and Audit Committee  
Kansas City Art Institute  
Kansas City, Missouri

### Report on the Financial Statements

We have audited the accompanying financial statements of Kansas City Art Institute (the "Institute"), which comprise the statements of financial position as of June 30, 2016 and 2015, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

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

Management is responsible for the preparation and fair presentation of these financial statements in 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.

### *Auditor's Responsibility*

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Institute'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 Institute'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.

Board of Trustees and Audit Committee  
Kansas City Art Institute  
Page 2

*Opinion*

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Kansas City Art Institute as of June 30, 2016 and 2015, 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.

*BKD, LLP*

Kansas City, Missouri  
October 19, 2016

**Kansas City Art Institute**  
**Statements of Financial Position**  
**June 30, 2016 and 2015**

**Assets**

	<b>2016</b>	<b>2015</b>
Cash and cash equivalents	\$ 6,899,784	\$ 7,164,708
Restricted cash	<u>297,239</u>	<u>332,020</u>
Total cash and cash equivalents	<u>7,197,023</u>	<u>7,496,728</u>
Receivables		
Student accounts receivable and other miscellaneous receivables, net of allowance, 2016 - \$165,277, 2015 - \$170,642	157,511	317,326
Student loans receivable	1,707,335	1,737,511
Pledges receivable, net of allowance 2016 and 2015 - \$3,200,000	<u>10,085,611</u>	<u>5,935,912</u>
Total net receivables	11,950,457	7,990,749
Prepaid expenses and other assets	289,406	356,790
Investments	64,437,938	61,782,344
Funds held in trust by others	2,401,821	2,472,767
Property and equipment, net	24,295,448	19,602,368
Assets held for sale	600,000	785,850
Paintings and works of art	<u>947,962</u>	<u>947,962</u>
Total assets	<u><u>\$ 112,120,055</u></u>	<u><u>\$ 101,435,558</u></u>

**Liabilities and Net Assets**

**Liabilities**

Accounts payable and accrued expenses	\$ 2,140,858	\$ 1,599,551
Deferred revenue	435,254	334,507
Bonds payable	10,500,000	10,500,000
Refundable loan program	<u>1,860,949</u>	<u>1,853,316</u>
Total liabilities	<u>14,937,061</u>	<u>14,287,374</u>

**Net Assets**

Unrestricted	28,015,147	26,646,595
Temporarily restricted	24,754,147	24,809,249
Permanently restricted	<u>44,413,700</u>	<u>35,692,340</u>
Total net assets	<u>97,182,994</u>	<u>87,148,184</u>
Total liabilities and net assets	<u><u>\$ 112,120,055</u></u>	<u><u>\$ 101,435,558</u></u>

**Kansas City Art Institute**  
**Statements of Activities**  
**Years Ended June 30, 2016 and 2015**

	2016			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Revenues, Gains and Other Support</b>				
Student tuition and fees	\$ 21,434,881			\$ 21,434,881
Less institutional financial aid	(10,640,327)			(10,640,327)
	10,794,554			10,794,554
Summer and continuing education	850,468			850,468
Interest and dividend income	1,318,409	\$ 125,705		1,444,114
Contributions, gifts and grants	3,192,193	3,619,523	\$ 8,900,892	15,712,608
Net realized and unrealized losses on investments and funds held in trust by others	(236,689)	(979,561)	(179,532)	(1,395,782)
Auxiliary enterprises	1,681,767			1,681,767
Net assets released to (from) restrictions	2,820,769	(2,820,769)		-
Total revenues, gains and other support	20,421,471	(55,102)	8,721,360	29,087,729
<b>Expenses</b>				
Program services				
Instruction	4,565,361			4,565,361
Academic support	1,983,424			1,983,424
Summer and continuing education	816,990			816,990
Student services	1,587,487			1,587,487
Auxiliary enterprises	1,042,008			1,042,008
Support services				
General administration	1,225,748			1,225,748
Fundraising	706,499			706,499
General institutional	3,552,981			3,552,981
Plant operations and maintenance	3,572,421			3,572,421
Total expenses	19,052,919			19,052,919
<b>Increase (Decrease) in Net Assets</b>	1,368,552	(55,102)	8,721,360	10,034,810
<b>Net Assets, Beginning of Year</b>	26,646,595	24,809,249	35,692,340	87,148,184
<b>Net Assets, End of Year</b>	\$ 28,015,147	\$ 24,754,147	\$ 44,413,700	\$ 97,182,994

See Notes to Financial Statements

	2015			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
<b>Revenues, Gains and Other Support</b>				
Student tuition and fees	\$ 21,661,145			\$ 21,661,145
Less institutional financial aid	(10,416,498)			(10,416,498)
	11,244,647			11,244,647
Summer and continuing education	975,459			975,459
Interest and dividend income	482,143	\$ 401,134		883,277
Contributions, gifts and grants	1,701,059	5,672,897	\$ 92,786	7,466,742
Net realized and unrealized gains (losses) on investments and funds held in trust by others	103,138	1,026,832	(119,628)	1,010,342
Auxiliary enterprises	1,690,650			1,690,650
Net assets released to (from) restrictions	2,306,621	(2,306,621)		-
Total revenues, gains and other support	18,503,717	4,794,242	(26,842)	23,271,117
<b>Expenses</b>				
Program services				
Instruction	4,324,936			4,324,936
Academic support	1,928,046			1,928,046
Summer and continuing education	824,705			824,705
Student services	1,582,335			1,582,335
Auxiliary enterprises	1,116,748			1,116,748
Support services				
General administration	1,064,613			1,064,613
Fundraising	776,781			776,781
General institutional	3,732,876			3,732,876
Plant operations and maintenance	2,861,628			2,861,628
Total expenses	18,212,668			18,212,668
<b>Increase (Decrease) in Net Assets</b>	291,049	4,794,242	(26,842)	5,058,449
<b>Net Assets, Beginning of Year</b>	26,355,546	20,015,007	35,719,182	82,089,735
<b>Net Assets, End of Year</b>	\$ 26,646,595	\$ 24,809,249	\$ 35,692,340	\$ 87,148,184

# Kansas City Art Institute

## Statements of Cash Flows

### Years Ended June 30, 2016 and 2015

	2016	2015
<b>Operating Activities</b>		
Change in net assets	\$ 10,034,810	\$ 5,058,449
Items not requiring (providing) cash		
Depreciation and amortization	1,014,419	939,205
Net realized and unrealized (gains) losses on investments and funds held in trust by others	1,395,782	(1,010,342)
Discount on pledges receivable	141,468	(3,147)
Contribution of land and building	(1,200,000)	-
Contributions and investment income restricted for long-term investment	(12,520,415)	(5,092,786)
Impairment on building held for sale	185,850	50,079
Loss from sale of equipment	-	3,351
Changes in		
Student accounts receivable	159,815	(205,016)
Pledges receivable	1,167	10,416
Prepaid expenses and other assets	67,384	136,471
Accounts payable and accrued expenses	(176,182)	(98,481)
Deferred revenue	100,747	(88,921)
Net cash used in operating activities	(795,155)	(300,722)
<b>Investing Activities</b>		
Purchases of property and equipment	(3,790,010)	(556,765)
Purchases of investments	(15,361,068)	(9,318,126)
Sales of investments	11,380,638	10,809,083
Net change in student loans receivable	30,176	7,676
Net cash provided by (used in) investing activities	(7,740,264)	941,868
<b>Financing Activities</b>		
Net increase in refundable loan programs	7,633	7,030
Changes in pledges receivable restricted for long-term investment	328,483	359,750
Contributions and investment income restricted for long-term investment	7,899,598	92,786
Net cash provided by financing activities	8,235,714	459,566
<b>Increase (Decrease) in Cash and Cash Equivalents</b>	(299,705)	1,100,712
<b>Cash and Cash Equivalents, Beginning of Year</b>	7,496,728	6,396,016
<b>Cash and Cash Equivalents, End of Year</b>	\$ 7,197,023	\$ 7,496,728
<b>Supplemental Cash Flows Information</b>		
Cash paid for interest	\$ 12,513	\$ 5,693
Property and equipment additions included in accounts payable	717,489	-



# **Kansas City Art Institute**

## **Notes to Financial Statements**

**June 30, 2016 and 2015**

### **Note 1: Nature of Operations and Summary of Significant Accounting Policies**

#### ***Nature of Operations***

The Kansas City Art Institute (the Institute) is a private, non-profit, independent college of visual art and design offering the Bachelor of Fine Arts degree in a variety of disciplines. Founded in 1885, the Institute is Kansas City's oldest cultural institution. In 1946, the Institute became a degree-granting college, maintaining its founding philosophical premise as a studio school based on the master-apprentice model. The Institute's mission is preparing gifted students to transform the world creatively through art and design.

As an independent college, the Institute receives no financial support from city, county or federal governments with the exception of funds for student financial aid and periodic restricted grants in small amounts. Since 1946, the Institute has been accredited by what is now the National Association of Schools of Art and Design; and since 1964 by the North Central Association of Colleges and Schools.

#### ***Use of Estimates***

The preparation of financial statements in conformity with 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, 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 those estimates.

Significant estimates in the Institute's financial statements for the years ended June 30, 2016 and 2015 include receivable reserves, depreciation, investment valuations and government loan obligations.

#### ***Cash and Cash Equivalents***

The Institute considers all liquid investments with an original maturities of three months or less to be cash equivalents. As of June 30, 2016 and 2015, cash equivalents consisted primarily of bank deposits, money market accounts, overnight investments and federal agency discount notes.

At June 30, 2016, the Institute's cash accounts exceeded federally insured limits by approximately \$6,295,000. However, management monitors the financial stability of these financial institutions and believes the risk of loss is minimal.

#### ***Investments and Funds Held in Trusts by Others and Investment Return***

Investments in equity securities having a readily determinable fair value, all debt securities and funds held in trusts by others are carried at fair value. Investments in the Commonfund are recorded at the estimated net asset value per share, as a practical expedient, of the investments. Other investments and funds are valued at the lower of cost (or fair value at time of donation, if acquired by contribution) or fair value. Investment income return includes dividend, interest and

# **Kansas City Art Institute**

## **Notes to Financial Statements**

### **June 30, 2016 and 2015**

other investment income; realized and unrealized gains and losses on investments carried at fair value; and realized gains and losses on other investments.

Investment return that is initially restricted by donor stipulation and for which the restriction will be satisfied in the same year, is included in unrestricted net assets. Other investment return is reflected in the statements of activities as unrestricted, temporarily restricted or permanently restricted based upon the existence and nature of any donor or legally imposed restrictions.

The Institute maintains pooled investment accounts for its endowments. Investment income and realized and unrealized gains and losses from securities in the pooled investment accounts are allocated monthly to the individual endowments based on the relationship of the fair value of the interest of each endowment to the total fair value of the pooled investments accounts, as adjusted for additions to or deductions from those accounts.

#### ***Student Accounts and Notes Receivable***

Student accounts receivables are stated at the amounts billed to students less applied scholarships and loan proceeds. The Institute provides an allowance for doubtful accounts, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions.

Tuition is due at the beginning of the semester. Charges that are past due and have had no response to the due diligence process are assigned to third-party collection agencies. Delinquent receivables are written off based on individual credit evaluation and specific circumstances of the student.

Student loans receivable consists of amounts due under the Federal Perkins Loan Program and are stated at their outstanding principal amount, net of an allowance for doubtful notes. Perkins loans are made to students based on demonstrated financial need and satisfaction of federal eligibility requirements for the Federal Perkins Loan Program. Principal and interest payments on loans generally do not commence until after the borrower graduates or otherwise ceases enrollment. The Institute provides an allowance for doubtful notes which is based upon a review of outstanding loans, historical collection information and other existing conditions. Interest income is recorded as received which is not materially different from the amount that would have been recognized on the accrual basis. Loans that are delinquent continue to accrue interest. Loans that are past due for at least one payment are considered delinquent. Delinquent loans are written off based on individual credit evaluation and specific circumstances of the student.

#### ***Property and Equipment***

Property and equipment are stated at cost less accumulated depreciation. Depreciation is charged to expense over the estimated useful life of each asset, ranging from 3 to 40 years. Annual depreciation is primarily computed using the straight-line method. Physical plant and equipment have been recorded at cost with the exception of gifts, which are recorded at fair value at the date of donation.

The Institute 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. No interest was capitalized for the years ended June 30, 2016 and 2015.

# **Kansas City Art Institute**

## **Notes to Financial Statements**

### **June 30, 2016 and 2015**

#### ***Long-lived Asset Impairment***

The Institute 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 fair value.

Impairment losses of \$185,850 and \$50,079 were recognized for a building classified as held for sale for the years ended June 30, 2016 and 2015, respectively, based on the carrying value of the asset exceeding the fair value of the asset. The loss is included in plant operations and maintenance in the accompanying statements of activities. Fair value of the building was estimated to be \$600,000, which was determined based on the list price of the building.

#### ***Paintings and Works of Art***

The Institute has capitalized its paintings and works of art since its inception. If purchased, paintings and works of art are capitalized at cost and, if donated, they are capitalized at their appraised or fair value on the accession date (the date on which the item is accepted by the Board of Trustees). Gains or losses on de-accession of collection items are classified on the statement of activities as unrestricted or temporarily restricted support depending on donor restrictions, if any, placed on the item at the time of accession. Paintings and works of art are not depreciated.

The Institute's paintings and works of art are held for educational, research, scientific and curatorial purposes. Each of the items is cataloged, preserved and cared for, and the activities verifying their existence and assessing their condition are performed continuously.

#### ***Deferred Revenue***

Tuition revenues and fees are deferred and recognized over the periods to which the tuition and fees relate.

#### ***Net Assets***

Unrestricted net assets represent those net assets whose use is not restricted by donor-imposed stipulations. Temporarily restricted net assets are those whose use by the Institute has been limited by donors to a specific time period or purpose. Permanently restricted assets are those which are subject to the restrictions of gift instruments requiring that the principal be invested in perpetuity and the income only be utilized for purposes specified by the donor, if any.

#### ***Contributions, Gifts and Grants***

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

# **Kansas City Art Institute**

## **Notes to Financial Statements**

### **June 30, 2016 and 2015**

reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Gifts having donor stipulations that are satisfied in the period the gift is received are reported as unrestricted revenue and net assets.

Gifts of land, buildings, 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.

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.

#### ***Income Taxes***

The Internal Revenue Service has issued a determination letter that the Institute is a non-profit organization as defined under Section 501(c)(3) of the Internal Revenue Code and is exempt from income tax on related income. The Institute is subject to unrelated business income tax. The Institute files tax returns in the U.S. federal jurisdiction.

#### ***Functional Allocation of Expenses***

The costs of supporting the various programs and other activities have been summarized on a functional basis in the statements of activities. Certain costs have been allocated among the educational and general and auxiliary enterprises.

#### ***Transfers Between Fair Value Hierarchy Levels***

Transfers in and out of Level 1 (quoted market prices) and Level 2 (other significant observable inputs) are recognized on the period ending date.

#### ***Reclassifications***

Certain reclassifications have been made to the 2015 financial statements to conform to the 2016 financial statement presentation. These reclassifications had no effect on the increase in net assets.

# Kansas City Art Institute

## Notes to Financial Statements

June 30, 2016 and 2015

### Note 2: Student Loans Receivable

The Institute makes uncollateralized loans to students through its participation in the Federal Perkins Loan (FPL) program. The availability of funds under the FPL program is dependent on reimbursement to the loan fund from repayments on outstanding loans. Cumulative funds advanced by the federal government for the FPL program totaled \$1,466,383 as of June 30, 2016 and 2015. These advances are ultimately refundable to the federal government and are classified as liabilities in the statements of financial position along with any gains or losses allocated to the cumulative federal capital contributions. Outstanding loans canceled under the program result in a reduction of funds available for future loans and a decrease in the Institute's liability to the federal government. These loan amounts represent approximately 1.5% and 1.7% of total assets as of June 30, 2016 and 2015, respectively.

Allowances for doubtful accounts are established based on current economic factors and specific circumstances of the borrower which, in management's judgment, could influence the ability of the borrower to repay the amounts per the loan terms. For the FPL program, the federal government bears the risk of loss of uncollectible loans provided the Institute performs required collection due diligence procedures; therefore, no allowance for doubtful collections was recorded for the FPL program.

	<b>2016</b>	<b>2015</b>
Student loans receivable		
FPL program	\$ 1,707,335	\$ 1,737,511

The following tables represent the amounts past due under the Institute's student loan programs as of June 30, 2016 and 2015:

	<b>Less Than 120 Days Past Due</b>	<b>Greater Than 120 Days Past Due</b>	<b>Total Past Due</b>	<b>Current</b>	<b>Total Loans Receivable</b>
<b><u>June 30, 2016</u></b>					
Student loans receivable					
FPL program	\$ 133,763	\$ 411,389	\$ 545,152	\$1,278,246	\$ 1,823,398
Less interest and principal canceled	-	-	-	-	(116,063)
Total	<u>\$ 133,763</u>	<u>\$ 411,389</u>	<u>\$ 545,152</u>	<u>\$1,278,246</u>	<u>\$ 1,707,335</u>
<b><u>June 30, 2015</u></b>					
Student loans receivable					
FPL program	\$ 117,439	\$ 376,401	\$ 493,840	\$1,359,734	\$ 1,853,574
Less interest and principal canceled	-	-	-	-	(116,063)
Total	<u>\$ 117,439</u>	<u>\$ 376,401</u>	<u>\$ 493,840</u>	<u>\$1,359,734</u>	<u>\$ 1,737,511</u>

**Kansas City Art Institute**  
**Notes to Financial Statements**  
**June 30, 2016 and 2015**

**Note 3: Pledges Receivable**

Pledges receivable consisted of the following as of June 30, 2016 and 2015:

	<b>2016</b>	<b>2015</b>
Due within one year	\$ 7,525,398	\$ 3,351,231
Due in one to five years	5,293,219	5,214,908
In excess of five years	773,781	735,092
	<u>13,592,398</u>	<u>9,301,231</u>
Less		
Unamortized discount on pledges	306,787	165,319
Allowance for doubtful pledge	<u>3,200,000</u>	<u>3,200,000</u>
	<u><u>\$ 10,085,611</u></u>	<u><u>\$ 5,935,912</u></u>

Unconditional pledges receivable are recognized at a discounted value of anticipated future cash flows using a discount rate of 3.50% and 3.25% at June 30, 2016 and 2015, respectively.

During 2015, the Institute was notified of a significant gift which was transferred to a community foundation (the "Foundation") totaling approximately \$25,230,000. This gift is designated by the original donor to support the Institute. The gift has three separate components as outlined below:

- An endowment fund for general operations – According to the Endowment Fund for Kansas City Art Institute Establishing Document dated May 25, 2015, the Foundation is to transfer 4.5% of the average past three year-end fund balances to the Institute for general operations, with the first distribution due during the fiscal year ending June 30, 2016. The estimated value of this fund as of June 30, 2016 and 2015, was \$14,160,000 and \$14,230,000, respectively. The donor provided the Foundation's Board with variance power to redirect the funds to other not-for-profit organizations as appropriate. The Institute will recognize the gift income from the fund when each distribution is approved by the Foundation Board. However, in the event of extraordinary circumstances, or if the Foundation determines the Institute is in a position to manage the funds, the Foundation may recommend the principal of the Fund, up to the entire Fund balance, be distributed to the Institute. The Institute received the first annual contribution of approximately \$648,000 during the year ended June 30, 2016, and is included in unrestricted contributions in the statement of activities.

# Kansas City Art Institute

## Notes to Financial Statements

### June 30, 2016 and 2015

- A campus improvement grant – According to the Grant Document dated May 25, 2015, the Foundation is to distribute \$5,000,000 for campus improvements, primarily for deferred maintenance, to be administered by a committee of the Institute’s board of directors. The Institute recorded a contribution and related pledge receivable of \$5,000,000 during 2015, related to this grant. The Institute received approximately \$228,000 for capital improvements made during the year ended June 30, 2016.
- A \$2 for \$1 challenge grant – According to the Challenge Grant Document dated May 27, 2015, the Foundation is to distribute \$6,000,000 to the Institute to be used for endowing the president, professors and scholarships contingent upon the Institute satisfying certain fundraising requirements. During the year ended June 30, 2016, the Institute raised approximately \$2,965,000 in committed donations, allowing the Institute to record approximately \$5,930,000 in matching contributions based on the conditions of the grant. These contributions are included in permanently restricted contributions in the statement of activities.

#### **Note 4: Investments and Funds Held in Trust by Others and Investment Return**

Investments are stated at fair value as of June 30, 2016 and 2015. The following identifies the major categories of investments:

	<b>2016</b>	<b>2015</b>
Money market funds	\$ 1,872,134	\$ 760,406
Mutual funds		
Vanguard intermediate term	7,130,560	6,601,231
Commerce Bond Fund	3,873,335	-
Other mutual funds	6,978,719	10,978,305
Common stock	6,894,129	7,868,743
Exchange traded funds	2,797,104	3,985,783
U.S. Government agency obligations	39,853	75,501
Commonfund Government Money Market Fund	-	11,850
Commonfund Multi-Strategy Equity Fund	23,547,029	21,653,021
Commonfund Multi-Strategy Bond Fund	11,305,075	9,847,504
	<hr/>	<hr/>
Total investments	<u>\$ 64,437,938</u>	<u>\$ 61,782,344</u>

The Institute’s temporarily and permanently restricted net assets include various endowment funds established by donors. The fair value of the assets of some of these funds was \$22,417 and \$55,667 less than the level required by donor stipulation or law at June 30, 2016 and 2015, respectively, (see *Note 10*).

**Kansas City Art Institute**  
**Notes to Financial Statements**  
**June 30, 2016 and 2015**

***Funds Held in Trust by Others***

	<b>2016</b>	<b>2015</b>
Funds held in trust by others	\$ 2,401,821	\$ 2,472,767

The Institute records its percentage interest in the fair value of these Trust assets as permanently restricted or temporarily restricted net assets based on the restrictions set by the donor, which approximates the present value of the estimated futures cash receipts, in accordance with ASC 958, *Transfers of Assets to a Not-for-Profit Institute or Charitable Trust that Raises or Holds Contributions for Others*. The annual interest and dividend distributions received from these Trust assets are recognized as a component of endowment interest and dividends in the statements of activities, in accordance with the donor's intention.

Total investment return during the years ended June 30, 2016 and 2015 consisted of the following:

	<b>2016</b>	<b>2015</b>
Interest and dividend income	\$ 1,444,114	\$ 883,277
Net realized and unrealized gains (losses) on investments	(1,324,836)	1,162,648
Net realized and unrealized losses on funds held in trusts by others	(70,946)	(152,306)
	<u>\$ 48,332</u>	<u>\$ 1,893,619</u>

**Note 5: Property and Equipment**

Property and equipment consisted of the following as of June 30:

	<b>2016</b>	<b>2015</b>
Land	\$ 2,270,581	\$ 1,970,580
Buildings and improvements	32,836,489	31,130,659
Equipment, furniture and fixtures	8,361,227	8,078,506
Construction in progress	3,642,690	222,893
	<u>47,110,987</u>	<u>41,402,638</u>
Less accumulated depreciation	22,815,539	21,800,270
	<u>\$ 24,295,448</u>	<u>\$ 19,602,368</u>

At June 30, the Institute had approximately \$2,750,000 in outstanding contracts with related parties on various construction projects.



# Kansas City Art Institute

## Notes to Financial Statements

### June 30, 2016 and 2015

#### Note 6: Bonds Payable

Bonds payable consisted of the following as of June 30:

	<u>2016</u>	<u>2015</u>
Health and Educational Facilities Authority of the State of Missouri, variable rate Demand Educational Facilities Revenue Bonds, Series 2005; principal due December 31, 2035; interest is payable monthly at the MOHEFA variable rate, which was 0.44% and 0.05% at June 30, 2016 and 2015, respectively, this variable interest rate cannot exceed 12%.	<u>\$ 10,500,000</u>	<u>\$ 10,500,000</u>

The Institute maintains a letter-of-credit facility, which expires on December 5, 2016, that permits the trustee to draw an amount up to the principal amount outstanding should the Series 2005 bonds not be remarketed and become due. If the letter-of-credit is drawn upon, the Institute would be required to repay the "Bank Bonds" by the expiration date of the letter-of-credit at an interest rate of prime plus 2%.

The 2005 series bond agreement, among other provisions, contains certain nonfinancial and financial covenants, which includes the requirement that the Institute maintains liquid assets, plus capital campaign pledges that total at least 125% of the amount of the outstanding letter of credit securing the bonds. Management believes the Institute was in compliance with these covenants at June 30, 2016 and 2015.

Minimum annual principal payments on the loans and bonds payable as of June 30, 2016 are as follows:

2035	<u>\$ 10,500,000</u>
------	----------------------

The Institute also has two line-of-credit agreements with a financial institution. Total borrowings available on these lines totals \$3,500,000. Any outstanding borrowings bear interest at bank's prime rate for amounts borrowed up to \$1,000,000, and for amounts over \$1,000,000 the interest rate is the bank's prime rate minus one-half percent. Both notes have a maturity date of January 31, 2017. No borrowings were outstanding on these lines as of June 30, 2016 and 2015.

**Kansas City Art Institute**  
**Notes to Financial Statements**  
**June 30, 2016 and 2015**

**Note 7: Net Assets**

***Temporarily Restricted Net Assets***

Temporarily restricted net assets at June 30 are available for the following purposes or periods:

	<b>2016</b>	<b>2015</b>
Capital projects	\$ 7,689,544	\$ 5,021,019
Scholarships	12,061,206	13,977,594
Funds held in trust	466,898	429,854
Faculty chairs	925,340	966,312
General operations	3,611,159	4,414,470
	<u>\$ 24,754,147</u>	<u>\$ 24,809,249</u>

***Permanently Restricted Net Assets***

Permanently restricted net assets at June 30 are restricted to provide income for:

	<b>2016</b>	<b>2015</b>
Student scholarships	\$ 5,215,113	\$ 2,627,057
Faculty chairs	3,500,000	1,500,000
Presidential chair	1,500,000	-
General operations	32,263,664	29,522,370
Funds held in trust	1,934,923	2,042,913
	<u>\$ 44,413,700</u>	<u>\$ 35,692,340</u>

***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.

	<b>2016</b>	<b>2015</b>
Capital projects	\$ 768,996	\$ -
Scholarships	137,912	1,800,272
Faculty chairs	1,647,837	101,239
General operations	266,024	405,110
	<u>\$ 2,820,769</u>	<u>\$ 2,306,621</u>

# Kansas City Art Institute

## Notes to Financial Statements

### June 30, 2016 and 2015

#### **Note 8: Retirement Plan**

The Institute participates in a multi-employer defined contribution retirement plan administered by the Teachers Insurance and Annuity Association ("TIAA") for eligible personnel. Employee benefits under this plan call for payments at retirement based on the accumulated values in the individual participants' accounts. Employees may elect to defer a percentage of their compensation for contribution to the plan, of which the Institute will match a certain portion of such employee contributions. Total contributions by the Institute were \$324,404 and \$281,910 for the years ended June 30, 2016 and 2015, respectively.

#### **Note 9: Disclosures About Fair Value of Assets**

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
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets; 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
- Level 3** Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets

**Kansas City Art Institute**  
**Notes to Financial Statements**  
**June 30, 2016 and 2015**

***Recurring Measurements***

The following tables present the fair value measurements of assets and liabilities recognized in the accompanying 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 at June 30, 2016 and 2015:

		2016	
		Fair Value Measurements Using	
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
	Fair Value		
Investments			
Money market funds	\$ 1,872,134	\$ 1,872,134	\$ -
Mutual funds			
Vanguard intermediate term fund	7,130,560	7,130,560	-
Commerce bond fund	3,873,335	3,873,335	-
Other mutual funds	6,978,719	6,978,719	-
Common stock	6,894,129	6,894,129	-
Exchange traded funds	2,797,104	2,797,104	-
U.S. Government agency obligations	39,853	-	39,853
Commonfund Multi-Strategy Equity Fund measured at net asset value (A)	23,547,029	-	-
Commonfund Multi-Strategy Bond Fund measured at net asset value (A)	11,305,075	-	-
Total investments	64,437,938	29,545,981	39,853
Funds Held In Trusts by Others	2,401,821	-	2,401,821
Total fair value of recurring measurements	\$ 66,839,759	\$ 29,545,981	\$ 2,441,674

**Kansas City Art Institute**  
**Notes to Financial Statements**  
**June 30, 2016 and 2015**

		2015	
		Fair Value Measurements Using	
		Quoted Prices	
		in Active	Significant
		Markets for	Other
		Identical	Observable
		Assets	Inputs
	Fair Value	(Level 1)	(Level 2)
Investments			
Money market funds	\$ 760,406	\$ 760,406	\$ -
Mutual funds			
Vanguard intermediate term fund	6,601,231	6,601,231	-
Other mutual funds	10,978,305	10,978,305	-
Common stock	7,868,743	7,868,743	-
Exchange traded funds	3,985,783	3,985,783	-
U.S. Government agency obligations	75,501	-	75,501
Commonfund Government Money Market			
Fund measured at net asset value (A)	11,850	-	-
Commonfund Multi-Strategy Equity Fund			
measured at net asset value (A)	21,653,021	-	-
Commonfund Multi-Strategy Bond Fund			
measured at net asset value (A)	9,847,504	-	-
Total investments	61,782,344	30,194,468	75,501
Funds Held In Trusts by Others	2,472,767	-	2,472,767
Total fair value of			
recurring measurements	\$ 64,255,111	\$ 30,194,468	\$ 2,548,268

(A) Certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts included above are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statements of financial position.

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying 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 year ended June 30, 2016.

# Kansas City Art Institute

## Notes to Financial Statements

### June 30, 2016 and 2015

#### ***Investments and Funds Held in Trust***

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projection and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. The Institute holds no Level 3 securities.

#### ***Commonfund Investments***

The fair value of the Commonfund government money market fund, multi-strategy equity and bond funds has been estimated using the net asset value per share as a practical expedient for the investments. Commonfund investments held at June 30 consist of the following:

	<b>Fair Value</b>	<b>Unfunded Commitments</b>	<b>Redemption Frequency</b>	<b>Redemption Notice Period</b>
<b><u>June 30, 2016</u></b>				
Commonfund Multi-Strategy Equity Fund (A)	\$23,547,029	Not Applicable	Limited to monthly redemption	5 days
Commonfund Multi-Strategy Bond Fund (A)	11,305,075	Not Applicable	Limited to monthly redemption	5 days
<b><u>June 30, 2015</u></b>				
Commonfund Multi-Strategy Equity Fund (A)	\$21,653,021	Not Applicable	Limited to monthly redemption	5 days
Commonfund Multi-Strategy Bond Fund (A)	9,847,504	Not Applicable	Limited to monthly redemption	5 days
Commonfund Government Money Market Fund (A)	11,850	Not Applicable	Daily	1 day

- (A) The investments in common trust funds permit the commingling or pooling of investor's money into one account (known as Commonfund) for the purpose of creating a single investment. Common trust funds strike a net asset value on a periodic basis and have varying investment strategies that primarily include investments in traditional assets such as domestic and international equity, fixed income securities and other securities. The Funds' investments are subject to various risk factors arising from the investment activities of the underlying vehicles including market, credit and currency risk. A determination of net asset value per share is made as a practical expedient and these commonfund investments asset value is considered to be the fair value for the commonfund investments.

# Kansas City Art Institute

## Notes to Financial Statements

### June 30, 2016 and 2015

#### ***Nonrecurring Measurements***

The following table presents the fair value measurement of assets and liabilities measured at fair value on a nonrecurring basis and the level within the fair value hierarchy in which the fair value measurements fall at June 30, 2016 and 2015:

		<b>Fair Value Measurements Using</b>	
		<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>
	<b>Fair Value</b>		
<b><u>June 30, 2016</u></b>			
Assets held for sale	\$ 600,000	\$ -	\$ 600,000
<b><u>June 30, 2015</u></b>			
Assets held for sale	\$ 785,850	\$ -	\$ 785,850

Following is a description of the valuation methodologies and inputs used for assets and liabilities measured at fair value on a nonrecurring basis and recognized in the accompanying statements of financial position, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy.

#### ***Assets Held for Sale***

Assets held for sale are valued at fair value on June 30, 2016 and 2015, due to an impairment recorded. The fair value is estimated based on the listing price of the assets, which is a quoted price in an active market for similar comparable assets, therefore, is classified within Level 2 of the valuation hierarchy.

#### **Note 10: Endowment**

##### ***Interpretation of State Law***

The Institute's endowment consists of approximately 100 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the governing body to function as endowments (board-designated endowment funds). As required by accounting principles generally accepted in the United States of America (GAAP), net assets associated with endowment funds, including board-designated endowment funds, are classified and reported based on the existence or absence of donor-imposed restrictions.

# Kansas City Art Institute

## Notes to Financial Statements

June 30, 2016 and 2015

The Institute's governing body has interpreted the State of Missouri 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, the Institute 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 the Institute in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, the Institute considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. Duration and preservation of the fund
2. Purposes of the Institute 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 the Institute
7. Investment policies of the Institute

The composition of net assets by type of endowment fund at June 30, 2016 and 2015 was:

<b>2016</b>				
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Donor-restricted endowment funds	\$ (22,417)	\$ 16,162,480	\$ 37,515,560	\$ 53,655,623
Board-designated endowment funds	3,176,686	-	-	3,176,686
Total endowment funds	<u>\$ 3,154,269</u>	<u>\$ 16,162,480</u>	<u>\$ 37,515,560</u>	<u>\$ 56,832,309</u>
<b>2015</b>				
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Donor-restricted endowment funds	\$ (55,667)	\$ 18,484,872	\$ 32,555,200	\$ 50,984,405
Board-designated endowment funds	3,505,912	-	-	3,505,912
Total endowment funds	<u>\$ 3,450,245</u>	<u>\$ 18,484,872</u>	<u>\$ 32,555,200</u>	<u>\$ 54,490,317</u>



**Kansas City Art Institute**  
**Notes to Financial Statements**  
**June 30, 2016 and 2015**

Changes in endowment net assets for the years ended June 30, 2016 and 2015 were:

	<b>2016</b>			<b>Total</b>
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	
Endowment net assets, beginning of year	\$ 3,450,245	\$ 18,484,872	\$ 32,555,200	\$ 54,490,317
Total investment return	(148,040)	(442,517)	-	(590,557)
Addition of contributions and collections on pledges	-	-	4,960,360	4,960,360
Appropriation of endowment assets for expenditure	<u>(147,936)</u>	<u>(1,879,875)</u>	<u>-</u>	<u>(2,027,811)</u>
Endowment net assets, end of year	<u>\$ 3,154,269</u>	<u>\$ 16,162,480</u>	<u>\$ 37,515,560</u>	<u>\$ 56,832,309</u>

	<b>2015</b>			<b>Total</b>
	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	
Endowment net assets, beginning of year	\$ 3,571,205	\$ 18,878,610	\$ 32,509,585	\$ 54,959,400
Total investment return	15,636	1,343,988	(46,497)	1,313,127
Addition of contributions and collections on pledges	-	-	92,112	92,112
Appropriation of endowment assets for expenditure	<u>(136,596)</u>	<u>(1,737,726)</u>	<u>-</u>	<u>(1,874,322)</u>
Endowment net assets, end of year	<u>\$ 3,450,245</u>	<u>\$ 18,484,872</u>	<u>\$ 32,555,200</u>	<u>\$ 54,490,317</u>

Included in the 2016 and 2015 temporarily restricted net assets above is a donation the Institute received in previous years for scholarships which management designated as a term-endowment during 2014.

# Kansas City Art Institute

## Notes to Financial Statements

### June 30, 2016 and 2015

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

	<u>2016</u>	<u>2015</u>
Permanently restricted net assets – portion of perpetual endowment funds required to be retained permanently by explicit donor stipulation on SPMIFA	\$ 37,515,560	\$ 32,555,200
Permanently restricted net assets not subject to the Institute’s investment policies consisting of pledges, perpetual trusts held by others and other assets	<u>6,898,140</u>	<u>3,137,140</u>
	<u>\$ 44,413,700</u>	<u>\$ 35,692,340</u>

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level the Institute is required to retain as a fund of perpetual duration pursuant to donor stipulation or SPMIFA. In accordance with accounting principles generally accepted in the United States of America, deficiencies of this nature are reported in unrestricted net assets and aggregated \$22,417 and \$55,667 at June 30, 2016 and 2015, respectively. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after investment of new permanently restricted contributions and continued appropriation for certain purposes that was deemed prudent by the governing body.

The Institute 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 the Institute must hold in perpetuity or for donor-specified periods, as well as those of board-designated endowment funds. Under the Institute’s policies, endowment assets are invested in a manner that is intended to produce results that meet or exceed S&P 500 Performance over a three to five-year market cycle, while assuming a low level of investment risk. The Institute expects its endowment funds to provide an average rate of return of approximately 6% annually over time. Actual returns in any given year may vary from this amount.

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

# **Kansas City Art Institute**

## **Notes to Financial Statements**

### **June 30, 2016 and 2015**

For operational purposes, the Board of Trustees annually directs that a percentage of the previous twelve quarters' average fair value of investments held for endowment purposes be allocated as a distribution of endowment investment income for current operations. For the years ended June 30, 2016 and 2015, such percentage was 4.5% and the allocation totaled \$1,879,875 and \$1,737,726, respectively. In establishing this policy, the Institute considered the long-term expected return on its endowment. Accordingly, over the long term, the Institute expects the current spending policy to allow its endowment to grow. This is consistent with the Institute's objective to maintain the purchasing power of endowment assets held in perpetuity or for a specified term, as well as to provide additional real growth through new gifts and investment return.

#### **Note 11: Significant Estimates and Concentrations**

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

##### ***Contributions***

Approximately 36% and 67% of all contributions, respectively, were received from one donor during 2016 and 2015.

##### ***General Litigation***

The Institute is subject to claims and lawsuits that arise primarily in the ordinary course of business. 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 of the Institute. No accrual for any potential losses, if any, has been included in these financial statements.

##### ***Allowance for Uncollectible Receivables***

Significant estimates used in determining the allowance for uncollectible student accounts and loans receivable are described in *Note 1*. Management believes the remaining net outstanding pledges receivable balances are collectible as of June 30, 2016. This estimate could materially change in future periods due to unforeseen events and circumstances.

##### ***Depreciation***

As described in *Note 1*, depreciation is charged to expense using the straight-line method over the estimated useful life of each asset, which ranges from three to forty years.

# **Kansas City Art Institute**

## **Notes to Financial Statements**

### **June 30, 2016 and 2015**

#### ***Refundable Government Student Loan Program***

As discussed in *Note 1*, allowances for doubtful accounts are established based on current economic factors and specific circumstances of the borrower which, in management's judgment, could influence the ability of the borrower to repay the amounts per the loan terms. For the FPL program, the federal government bears the risk of loss of uncollectible loans provided the Institute performs required collection due diligence procedures.

#### ***Investments***

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

#### **Note 12: Subsequent Events**

Subsequent events have been evaluated through the date of the Independent Auditor's Report, which is the date the financial statements were available to be issued.