

Kansas City Art Institute

Auditor's Report and Financial Statements

June 30, 2014 and 2013



Kansas City Art Institute

June 30, 2014 and 2013

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Independent Auditor's Report

Board of Trustees
Kansas City Art Institute
Kansas City, Missouri

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, 2014 and 2013, 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
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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Institute as of June 30, 2014 and 2013, 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 13, 2014

Kansas City Art Institute
Statements of Financial Position
June 30, 2014 and 2013

Assets

	2014	2013
Cash and cash equivalents	\$ 6,074,278	\$ 8,435,424
Restricted cash	<u>321,738</u>	<u>377,259</u>
Total cash and cash equivalents	<u>6,396,016</u>	<u>8,812,683</u>
Receivables		
Student accounts receivable and other miscellaneous receivables, net of allowance, 2014 - \$187,770, 2013 - \$162,443	112,310	110,270
Student loans receivable	1,745,187	1,750,097
Pledges receivable, net of allowance 2014 and 2013 - \$3,200,000	<u>1,302,931</u>	<u>1,658,459</u>
Total net receivables	3,160,428	3,518,826
Art store inventory	289,056	307,817
Prepaid expenses and other assets	204,205	153,855
Investments	62,110,653	54,720,607
Funds held in trust by others	2,625,073	2,361,906
Property and equipment, net	20,824,088	21,057,210
Paintings and works of art	<u>947,962</u>	<u>939,173</u>
Total assets	<u><u>\$ 96,557,481</u></u>	<u><u>\$ 91,872,077</u></u>

Liabilities and Net Assets

Liabilities

Accounts payable and accrued expenses	\$ 1,698,032	\$ 1,952,830
Deferred revenue	423,428	590,449
Loans and bonds payable	10,500,000	12,765,540
Refundable loan program	<u>1,846,286</u>	<u>1,841,021</u>
Total liabilities	<u>14,467,746</u>	<u>17,149,840</u>

Net Assets

Unrestricted	26,355,546	24,680,366
Temporarily restricted	20,015,007	14,909,710
Permanently restricted	<u>35,719,182</u>	<u>35,132,161</u>
Total net assets	<u>82,089,735</u>	<u>74,722,237</u>
Total liabilities and net assets	<u><u>\$ 96,557,481</u></u>	<u><u>\$ 91,872,077</u></u>

Kansas City Art Institute
Statements of Activities
Years Ended June 30, 2014 and 2013

		2014		
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, Gains and Other Support				
Student tuition and fees	\$ 23,438,313			\$ 23,438,313
Less institutional financial aid	(11,004,714)			(11,004,714)
	12,433,599			12,433,599
Summer and continuing education	1,134,099			1,134,099
Interest and dividend income	743,026			743,026
Contributions, gifts and grants	1,455,723	\$ 257,104	\$ 82,486	1,795,313
Net realized and unrealized gains on investments and funds held in trust by others	2,135,409	5,995,230	504,535	8,635,174
Auxiliary enterprises	1,635,751			1,635,751
Net assets released from restrictions	1,147,037	(1,147,037)		-
Total revenues, gains and other support	20,684,644	5,105,297	587,021	26,376,962
Expenses				
Program services				
Instruction	4,197,432			4,197,432
Academic support	2,004,642			2,004,642
Summer and continuing education	985,725			985,725
Student services	1,744,201			1,744,201
Auxiliary enterprises	1,047,058			1,047,058
Support services				
General administration	1,272,356			1,272,356
Fundraising	712,011			712,011
General institutional	4,168,643			4,168,643
Plant operations and maintenance	2,877,396			2,877,396
Total expenses	19,009,464			19,009,464
Change in Net Assets	1,675,180	5,105,297	587,021	7,367,498
Net Assets, Beginning of Year	24,680,366	14,909,710	35,132,161	74,722,237
Net Assets, End of Year	\$ 26,355,546	\$ 20,015,007	\$ 35,719,182	\$ 82,089,735

See Notes to Financial Statements

	2013			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, Gains and Other Support				
Student tuition and fees	\$ 25,308,236			\$ 25,308,236
Less institutional financial aid	(12,142,437)			(12,142,437)
	13,165,799			13,165,799
Summer and continuing education	1,139,210			1,139,210
Interest and dividend income	797,374			797,374
Contributions, gifts and grants	1,744,388	\$ 301,436	\$ 74,679	2,120,503
Net realized and unrealized gains on investments and funds held in trust by others	445,554	4,830,766	221,027	5,497,347
Auxiliary enterprises	1,775,990			1,775,990
Other	66,784			66,784
Net assets released from restrictions	1,397,101	(1,397,101)		-
Total revenues, gains and other support	20,532,200	3,735,101	295,706	24,563,007
Expenses				
Program services				
Instruction	4,283,392			4,283,392
Academic support	2,035,009			2,035,009
Summer and continuing education	1,059,853			1,059,853
Student services	1,727,460			1,727,460
Auxiliary enterprises	1,130,616			1,130,616
Support services				
General administration	1,186,295			1,186,295
Fundraising	787,970			787,970
General institutional	4,011,365			4,011,365
Plant operations and maintenance	2,894,955			2,894,955
Total expenses	19,116,915			19,116,915
Change in Net Assets	1,415,285	3,735,101	295,706	5,446,092
Net Assets, Beginning of Year	23,265,081	11,174,609	34,836,455	69,276,145
Net Assets, End of Year	\$ 24,680,366	\$ 14,909,710	\$ 35,132,161	\$ 74,722,237

Kansas City Art Institute

Statements of Cash Flows

Years Ended June 30, 2014 and 2013

	2014	2013
Operating Activities		
Change in net assets	\$ 7,367,498	\$ 5,446,092
Items not requiring (providing) cash		
Depreciation and amortization	725,584	961,448
Net realized and unrealized gains on investments and funds held in trust by others	(8,635,174)	(5,497,347)
Discount on pledges receivable	(46,119)	(9,149)
Contributions and investment income restricted for long-term investment	(82,486)	(176,526)
Donated works of art	(8,789)	-
Changes in		
Accounts receivable	(2,040)	(67,555)
Pledges receivable	301,647	255,342
Art store inventory	18,761	(14,171)
Prepaid expenses and other assets	(50,350)	33,997
Accounts payable and accrued expenses	(254,798)	(795,845)
Deferred revenue	(167,021)	334,413
Net cash provided by (used in) operating activities	<u>(833,287)</u>	<u>470,699</u>
Investing Activities		
Purchases of property and equipment	(492,462)	(1,586,387)
Purchases of investments	(6,063,548)	(4,020,867)
Sales of investments	7,045,509	4,314,632
Net change in student loans receivable	<u>4,910</u>	<u>(6,722)</u>
Net cash provided by (used in) investing activities	<u>494,409</u>	<u>(1,299,344)</u>
Financing Activities		
Net increase in refundable loan programs	5,265	17,997
Payments on loans and bonds	(2,265,540)	(70,789)
Proceeds from issuance of notes payable to bank	-	1,065,045
Changes in pledges receivable restricted for long-term investment	100,000	146,660
Contributions and investment income restricted for long-term investment	<u>82,486</u>	<u>176,526</u>
Net cash provided by (used in) financing activities	<u>(2,077,789)</u>	<u>1,335,439</u>
Increase (Decrease) in Cash and Cash Equivalents	<u>(2,416,667)</u>	<u>506,794</u>
Cash and Cash Equivalents, Beginning of Year	<u>8,812,683</u>	<u>8,305,889</u>
Cash and Cash Equivalents, End of Year	<u><u>\$ 6,396,016</u></u>	<u><u>\$ 8,812,683</u></u>
Supplemental Cash Flow Information		
Cash paid for interest	\$ 75,293	\$78,341

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

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 four-year college of visual art and design granting a Bachelor of Fine Arts degree. 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 Mission of the Institute as adopted by the Board of Trustees on March 13, 1990, is as follows:

“The mission of Kansas City Art Institute is to be a leader in the visual arts and design education by preparing gifted students for lifelong creativity through intensive interaction with preeminent faculty and facilities, and by stimulating active public awareness, support and participation in the visual arts 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.

Cash and Cash Equivalents

The Institute considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. As of June 30, 2014 and 2013, cash equivalents consisted primarily of bank deposits, money market accounts, overnight investments and federal agency discount notes.

At June 30, 2014, the Institute's cash accounts exceeded federally insured limits by approximately \$105,000.

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.

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

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.

Inventories

Inventories consist of merchandise and other items held for resale. The inventories are recorded at the lower of cost or market using the first-in, first-out method.

Investments and Funds Held in Trust by Others

Investments and funds held in trust in equity securities having a readily determinable fair value and all debt securities are carried at fair value. 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 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.

Property and Equipment

Property and equipment are depreciated over the estimated useful life of each asset, ranging from 10 to 40 years. Depreciation is 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.

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

Long-lived Asset Improvement

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. No asset impairment was recognized during the years ended June 30, 2014 and 2013.

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 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.

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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 Institute is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code, as provided by a determination letter from the Internal Revenue Service. As such, the Institute is generally exempt from income taxes; however, certain income is considered unrelated business income and is subject to taxation.

With few exceptions, the Institute is no longer subject to U.S. federal examinations by tax authorities for years before 2011.

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.

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.

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

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, 2014 and 2013. These advances along with allocated cumulative gains/losses are ultimately refundable to the federal government and are classified as liabilities in the statements of financial position. Outstanding loans canceled under the program result in a reduction of funds available for future loans. These loan amounts represent approximately 2% of total assets as of June 30, 2014 and 2013.

The Institute also makes uncollateralized loans to students through institutional loan funds. These loans are generally based on financial need.

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. As of June 30, 2014 and 2013, management did not feel that there was a need for an allowance for doubtful accounts relating to institutional student loan receivables. 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. The Institute does not stop the accrual of interest until a loan is written off; therefore, the Institute has no loans on nonaccrual status.

	<u>2014</u>	<u>2013</u>
Student loans receivable		
FPL program	\$ 1,745,187	\$ 1,741,320
Institutional programs	<u>-</u>	<u>8,777</u>
Total student loans receivable	<u><u>\$ 1,745,187</u></u>	<u><u>\$ 1,750,097</u></u>

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

The following tables represent the amounts past due under the Institute's student loan programs as of June 30, 2014 and 2013:

2014					
	Less Than 120 Days Past Due	Greater Than 120 Days Past Due	Total Past Due	Current	Total Loans Receivable
Student loans receivable					
FPL program	\$ 89,318	\$ 378,195	\$ 467,513	\$1,393,682	\$ 1,861,195
Institutional programs	-	-	-	-	-
Less interest and principal cancelled	-	-	-	-	(116,008)
Total	<u>\$ 89,318</u>	<u>\$ 378,195</u>	<u>\$ 467,513</u>	<u>\$1,393,682</u>	<u>\$ 1,745,187</u>

2013					
	Less Than 120 Days Past Due	Greater Than 120 Days Past Due	Total Past Due	Current	Total Loans Receivable
Student loans receivable					
FPL program	\$ 93,335	\$ 367,124	\$ 460,459	\$1,396,869	\$ 1,857,328
Institutional programs	-	-	-	8,777	8,777
Less interest and principal cancelled	-	-	-	-	(116,008)
Total	<u>\$ 93,335</u>	<u>\$ 367,124</u>	<u>\$ 460,459</u>	<u>\$1,405,646</u>	<u>\$ 1,750,097</u>

Note 3: Pledges Receivable

Pledges receivable consisted of the following as of June 30, 2014 and 2013:

	2014	2013
Due within one year	\$ 3,621,397	\$ 3,673,480
Due in one to five years	314,908	664,908
In excess of five years	735,092	734,656
	<u>4,671,397</u>	<u>5,073,044</u>
Less		
Unamortized discount on pledges	168,466	214,585
Allowance for doubtful pledge	3,200,000	3,200,000
	<u>\$ 1,302,931</u>	<u>\$ 1,658,459</u>

Unconditional pledges receivable are recognized at a discounted value of anticipated future cash flows using a discount rate of 3.25% at June 30, 2014 and 2013.

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

Approximately \$1,250,000 and \$1,500,000 of the gross outstanding pledges receivable as of June 30, 2014 and 2013, respectively, were due from members of the Institute's Board of Trustees or their affiliated entities.

Note 4: Investments and Funds Held in Trust by Others

Investments are stated at fair value as of June 30, 2014 and 2013. The following identifies the major categories of investments:

	2014	2013
Money market funds	\$ 684,164	\$ 276,812
Mutual funds		
Vanguard intermediate term	3,340,050	3,281,809
Other mutual funds	13,980,548	9,786,795
Common stock	8,111,035	6,986,697
Exchange traded funds	4,295,729	5,297,114
U.S. Government agency obligations	116,120	1,433,622
Commonfund Government Money Market Fund	11,850	11,850
Commonfund Multi-Strategy Equity Fund	21,431,419	17,773,481
Commonfund Multi-Strategy Bond Fund	10,139,738	9,872,427
Total investments	<u>\$ 62,110,653</u>	<u>\$ 54,720,607</u>

Commonfund Government Money Market Fund, Multi-Strategy Equity and Bond Funds

The fair value of the Commonfund investments has been estimated using the net asset value per share of the investments. The Commonfund investments held at June 30 consist of the following:

		June 30, 2014		
	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Commonfund Multi-Strategy Equity Fund	\$ 21,431,419	Not Applicable	Limited to monthly redemption	5 days
Commonfund Multi-Strategy Bond Fund	10,139,738	Not Applicable	Limited to monthly redemption	5 days
Commonfund Government Money Market Fund	11,850	Not Applicable	Daily	1 day

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Notes to Financial Statements

June 30, 2014 and 2013

			June 30, 2013		
	Fair Value		Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Commonfund Multi-Strategy Equity Fund	\$ 17,773,481		Not Applicable	Limited to monthly redemption	5 days
Commonfund Multi-Strategy Bond Fund	9,872,427		Not Applicable	Limited to monthly redemption	5 days
Commonfund Government Money Market Fund	11,850		Not Applicable	Daily	1 day

As of June 30, 2014 and 2013, the Institute held \$31,583,007 and \$27,657,758, respectively, in common trust funds, which permit the commingling or pooling of investors' money into one account (known as Commonfund) for the purpose of creating a single investment. Because they are a bank product, common trust funds are not considered to be a security under state and federal securities laws. Much like mutual funds, 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 Institute's investments in common trust multi-strategy equity and multi-strategy bond funds can be redeemed monthly with five business days' notice. The Institute's investments in common trust governmental money market funds can be redeemed daily with one day's notice.

These Funds have investments in certain securities, limited partnerships and other investment funds, for which market quotations may not be readily available. Such investments have been valued in accordance with the Commonfund's valuation policies. Those estimated values may differ significantly from the values that would have been used had a ready market for the investments existed, and the differences could be material. Additionally, certain investments in limited partnerships, investment funds and other debt instruments may be restricted as to resale or may require advance notice for redemption or withdrawal.

The Funds' investments in partnerships are subject to various risk factors arising from the investment activities of the underlying vehicles including market, credit and currency risk. Certain investment partnerships owned by the Funds transact in short sales and various domestic and international derivative investments, including forward foreign currency contracts, futures, written and purchased options and swaps, exposing the investment partnership to market risk in excess of the amounts recorded in their financial statements. In addition, credit risk arises from certain options, forwards and swaps from potential counterparty nonperformance. The Funds' risk of loss in any of its investment partnerships is limited to the value of the investment, including any unfunded commitments. The Institute's risk of loss is limited to the value of its investment.

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

The Funds also invest in securities of foreign companies which involve special risks including revaluation of currency and future adverse political and economic developments. Moreover, securities of many foreign companies and their markets may be less liquid, and their prices more volatile, than those of comparable U.S. companies. In the case of a foreign market event that may materially impact the closing prices of foreign exchange-traded securities, Commonfund, in consultation with the Custodian and the applicable Sub-adviser(s), will determine fair value for the affected securities.

The Funds also invest in mortgage-backed securities including collateralized mortgage obligations. Yields on mortgage-backed securities are affected by interest and prepayment rates which, in turn, are influenced by a variety of economic, geographical, social and other factors. Maturities on mortgage-backed securities represent stated maturity dates. Actual maturity dates may differ based on prepayment rates.

The Multi-Strategy Equity Fund owns certain investment partnerships which have limited liquidity and only permit redemptions at specified intervals. Such liquidity parameters may impact the Fund's ability to react quickly to changing market conditions and to meet its own liquidity needs. However, the Institute may withdraw its investment in the Funds, as needed.

Funds Held in Trust by Others

	2014	2013
Funds held in trust by others	\$ 2,625,073	\$ 2,361,906

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.

Note 5: Property and Equipment

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

	2014	2013
Land	\$ 1,970,580	\$ 1,970,580
Buildings and improvements	31,966,703	31,371,824
Equipment, furniture and fixtures	7,925,419	7,879,638
Construction in progress	-	148,198
	<u>41,862,702</u>	<u>41,370,240</u>
Less accumulated depreciation	21,038,614	20,313,030
	<u>\$ 20,824,088</u>	<u>\$ 21,057,210</u>

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

Note 6: Loans and Bonds Payable

Loans and bonds payable consisted of the following as of June 30:

	<u>2014</u>	<u>2013</u>
A promissory note with a bank that has an interest rate of 3.72% due in monthly installments of \$4,618 through November 2014 and a balloon payment in December 2014 of the final balance, collateralized by certain property.	\$ -	\$ 633,360
A promissory note with a bank that has an interest rate of 3.6% due in monthly installments of \$10,239 through September 2015 and a balloon payment in October 2015 of the final balance, collateralized by certain property. The Institute can borrow up to \$1,750,000 on this note.	-	1,632,180
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 0.15% and 0.18% at June 30, 2014 and 2013, respectively, this variable interest rate cannot exceed 12%.	<u>10,500,000</u>	<u>10,500,000</u>
	<u><u>\$ 10,500,000</u></u>	<u><u>\$ 12,765,540</u></u>

The Institute maintains a letter-of-credit facility, which expires on December 5, 2014, 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, 2014 and 2013.

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

Minimum annual principal payments on the loans and bonds payable as of June 30, 2014 are as follows:

2035	\$ 10,500,000
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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, 2015. No amounts were outstanding on these lines as of June 30, 2014 and 2013.

Note 7: Net Assets

Temporarily Restricted Net Assets

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

	2014	2013
Capital projects	\$ 1,533	\$ 769,880
Scholarships	14,199,750	9,849,931
Funds held in trust	447,010	387,977
Faculty chairs	1,084,747	771,353
General operations	4,281,967	3,130,569
	<u>\$ 20,015,007</u>	<u>\$ 14,909,710</u>

Permanently Restricted Net Assets

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

	2014	2013
Student scholarships	\$ 2,605,649	\$ 2,590,189
Faculty chairs	1,500,000	1,500,000
General operations	29,435,470	29,068,043
Funds held in trust	2,178,063	1,973,929
	<u>\$ 35,719,182</u>	<u>\$ 35,132,161</u>

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

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.

	2014	2013
Capital projects	\$ 768,347	\$ -
Scholarships	202,109	981,063
Faculty chairs	85,156	109,628
General operations	91,425	306,410
	<hr/>	<hr/>
Net assets released from restrictions	<u><u>\$ 1,147,037</u></u>	<u><u>\$ 1,397,101</u></u>

Note 8: Retirement Plan

The Institute participates in a multi-employer defined contribution retirement plan administered by the Teachers Insurance and Annuity Association and College Retirement Equities Fund ("TIAA-CREF") for certain academic, administrative and staff 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 \$278,879 and \$245,519 for the years ended June 30, 2014 and 2013, respectively.

Note 9: Fair Value Disclosures

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, 2014 and 2013

Following is a description of the valuation methodologies and inputs used for assets 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 pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended June 30, 2014.

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, 2014 and 2013:

		2014	
		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	\$ 684,164	\$ 684,164	\$ -
Mutual funds			
Vanguard intermediate term	3,340,050	3,340,050	-
Other mutual funds	13,980,548	13,980,548	-
Common stock	8,111,035	8,111,035	-
Exchange traded funds	4,295,729	4,295,729	-
U.S. Government agency obligations	116,120	-	116,120
Commonfund Multi-Strategy Equity Fund	21,431,419	-	21,431,419
Commonfund Multi-Strategy Bond Fund	10,139,738	-	10,139,738
Commonfund Government Money Market Fund	11,850	11,850	-
Total investments	<u>\$ 62,110,653</u>	<u>\$ 30,423,376</u>	<u>\$ 31,687,277</u>
Funds Held In Trust	<u>\$ 2,625,073</u>	<u>\$ -</u>	<u>\$ 2,625,073</u>

Kansas City Art Institute
Notes to Financial Statements
June 30, 2014 and 2013

		2013	
		<u>Fair Value Measurements Using</u>	
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Investments	Fair Value		
Money market funds	\$ 276,812	\$ 276,812	\$ -
Mutual funds			
Vanguard intermediate term	3,281,809	3,281,809	-
Other mutual funds	9,786,795	9,786,795	-
Common stock	6,986,697	6,986,697	-
Exchange traded funds	5,297,114	5,297,114	-
U.S. Government agency obligations	1,433,622	-	1,433,622
Commonfund Multi-Strategy Equity Fund	17,773,481	-	17,773,481
Commonfund Multi-Strategy Bond Fund	9,872,427	-	9,872,427
Commonfund Government Money Market Fund	11,850	11,850	-
	<u>\$ 54,720,607</u>	<u>\$ 25,641,077</u>	<u>\$ 29,079,530</u>
Funds Held In Trust	<u>\$ 2,361,906</u>	<u>\$ -</u>	<u>\$ 2,361,906</u>

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.

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

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.

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 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, 2014 and 2013 was:

	2014			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ (87)	\$ 18,878,610	\$ 32,509,585	\$ 51,388,108
Board-designated endowment funds	3,571,292	-	-	3,571,292
Total endowment funds	<u>\$ 3,571,205</u>	<u>\$ 18,878,610</u>	<u>\$ 32,509,585</u>	<u>\$ 54,959,400</u>

Kansas City Art Institute

Notes to Financial Statements

June 30, 2014 and 2013

	2013			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ (3,786)	\$ 12,910,853	\$ 32,065,448	\$ 44,972,515
Board-designated endowment funds	3,138,283	-	-	3,138,283
Total endowment funds	<u>\$ 3,134,497</u>	<u>\$12,910,853</u>	<u>\$ 32,065,448</u>	<u>\$ 48,110,798</u>

Changes in endowment net assets for the years ended June 30, 2014 and 2013 were:

	2014			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ 3,134,497	\$ 12,910,853	\$ 32,065,448	\$ 48,110,798
Total investment return	554,366	4,042,547	316,802	4,913,715
Addition of contributions and collections on pledges	-	-	127,335	127,335
Term endowment	-	3,358,820	-	3,358,820
Appropriation of endowment assets for expenditure	(117,658)	(1,433,610)	-	(1,551,268)
Endowment net assets, end of year	<u>\$ 3,571,205</u>	<u>\$ 18,878,610</u>	<u>\$ 32,509,585</u>	<u>\$ 54,959,400</u>

	2013			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, beginning of year	\$ 2,873,406	\$ 6,628,923	\$ 31,494,278	\$ 40,996,607
Total investment return	375,701	4,741,854	174,726	5,292,281
Addition of contributions and collections on pledges	-	-	396,444	396,444
Term endowment	-	2,931,247	-	2,931,247
Appropriation of endowment assets for expenditure	(114,610)	(1,391,171)	-	(1,505,781)
Endowment net assets, end of year	<u>\$ 3,134,497</u>	<u>\$ 12,910,853</u>	<u>\$ 32,065,448</u>	<u>\$ 48,110,798</u>

Included in the 2014 and 2013 temporarily restricted net assets above is a donation the Institute received in previous years for scholarships which management designated as a term-endowment during 2013.

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Notes to Financial Statements

June 30, 2014 and 2013

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

	2014	2013
Permanently restricted net assets – portion of perpetual endowment funds required to be retained permanently by explicit donor stipulation on SPMIFA	\$ 32,509,585	\$ 32,065,448
Perpetual trust held by others	2,178,063	1,973,929
Outstanding pledges	1,031,534	1,092,784
	<u>\$ 35,719,182</u>	<u>\$ 35,132,161</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 \$87 and \$3,786 at June 30, 2014 and 2013, 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.

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, 2014 and 2013, such percentage was 4% and the allocation totaled \$1,433,610 and \$1,391,171, 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.

Kansas City Art Institute
Notes to Financial Statements
June 30, 2014 and 2013

Note 11: Operating Leases

The Institute entered into a noncancellable operating lease for additional classroom space, which expired July 31, 2014. This lease contains an option to purchase the property during the lease term.

Future minimum lease payments under the operating lease are:

2015	\$ 7,047
Total minimum lease payments	<u>\$ 7,047</u>

Rent expense incurred during the years ended June 30, 2014 and 2013, was approximately \$129,000 and \$115,000, respectively.

Note 12: 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:

Pledges Receivable

Management believes the remaining net outstanding pledges receivable balances are collectible as of June 30, 2014. This estimate could materially change in future periods due to unforeseen events and circumstances.

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.

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.