

**THE FALCON FOUNDATION**

**Financial Statements**

**For the Year Ended June 30, 2017**

**And**

**Independent Auditors' Report**

# THE FALCON FOUNDATION

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## INDEPENDENT AUDITORS' REPORT

The Board of Governing Trustees  
The Falcon Foundation

We have audited the accompanying financial statements of The Falcon Foundation (the Foundation), which comprise the statement of financial position as of June 30, 2017 and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Falcon Foundation as of June 30, 2017 and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

## **Report on Summarized Comparative Information**

We have previously audited The Falcon Foundation's 2016 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated October 3, 2016. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2016 is consistent, in all material respects, with the audited financial statements from which it has been derived.

*Stockman Kast Ryan & Co., LLP*

November 22, 2017

# THE FALCON FOUNDATION

## STATEMENT OF FINANCIAL POSITION

**JUNE 30, 2017 (with comparative totals for 2016)**

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	<b>2017</b>	<b>2016</b>
<b>ASSETS</b>		
CURRENT ASSETS		
Cash and cash equivalents	\$ 296,566	\$ 471,542
Accounts receivable	<u>21,620</u>	<u>15,615</u>
Total current assets	318,186	487,157
INVESTMENTS	22,851,936	20,742,394
BENEFICIAL INTEREST IN FUNDS HELD BY THE AOG	681,331	614,930
ARTWORK	110,400	103,000
FURNITURE AND EQUIPMENT, NET	<u>2,119</u>	<u>3,797</u>
TOTAL ASSETS	<u>\$ 23,963,972</u>	<u>\$ 21,951,278</u>
<b>LIABILITIES AND NET ASSETS</b>		
CURRENT LIABILITIES		
Accounts payable and other current liabilities	<u>\$ 6,361</u>	<u>\$ 7,121</u>
NET ASSETS		
Unrestricted	18,829,223	16,914,091
Temporarily restricted	254,249	222,328
Permanently restricted	<u>4,874,139</u>	<u>4,807,738</u>
Total net assets	<u>23,957,611</u>	<u>21,944,157</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 23,963,972</u>	<u>\$ 21,951,278</u>

See notes to financial statements.

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# THE FALCON FOUNDATION

## STATEMENT OF ACTIVITIES

FOR THE YEAR ENDED JUNE 30, 2017 (with comparative totals for 2016)

	2017			2016 Total	
	Unrestricted	Temporarily Restricted	Permanently Restricted		Total
<b>REVENUES</b>					
Investment income (loss), net	\$ 2,130,262	\$ 504,176		\$ 2,634,438	\$ (499,088)
Trustee dues	121,200			121,200	92,900
Contributions	98,771			98,771	122,554
Change in beneficial interest in funds held by the AOG			\$ 66,401	66,401	(77,374)
Other	248			248	827
Net assets released from restrictions	<u>472,255</u>	<u>(472,255)</u>			
Total revenues	<u>2,822,736</u>	<u>31,921</u>	<u>66,401</u>	<u>2,921,058</u>	<u>(360,181)</u>
<b>EXPENSES</b>					
Program:					
Scholarships	569,412			569,412	611,343
Wages and benefits	136,256			136,256	135,897
Air Force Academy educational programs	66,000			66,000	16,000
Other	<u>48,737</u>			<u>48,737</u>	<u>57,111</u>
Total program expense	<u>820,405</u>	<u>—</u>	<u>—</u>	<u>820,405</u>	<u>820,351</u>
General and administrative:					
Wages and benefits	58,396			58,396	58,242
Other	<u>28,803</u>			<u>28,803</u>	<u>22,375</u>
Total general and administrative	<u>87,199</u>	<u>—</u>	<u>—</u>	<u>87,199</u>	<u>80,617</u>
Total expenses	<u>907,604</u>	<u>—</u>	<u>—</u>	<u>907,604</u>	<u>900,968</u>
CHANGE IN NET ASSETS	1,915,132	31,921	66,401	2,013,454	(1,261,149)
<b>NET ASSETS,</b>					
Beginning of year	<u>16,914,091</u>	<u>222,328</u>	<u>4,807,738</u>	<u>21,944,157</u>	<u>23,205,306</u>
NET ASSETS, End of year	<u>\$ 18,829,223</u>	<u>\$ 254,249</u>	<u>\$ 4,874,139</u>	<u>\$ 23,957,611</u>	<u>\$21,944,157</u>

See notes to financial statements.

# THE FALCON FOUNDATION

## STATEMENT OF CASH FLOWS

**FOR THE YEAR ENDED JUNE 30, 2017 (with comparative totals for 2016)**

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	2017	2016
OPERATING ACTIVITIES		
Change in net assets	\$ 2,013,454	\$ (1,261,149)
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Depreciation	1,678	1,678
Donated art work	(7,400)	
Change in beneficial interest in funds held by the AOG	(66,401)	77,374
Net realized and unrealized (gains) losses on investments	(2,206,651)	1,379,904
Changes in operating assets and liabilities:		
Accounts receivable	(6,005)	(5,438)
Accounts payable and other current liabilities	(760)	(49,129)
Net cash provided by (used in) operating activities	<u>(272,085)</u>	<u>143,240</u>
INVESTING ACTIVITIES		
Purchases of investments	(12,622,126)	(1,772,028)
Proceeds from the sale of investments	<u>12,719,235</u>	<u>1,906,539</u>
Net cash provided by operating activities	<u>97,109</u>	<u>134,511</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(174,976)	277,751
CASH AND CASH EQUIVALENTS, Beginning of year	<u>471,542</u>	<u>193,791</u>
CASH AND CASH EQUIVALENTS, End of year	<u>\$ 296,566</u>	<u>\$ 471,542</u>

See notes to financial statements.

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# THE FALCON FOUNDATION

## NOTES TO FINANCIAL STATEMENTS

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### 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Organization** — The Falcon Foundation (the Foundation) is a not-for-profit corporation that supports charitable, educational and other undertakings in support of the mission of the United States Air Force Academy (the Academy). The Foundation's primary effort is to provide scholarships to selected preparatory schools, or other appropriate education or training for motivated young men and women seeking admission to the Academy and a career in the United States Air Force.

**Basis of Presentation** — The accompanying financial statements include certain prior-year summarized comparative information in total. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Foundation's financial statements for the year ended June 30, 2016, from which the summarized information was derived.

The Foundation reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, which represents the expendable resources that are available for operations at management's discretion; temporarily restricted net assets, which represents resources restricted by donors as to purpose or by the passage of time; and permanently restricted net assets, which represents resources whose use by the organization is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the organization.

**Cash and Cash Equivalents** — For purposes of the statement of cash flows, the Foundation considers all unrestricted cash on hand or in demand deposit accounts to be cash equivalents. Investments in money market funds held in investment accounts are not considered cash equivalents.

**Investments** — Investments are recorded at fair value. Realized and unrealized gains and losses are reflected in the statement of activities. Earnings on investments are recognized as an increase in unrestricted or temporarily restricted net assets according to the nature of the restrictions on the original gift. Donated investments are recorded at fair market value on the date of donation. See Note 2 for information on fair value measurements.

**Furniture and Equipment** — Furniture and equipment are recorded at cost. Expenditures for ordinary maintenance and repairs are charged to expense as incurred. Depreciation is provided using the straight-line method over the estimated useful lives of the respective assets.

**Contributions** — Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence or nature of any donor restrictions.

All donor restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a donor restriction is met, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

**Artwork** — Artwork consists of three sculptures and one painting recorded at fair value on the date of donation and is not depreciated.

**Tax Status** — The Foundation is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. In addition, the Foundation qualifies for the charitable contribution deduction. Management of the Foundation believes that it does not have any uncertain tax positions that are material to its financial statements. Tax years that remain subject to examination include 2014 through the current period.

**Use of Estimates** — The preparation of the Foundation's 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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Subsequent Events** — The Foundation has evaluated subsequent events for recognition or disclosure through the date of the Independent Auditors' Report, which is the date the financial statements were available for issuance.

## 2. INVESTMENTS AND FAIR VALUE MEASUREMENTS

The Foundation is required to use a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities that the Foundation has the ability to access.

Level 2: Prices determined using significant other observable inputs. Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3: Prices determined using significant unobservable inputs.

The investment's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The following is a description of the valuation methodologies used for assets measured at fair value. There have been no significant changes in the methodologies used at June 30, 2017 and 2016.

*Mutual Funds* — Valued at quoted market prices.

*TIFF Multi-Asset Fund* — Valued at quoted market prices. The TIFF multi-asset fund is invested in diversified asset classes including equity securities, fixed income securities, commodities, real estate and others.

*TIFF Absolute Return Fund* — Valued based on the net asset value (NAV) per share. The NAV is used as a practical expedient to estimate fair value. This practical expedient would not be used if it is determined to be probable that the investment will be sold at an amount different from the reported NAV. NAV is based upon the fair value of the underlying investments as determined by fund's management and its underlying investment managers. The TIFF absolute return fund is invested in investment funds, limited partnerships, limited liability companies and non-U.S. corporations. The strategies the fund may employ include but are not limited to capital structure arbitrage, event driven, fixed income, and long/short equity strategies. The fund may invest in a range of derivatives. The fair values of the underlying investments may differ significantly from the values that would have been used had a ready market for the underlying funds existed.

See Note 4 regarding the valuation of the beneficial interest in funds held by the AOG.

The following table sets forth by level, within the fair value hierarchy, the Foundation's financial instruments at fair value as of June 30:

	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>	<b>Total</b>
<b>2017:</b>				
Domestic equity mutual funds	\$ 8,730,156			\$ 8,730,156
Foreign equity mutual funds	7,559,170			7,559,170
Fixed income mutual funds	4,588,630			4,588,630
Beneficial interest in funds held by the AOG	<u>                    </u>	\$ 681,331	<u>                    </u>	<u>681,331</u>
Total investments in the fair value hierarchy	<u>\$ 20,877,956</u>	<u>\$ 681,331</u>	<u>\$ —</u>	21,559,287
Investments measured at net asset value				<u>1,973,980</u>
Total				<u>\$ 23,533,267</u>

	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>	<b>Total</b>
<b>2016:</b>				
Domestic equity mutual funds	\$ 5,116,525			\$ 5,116,525
Foreign equity mutual funds	3,364,651			3,364,651
Fixed income mutual funds	2,112,959			2,112,959
TIFF multi-asset fund	8,102,368			8,102,368
Beneficial interest in funds held by the AOG	<u>                    </u>	\$ 614,930	\$ —	<u>614,930</u>
Total investments in the fair value hierarchy	<u>\$ 18,696,503</u>	<u>\$ 614,930</u>	<u>\$ —</u>	19,311,433
Investments measured at net asset value				<u>2,045,891</u>
Total				<u>\$21,357,324</u>

The following table summarizes investments measured at net asset value per share as of June 30:

<b>Investment</b>	<b>Fair Value</b>	<b>Redemption Frequency</b>	<b>Redemption Notice Period</b>
<b>2017:</b>			
TIFF Absolute Return Fund	\$ 1,973,980	Annually, on the end of the calendar quarter associated with the date of investment	100 days advance written notice
<b>2016:</b>			
TIFF Absolute Return Fund	\$ 2,045,891	Annually, on the end of the calendar quarter associated with the date of investment	100 days advance written notice

Net investment income (loss) was composed of the following for the years ended June 30:

	<b>2017</b>	<b>2016</b>
Interest and dividends	\$ 487,716	\$ 901,600
Net realized and unrealized gains (losses)	2,206,651	(1,379,904)
Investment management and custodial fees	<u>(59,929)</u>	<u>(20,784)</u>
Investment income (loss), net	<u>\$ 2,634,438</u>	<u>\$ (499,088)</u>

### 3. FURNITURE AND EQUIPMENT

Furniture and equipment consists of the following as of June 30:

	2017	2016
Furniture and equipment	\$ 20,256	\$ 20,256
Less accumulated depreciation	<u>18,137</u>	<u>16,459</u>
Furniture and equipment, net	<u>\$ 2,119</u>	<u>\$ 3,797</u>

### 4. BENEFICIAL INTEREST IN FUNDS HELD BY THE AOG

The Foundation is the sole beneficiary of the Anna Keesling Ackerman Trust (the Ackerman Trust), whose principal is to be held in perpetuity. Assets of the trust are invested and administered by the Association of Graduates of the United States Air Force Academy (AOG), acting as trustee. Annual distributions are made from the Ackerman Trust to the Foundation. Assets of the Ackerman Trust consist of money market funds, mutual funds and hedge funds. The Foundation records its interest in the Ackerman Trust at the fair value of the assets held by the trust. Fair values for investments held by the Ackerman Trust are determined by reference to quoted market prices and other observable information. As of June 30, 2017 and 2016 the fair value of the Ackerman Trust was \$448,976 and \$405,217, respectively. The Foundation received a distribution from the Ackerman Trust of \$14,183 and recognized a gain on the change in value of \$43,759 for the year ended June 30, 2017. The Foundation received a distribution from the Ackerman Trust of \$15,967 and recognized a loss on the change in value of \$50,989 for the year ended June 30, 2016.

The Foundation is the beneficiary of funds raised and held by the AOG, for the Foundation (AOG Fund). The AOG Fund is to be held in perpetuity. Assets of the AOG Fund are invested and administered by the AOG, acting as trustee. Annual distributions are made from the AOG Fund to the Foundation. Assets consist of money market funds, mutual funds and hedge funds. The Foundation records its proportionate share of the fair value of the underlying assets of the fund. Fair values for investments held by the AOG Fund are determined by reference to quoted market prices and other observable information. As of June 30, 2017 and 2016 the Foundation's share of the fair value of the AOG Fund was \$232,355 and \$209,713, respectively. The Foundation received a distribution from the AOG of \$7,340 and recognized a gain on the change in value of \$22,642 for the year ended June 30, 2017. The Foundation received a distribution from the AOG of \$8,264 and recognized a loss on the change in value of \$26,385 for the year ended June 30, 2016.

### 5. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following at June 30:

	2017	2016
Wood Memorial	\$ 135,881	\$ 120,569
General William J. Evans "Honors" Program	71,485	64,414
Gerhard Neumann Memorial Fund	23,716	22,423
Ruth A. Eaker Fund	<u>23,167</u>	<u>14,922</u>
Total	<u>\$ 254,249</u>	<u>\$ 222,328</u>

## 6. PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets consist of the following at June 30:

	<b>2017</b>	<b>2016</b>
Scholarships	\$ 4,037,808	\$ 4,037,808
General William J. Evans "Honors" Program	70,000	70,000
Ruth A. Eaker Fund	50,000	50,000
Gerhard Neumann Memorial Fund	<u>35,000</u>	<u>35,000</u>
Total	4,192,808	4,192,808
Beneficial interest in assets held by the AOG (Note 4)	<u>681,331</u>	<u>614,930</u>
Total permanently restricted net assets	<u>\$ 4,874,139</u>	<u>\$ 4,807,738</u>

## 7. ENDOWMENT FUNDS

The Foundation's endowment funds are restricted for the purpose of supporting the operations of the Foundation (see Note 6 for the individual funds that have been established). As required by generally accepted accounting principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The State of Colorado has adopted the Uniform Prudent Management of Institutional Funds Act (UPMIFA). The act provides statutory guidance for management investment and expenditure of endowment funds held by not-for-profit organizations. The Foundation has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, and (b) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

Changes in endowment fund net assets and the Endowment Net Asset Composition by Type of Fund for the years ended June 30, 2017 and 2016 are as follows:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Donor restricted endowment net assets, July 1, 2015	\$ —	156,462	4,885,112	5,041,574
Investment loss	(72,493)	(54,705)		(127,198)
Change in beneficial interest in funds held by the AOG	_____	_____	(77,374)	(77,374)
Donor restricted endowment net assets, June 30, 2016	(72,493)	101,757	4,807,738	4,837,002
Investment income (loss)	72,493	488,864		561,357
Change in beneficial interest in funds held by the AOG			66,401	66,401
Appropriation of endowment assets for expenditures	_____	(472,255)	_____	(472,255)
Donor restricted endowment net assets, June 30, 2017	<u>\$ —</u>	<u>\$ 118,366</u>	<u>\$ 4,874,139</u>	<u>\$ 4,992,505</u>

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Foundation to retain as a fund of perpetual duration. In accordance with GAAP, a deficiency of this nature is reported in unrestricted net assets of \$72,493 as of June 30, 2016. No such deficiency existed as of June 30, 2017.

The Foundation has adopted investment and spending policies for the endowment assets with a balanced objective with an emphasis on long-term capital appreciation over current income to ensure preservation of real purchasing power and growth of principal. Included in endowments are perpetual trusts held by third parties; these trusts are controlled by the third party and the investment policies of the Foundation do not apply to them. The balance of perpetual trusts held by third parties was \$681,331 and \$614,930 at June 30, 2017 and 2016, respectively.

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

## **8. EMPLOYEE BENEFIT PLAN**

The Foundation adopted a simple IRA plan for its employees in which the Foundation matches employee contributions up to 3% of salaries. Employer contributions totaled \$2,063 and \$2,003 for the years ended June 30, 2017 and 2016, respectively.

**9. INVESTMENT RISKS AND CONCENTRATIONS**

The Foundation invests in investment securities which 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 change in the values of investments will occur in the near term and that such changes could materially affect the recorded amount of investments in the Foundation's financial statements

**10. RELATED PARTY TRANSACTIONS**

The Foundation has recognized dues from trustees of \$121,200 and \$92,900 for the years ended June 30, 2017 and 2016, respectively. The Foundation's trustees also made contributions to the Foundation of \$16,477 and \$48,182 during the years ended June 30, 2017 and 2016, respectively.