

The Institute of World Politics

Financial Report
July 31, 2018

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Independent Auditor's Report

To the Executive Committee
The Institute of World Politics

Report on the Financial Statements

We have audited the accompanying financial statements of The Institute of World Politics (the Institute), which comprise the statements of financial position as of July 31, 2018 and 2017, the related statements of activities, functional expenses 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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 Institute as of July 31, 2018 and 2017, 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our reports, dated February 15, 2019 and January 12, 2018, on our consideration of the Institute's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of those reports is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Institute's internal control over financial reporting and compliance.

RSM US LLP

Washington, D.C.
February 15, 2019

The Institute of World Politics

Statements of Financial Position
July 31, 2018 and 2017

	2018	2017
Assets		
Cash and cash equivalents	\$ 875,913	\$ 493,440
Tuition receivables, net of allowances for doubtful accounts and discounts (2018 – \$107,817; 2017 – \$108,392)	228,748	61,256
Contributions receivable, net	1,609,197	2,444,033
Prepaid expenses and other assets	126,613	73,415
Restricted cash	1,095,769	853,173
Investments	1,845,726	2,905,345
Investments held for split-interest agreement	404,350	204,841
Interest rate swap contract	481,745	215,605
Website development costs, net of accumulated amortization (2018 – \$192,584; 2017 – \$172,107)	8,688	29,165
Property and equipment, net	10,246,062	10,464,779
	\$ 16,922,811	\$ 17,745,052
Liabilities and Net Assets		
Liabilities:		
Lines of credit	\$ 500,000	\$ 500,000
Accounts payable and accrued expenses	115,446	183,505
Deferred tuition and revenue	86,830	13,400
Refundable advances	1,047,611	1,000,000
Long-term debt, net of issuance costs	7,926,870	8,167,691
Capital lease obligations	49,368	22,757
Annuity obligations	200,493	61,370
	9,926,618	9,948,723
Commitments and contingencies (Note 9)		
Net assets:		
Unrestricted:		
Undesignated	3,246,862	2,494,598
Board-designated	355,401	1,462,188
	3,602,263	3,956,786
Temporarily restricted	2,132,110	2,793,808
Permanently restricted	1,261,820	1,045,735
	6,996,193	7,796,329
	\$ 16,922,811	\$ 17,745,052

See notes to financial statements.

The Institute of World Politics

Statement of Activities
Year Ended July 31, 2018

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue and support:				
Student tuition and fees, net of discounts and scholarships of \$612,342	\$ 2,980,746	\$ -	\$ -	\$ 2,980,746
Contributions	2,043,624	370,989	216,085	2,630,698
Investment income, net	135,892	14,246	-	150,138
Other	70,214	-	-	70,214
Net assets released from restrictions	1,046,933	(1,046,933)	-	-
Total revenue and support	6,277,409	(661,698)	216,085	5,831,796
Expenses:				
Program	4,133,616	-	-	4,133,616
Management and general	2,004,380	-	-	2,004,380
Fundraising	796,627	-	-	796,627
Total expenses	6,934,623	-	-	6,934,623
Other gains:				
Unrealized gain on interest rate swaps	266,140	-	-	266,140
Change in valuation of charitable gift annuities	36,551	-	-	36,551
	302,691	-	-	302,691
Change in net assets	(354,523)	(661,698)	216,085	(800,136)
Net assets:				
Beginning	3,956,786	2,793,808	1,045,735	7,796,329
Ending	\$ 3,602,263	\$ 2,132,110	\$ 1,261,820	\$ 6,996,193

See notes to financial statements.

The Institute of World Politics

**Statement of Activities
Year Ended July 31, 2017**

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue and support:				
Student tuition and fees, net of discounts and scholarships of \$405,320	\$ 2,428,133	\$ -	\$ -	\$ 2,428,133
Contributions	2,028,597	1,209,500	137,640	3,375,737
Investment income, net	562,874	73,275	-	636,149
Other	63,970	-	-	63,970
Net assets released from restrictions	1,295,407	(1,295,407)	-	-
Total revenue and support	6,378,981	(12,632)	137,640	6,503,989
Expenses:				
Program	4,005,059	-	-	4,005,059
Management and general	1,693,997	-	-	1,693,997
Fundraising	654,088	-	-	654,088
Total expenses	6,353,144	-	-	6,353,144
Other gains:				
Unrealized gain on interest rate swaps	215,605	-	-	215,605
	215,605	-	-	215,605
Change in net assets before reclassifications	241,442	(12,632)	137,640	366,450
Reclassifications:				
Donor release of endowment fund restrictions	762,158	(12,158)	(750,000)	-
Change in net assets	1,003,600	(24,790)	(612,360)	366,450
Net assets:				
Beginning	2,953,186	2,818,598	1,658,095	7,429,879
Ending	\$ 3,956,786	\$ 2,793,808	\$ 1,045,735	\$ 7,796,329

See notes to financial statements.

The Institute of World Politics

**Statement of Functional Expenses
Year Ended July 31, 2018**

Expense Category	Program	Management and General	Fundraising	Total
Salaries	\$ 2,687,795	\$ 846,926	\$ 407,126	\$ 3,941,847
Other professional fees	149,189	66,550	34,201	249,940
Other employee benefits	289,412	62,550	65,998	417,960
Depreciation and amortization	169,613	73,549	38,814	281,976
Payroll taxes	198,103	61,537	22,090	281,730
Occupancy	82,990	144,171	17,016	244,177
Conferences, conventions and meetings	125,941	29,687	86,062	241,690
Interest expense	2,537	246,777	542	249,856
Office expenses	75,160	39,463	19,616	134,239
Accounting	-	120,775	-	120,775
Travel	38,466	49,253	37,134	124,853
Pension plan contributions	48,935	37,412	10,146	96,493
Publications and subscriptions	89,668	6,654	1,744	98,066
Information technology	57,847	75,612	12,221	145,680
Printing	21,151	5,657	21,233	48,041
Insurance	40,877	19,428	8,731	69,036
Legal	-	64,378	3,796	68,174
Investment management fees	-	16,440	-	16,440
Dues	14,027	14,846	2,655	31,528
Advertising	3,344	235	495	4,074
Miscellaneous	38,561	22,480	7,007	68,048
	\$ 4,133,616	\$ 2,004,380	\$ 796,627	\$ 6,934,623

See notes to financial statements.

The Institute of World Politics

**Statement of Functional Expenses
Year Ended July 31, 2017**

Expense Category	Program	Management and General	Fundraising	Total
Salaries	\$ 2,511,592	\$ 781,840	\$ 301,250	\$ 3,594,682
Other professional fees	258,129	88,911	59,222	406,262
Other employee benefits	215,988	81,458	30,750	328,196
Depreciation and amortization	224,923	9,519	38,015	272,457
Payroll taxes	190,876	56,240	21,880	268,996
Occupancy	124,194	67,665	20,823	212,682
Conferences, conventions and meetings	110,350	18,496	61,542	190,388
Interest expense	-	184,528	-	184,528
Office expenses	106,500	39,409	20,927	166,836
Accounting	-	145,595	-	145,595
Travel	80,162	35,927	26,826	142,915
Pension plan contributions	48,255	34,637	11,337	94,229
Publications and subscriptions	79,205	340	4,807	84,352
Information technology	15,195	42,074	6,532	63,801
Printing	23,876	1,720	35,104	60,700
Insurance	37,111	11,356	6,273	54,740
Legal	-	45,676	5,385	51,061
Investment management fees	-	19,811	-	19,811
Dues	4,275	6,018	2,900	13,193
Advertising	6,136	50	370	6,556
Miscellaneous	(31,708)	22,727	145	(8,836)
Total	\$ 4,005,059	\$ 1,693,997	\$ 654,088	\$ 6,353,144

See notes to financial statements.

The Institute of World Politics

**Statements of Cash Flows
Years Ended July 31, 2018 and 2017**

	2018	2017
Cash flows from operating activities:		
Change in net assets	\$ (800,136)	\$ 366,450
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Depreciation and amortization	281,976	272,457
Amortization of debt issuance costs	16,179	14,677
Realized and unrealized gain on investments, net	(94,554)	(547,113)
Realized and unrealized gain on swap, net	(266,140)	(215,605)
Bad debt expense	-	(74,348)
Contributions restricted to investment in perpetuity	(216,085)	(137,640)
Change in valuation of annuity obligations	(36,551)	-
Loss on disposal of fixed assets	4,610	-
Changes in assets and liabilities:		
(Increase) decrease in:		
Tuition receivables	(167,492)	50,718
Contributions receivable	834,836	297,218
Prepaid expenses and other assets	(53,198)	21,509
Deferred rent receivable	-	10,324
(Decrease) increase in:		
Accounts payable and accrued expenses	(68,059)	27,407
Deferred tuition and revenue	73,430	(7,000)
Refundable advances	47,611	-
Net cash (used in) provided by operating activities	(443,573)	79,054
Cash flows from investing activities:		
Proceeds from sales of investments	4,806,232	3,816,218
Purchases of investments	(3,851,568)	(2,675,316)
Purchases of property and equipment	-	(2,081,532)
Change in prepayments against building purchase	-	649,507
(Increase) decrease in restricted cash	(242,596)	646,677
Net cash provided by investing activities	712,068	355,554
Cash flows from financing activities:		
Net principal payments on lines of credit	-	(397,131)
Contributions restricted to investment in perpetuity	216,085	137,640
Capital lease obligation payments	(20,781)	(17,958)
Payments on annuity obligations	(23,018)	(11,964)
Cash received to establish annuity obligation	198,692	-
Payments borrowing on note payable	(257,000)	(186,000)
Debt issuance costs	-	(160,986)
Net cash provided by (used in) financing activities	113,978	(636,399)
Net increase (decrease) in cash and cash equivalents	382,473	(201,791)
Cash and cash equivalents:		
Beginning	493,440	695,231
Ending	\$ 875,913	\$ 493,440
Cash paid for interest	\$ 233,640	\$ 169,851
Supplemental disclosure of cash flow information:		
Property and equipment purchased with debt	\$ 47,392	\$ 8,500,000

See notes to financial statements.

The Institute of World Politics

Notes to Financial Statements

Note 1. Nature of Activities and Significant Accounting Policies

Nature of activities: The Institute of World Politics (the Institute) is a graduate school of national security and international affairs dedicated to developing leaders with a sound understanding of international realities and the ethical conduct of statecraft based on knowledge and appreciation of the principles of the American political economy and the Western moral tradition. The classrooms, library and administrative offices of the Institute are located in Washington, D.C.

The Institute offers Master's degree, certificate and continuing education programs with a professional curriculum covering the various elements of statecraft. It includes an interdisciplinary foundational course of study of the relevant elements of comparative political culture, Western moral precepts, practical political economics and political and diplomatic history. All degrees are designed for students who are pursuing a career in the international affairs, intelligence or national security fields.

A summary of the Institute's significant accounting policies follows:

Basis of accounting: The financial statements of the Institute have been prepared on the accrual basis of accounting, whereby unconditional support is recognized when received, revenue is recognized when earned and expenses are recognized when incurred.

Basis of presentation: Resources are reported, for accounting purposes, in separate classes of net assets based on the existence or absence of donor-imposed restrictions. In the accompanying financial statements, net assets that have similar characteristics have been combined into categories as follows:

Permanently restricted: Net assets subject to donor-imposed stipulations that they be maintained permanently by the Institute. Generally, the donors of these assets permit the Institute to use all or part of the income earned on related investments for general or specific purposes.

Temporarily restricted: Net assets whose use by the Institute is subject to donor-imposed stipulations that can be fulfilled by actions of the Institute pursuant to those stipulations or that expire by the passage of time.

Unrestricted: Net assets that are not subject to donor-imposed stipulations. The Institute's unrestricted net assets are comprised of the following:

Undesignated net assets: Represents funds available for general operations.

Board-designated net assets: Represents funds set aside by the Institute's Board of Trustees to support the Institute's programs and activities.

Expirations of temporary restrictions on net assets, that is, the donor-imposed stipulated purpose has been accomplished, or the stipulated time period has elapsed, are reported as net assets released from restrictions on the statements of activities. Temporarily restricted contributions received that are used according to donor restrictions in the same period are recognized as temporarily restricted contributions and reclassified as net assets released from restrictions in the same period.

Cash equivalents: For purposes of the statements of financial position and cash flows, the Institute considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents consisting of demand deposits, money market funds and short-term certificates of deposit held with banks.

Restricted cash: Restricted cash pertains to the Institute's permanently restricted endowments and include one restricted cash account and money market funds included in investment portfolios.

The Institute of World Politics

Notes to Financial Statements

Note 1. Nature of Activities and Significant Accounting Policies (Continued)

Financial risk: The Institute maintains cash in bank deposit accounts which, at times, may exceed federally insured limits. The Institute has not experienced any losses in such accounts. The Institute believes it is not exposed to any significant financial risk on cash.

The Institute invests in a professionally managed portfolio that contains money market funds, government and corporate bonds, mutual funds and corporate stocks. Such investments are exposed to various risks, such as market and credit. Due to the level of risk associated with such investments and the level of uncertainty related to changes in the value of such investments, it is at least reasonably possible that changes in risk in the near term would materially affect investment balances and the amounts reported in the financial statements.

Tuition receivables: Tuition receivables are carried at original tuition contract amount, less an estimate made for doubtful receivables based on a review of all outstanding accounts on an annual basis. Management determines the allowance for doubtful accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts. Accounts receivable are written off when deemed uncollectible.

Contributions receivable: Contributions receivable are recognized when the donor makes a written promise to give to the Institute that is, in substance, unconditional. Contributions to be received in a future period are discounted to their net present value at the time the support is recorded. The Institute's contributions receivable are generally receivable over a one- to four-year period and are discounted at a rate of 1.00% per annum. The allowance for doubtful contributions receivable is based on management's experience with prior campaigns and its analysis of specific contributions receivable. Recoveries of promises to give previously written off are recorded as support as received. Based on management's evaluation of the collectability of the contributions receivable, no allowance for doubtful promises to give was recorded at July 30, 2018 and 2017.

Other assets: During the year ended July 31, 2016, the Institute paid for and deferred certain costs in connection with the building purchase, which was consummated on September 26, 2016. Those costs included a deposit of \$515,000 paid to the escrow agent and \$134,507 paid for other related costs. Those costs were recorded as part of prepaid expenses and other assets in the asset section of the statements of financial position at July 31, 2016, and were capitalized as part of property and equipment during the year ended July 2017.

Investments: Investments in equity securities with readily determinable fair values and all investments in debt securities are reflected at fair market value. To adjust the carrying values of these securities, the change in fair market value is recorded as a component of investment income in the statements of activities.

Split-interest agreement: The Institute is a trustee of certain assets under a split-interest agreement, which provides for payments to the donors of specified annuity amounts. Assets held under this agreement are reported as investments in split-interest agreement on the statements of financial position. Contribution revenue was recognized at the date of the agreement after providing for the present value of estimated future payments to be made to the donors. The annuity obligation liability is adjusted during the term of the agreements for accretion of the discount, payments made and other changes in the estimates.

Property and equipment: Acquisitions of property and equipment in excess of \$1,000 and which have useful lives greater than one year are recorded at cost and depreciated using the straight-line method over the useful lives of 3 to 40 years. Leasehold improvements are amortized using the straight-line method over the estimated life of the asset or the term of the lease, whichever is less.

Note 1. Nature of Activities and Significant Accounting Policies (Continued)

Valuation of long-lived assets: The Institute reviews property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of the long-lived asset is measured by comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell.

Debt issuance costs: The Institute paid certain customary fees as required to secure the long-term debt used to acquire real property. These fees have been capitalized and are being amortized over the loan period up to the initial redemption date. The unamortized portion of these costs are netted with the respective debt on the accompany statements of financial position. Amortization expense for the years ended July 31, 2018 and 2017 was \$16,179 and \$14,677, respectively.

Interest rate swap contract: The Institute follows the accounting standard for derivative instruments and hedging activities related to participation in an interest rate swap contract pertaining to certain long-term debt acquired. This standard requires that all derivative financial instruments be recognized in the financial statements at fair value. Changes in the fair value of the derivative instrument are recognized each period as a component of change in net assets.

Revenue recognition: The Institute's activities are primarily supported through student tuition and fees, contributions and investment earnings.

Tuition and fees, and scholarship allowances are recognized ratably over the academic year. Tuition and fees received in advance are deferred and recognized ratably as revenue over the period in which the related instruction occurs. Allowances are made for uncollectible tuition and fees based on prior collection experience and economic factors, which in management's judgment, could influence the ability of students to repay outstanding amounts.

Unconditional contributions, including unconditional promises to give, are recognized as support in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Receipts of conditional contributions are recorded as refundable advances in the liability section of the statements of financial position. Contributions of assets other than cash are recorded at their estimated fair value at the date of gift. Contributions received for restricted purposes are reported as part of temporarily restricted net assets until the restriction expires or as permanently restricted. When temporary restrictions expire, the related net assets are reclassified to unrestricted net assets and reported on the statements of activities as net assets released due to satisfaction of program and/or time restrictions. Provisions for uncollectible restricted contributions receivable are charged directly to temporarily or permanently restricted net assets.

The Institute's share of bequests is recorded when the Institute has an irrevocable right to the bequest and the proceeds are measurable. Gifts in-kind are reported at their fair value at the date of the gift.

Functional allocation of expenses: The Institute's expenses have been presented on a functional basis in the statements of activities. Certain overhead costs have been allocated among program services, management and general and fundraising.

The Institute of World Politics

Notes to Financial Statements

Note 1. Nature of Activities and Significant Accounting Policies (Continued)

Income taxes: The Institute is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code (IRC). The Institute is exempt from federal taxes on income other than unrelated business income. Effective January 1, 2018, the Institute is now subject to unrelated business income tax on certain pretax employee benefits. Income tax expense for the year ended June 30, 2018, was insignificant. The Institute is not classified as a private foundation under Section 509(a)(1) of the IRC.

In accordance with authoritative guidance on accounting for uncertainty in income taxes issued by the Financial Accounting Standards Board (FASB), the Institute recognizes tax liabilities for uncertain tax positions when it is more likely than not that a tax position will not be sustained upon examination and settlement with various taxing authorities. Liabilities for uncertain tax positions are measured based upon the largest amount of benefit that is greater than 50% likely of being realized upon settlement. The guidance on accounting for uncertainty in income taxes also addresses de-recognition, classification, interest and penalties on income taxes and accounting in interim periods. The Institute recognizes interest accrued and penalties related to unrecognized tax benefits, if any, as income tax expense.

With few exceptions, the Institute is no longer subject to income tax examinations by the U.S. federal, state or local tax authorities for years ended July 31, 2015, and prior.

Management has evaluated the Institute's tax positions and has concluded that the Institute has taken no uncertain tax positions that require adjustment to the financial statements to comply with the provisions of this guidance.

Use of estimates: The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Recent accounting pronouncements: In August 2016, the FASB Accounting Standards Update (ASU) No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The amendments in this ASU make improvements to the information provided in financial statements and accompanying notes of not-for-profit entities. The amendments set forth the FASB's improvements to net asset classification requirements and the information presented about a not-for-profit entity's liquidity, financial performance and cash flows. The ASU is effective for fiscal years beginning after December 15, 2017. Early adoption is permitted. The changes in this ASU should generally be applied on a retrospective basis in the year that the ASU is first applied. The Institute is currently evaluating the impact of this ASU on the financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*. The amendments in this ASU require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. The ASU will be effective for fiscal years beginning after December 15, 2018. Early adoption is permitted. The changes in this ASU should generally be applied on a retrospective basis in the year that the ASU is first applied. The Institute is currently evaluating the impact of this ASU on the financial statements.

The Institute of World Politics

Notes to Financial Statements

Note 1. Nature of Activities and Significant Accounting Policies (Continued)

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, requiring an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The updated standard will replace most existing revenue recognition guidance in generally accepted accounting principles in the United States of America (GAAP) when it becomes effective and permits the use of either a full retrospective or retrospective with cumulative effect transition method. Early adoption is permitted. The updated standard will be effective for annual reporting periods beginning after December 15, 2018. Management has not yet selected a transition method and is currently evaluating the effect that the ASU will have on the financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. The guidance in this ASU supersedes the leasing guidance in Topic 840, *Leases*. Under the new guidance, lessees are required to recognize lease assets and lease liabilities on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Institute is currently evaluating the impact of the pending adoption of the new standard on the financial statements.

In June 2018, the FASB issued ASU No. 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. This ASU clarifies the guidance for evaluating whether a transaction is reciprocal (i.e., an exchange transaction) or nonreciprocal (i.e., a contribution) and for distinguishing between conditional and unconditional contributions. The ASU also clarifies the guidance used by entities other than not-for-profits to identify and account for contributions made. The ASU has different effective dates for resource recipients and resource providers. The updated standard will be effective for annual reporting periods beginning after December 15, 2018. Early adoption is permitted. Management is currently evaluating the impact of the adoption of this guidance on its financial statements.

Subsequent events: In preparing these financial statements, the Institute has evaluated events and transactions for potential recognition or disclosure through February 15, 2019, the date the financial statements were available to be issued.

Note 2. Contributions Receivable

At July 31, 2018 and 2017, the anticipated receipts of contributions receivable are as follows:

	2018	2017
Less than one year	\$ 634,500	\$ 662,700
One to four year	1,032,500	1,838,522
	1,667,000	2,501,222
Less discount factor	(57,803)	(57,189)
	<u>\$ 1,609,197</u>	<u>\$ 2,444,033</u>

The Institute of World Politics

Notes to Financial Statements

Note 3. Investments

Investments consist of the following at July 31, 2018 and 2017:

	2018	2017
Corporate stocks	\$ 1,684,455	\$ 2,687,842
Equity mutual funds	161,271	217,503
	<u>\$ 1,845,726</u>	<u>\$ 2,905,345</u>

Investment income for the years ended July 31, 2018 and 2017 is comprised of the following:

	2018	2017
Interest and dividends	\$ 55,584	\$ 89,036
Realized and unrealized gain	94,554	547,113
	<u>\$ 150,138</u>	<u>\$ 636,149</u>

Note 4. Split-Interest Agreement

Charitable gift annuity's investments as of July 31, 2018 and 2017, are comprised of the following:

	2018	2017
Money market fund	\$ 1,817	\$ 6,018
Domestic equity mutual funds	200,486	129,153
International equity mutual funds	47,512	-
Fixed income mutual funds	154,535	69,670
	<u>\$ 404,350</u>	<u>\$ 204,841</u>

The following is a summary of the changes in the annuity obligation for the years ended July 31, 2018 and 2017:

	2018	2017
Beginning of the year	\$ 61,370	\$ 73,334
Payments to annuitant	(23,018)	(11,964)
Change in value due to actuarial valuation	(36,551)	-
Charitable gift annuity received	198,692	-
End of the year	<u>\$ 200,493</u>	<u>\$ 61,370</u>

Note 5. Fair Value Measurements

The Fair Value Measurement Topic of the Accounting Standards Codification (the Codification) defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, and sets out a fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). Inputs are broadly defined under this topic as assumptions market participants would use in pricing an asset or liability.

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 reporting entity has the ability to access at the measurement date. The types of investments in Level 1 include money market funds, equity securities, mutual funds, corporate and government bonds. As required by the Fair Value Measurement Topic, the Institute does not adjust the quoted price for these investments, even in situations where the Institute holds a large position and a sale could reasonably impact the quoted price.
- Level 2:** Inputs other than quoted prices within Level 1 that are observable for the asset or liability, either directly or indirectly, and fair value is determined through the use of models or other valuation methodologies. The interest rate swap contract connected to the Institute's long-term debt is classified as a Level 2 instrument because its value is a function of the difference between the interest rate on the Institute's long-term debt and the rate in the swap agreement; hence, there are observable market-based inputs. A significant adjustment to a Level 2 input could result in the Level 2 measurement becoming a Level 3 measurement.
- Level 3:** Inputs are unobservable for the asset or liability and include situations where there is little, if any, market activity for the asset or liability. The inputs into the determination of fair value are based upon the best information in the circumstances and may require significant management judgment or estimation.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The Institute's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the investment. To determine the appropriate levels, the Institute performs a detailed analysis of the assets and liabilities that are subject to the Fair Value Measurement Topic.

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Note 5. Fair Value Measurements (Continued)

The tables below present the balances of assets and liabilities measured at fair value on a recurring basis by level within the hierarchy:

	2018			
	Total	Level 1	Level 2	Level 3
Assets:				
Restricted cash:				
Money market funds	\$ 1,095,769	\$ 1,095,769	\$ -	\$ -
Investments:				
Corporate stocks	\$ 1,684,455	\$ 1,684,455	\$ -	\$ -
Equity mutual funds	161,271	161,271	-	-
	\$ 1,845,726	\$ 1,845,726	\$ -	\$ -
Investments held for split-interest agreements:				
Domestic equity mutual funds	\$ 247,998	\$ 247,998	\$ -	\$ -
Fixed income mutual funds	154,535	154,535	-	-
Money market fund	1,817	1,817	-	-
	\$ 404,350	\$ 404,350	\$ -	\$ -
Interest rate swap contract	\$ 481,745	\$ -	\$ 481,745	\$ -
Annuity obligation	\$ 200,493	\$ -	\$ -	\$ 200,493
	2017			
	Total	Level 1	Level 2	Level 3
Assets:				
Restricted cash:				
Money market funds	\$ 853,173	\$ 853,173	\$ -	\$ -
Investments:				
Corporate stocks	\$ 2,687,842	\$ 2,687,842	\$ -	\$ -
Equity mutual funds	217,503	217,503	-	-
	\$ 2,905,345	\$ 2,905,345	\$ -	\$ -
Investments held for split-interest agreements:				
Domestic equity mutual funds	\$ 129,153	\$ 129,153	\$ -	\$ -
Fixed income mutual funds	69,670	69,670	-	-
Money market fund	6,018	6,018	-	-
	\$ 204,841	\$ 204,841	\$ -	\$ -
Interest rate swap contract	\$ 215,605	\$ -	\$ 215,605	\$ -
Annuity obligation	\$ 61,370	\$ -	\$ -	\$ 61,370

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Note 6. Property and Equipment

Property and equipment as of July 31, 2018 and 2017, and the related accumulated depreciation, are as follows:

	2018	2017
Land	\$ 2,060,000	\$ 2,060,000
Building and improvements	8,521,598	8,521,598
Leasehold improvements	7,593	7,593
Furniture and equipment	184,038	211,896
Software development costs	213,732	213,732
	<u>10,986,961</u>	<u>11,014,819</u>
Less accumulated depreciation	(740,899)	(550,040)
	<u>\$ 10,246,062</u>	<u>\$ 10,464,779</u>

Note 7. Lines of Credit

On September 26, 2016, the Institute obtained a line of credit with SunTrust Bank for \$500,000, which requires monthly payments of interest at a variable rate of London Interbank Offered Rate (LIBOR), plus 1.75% per annum. The principal payable is due on March 31, 2019.

Under the line of credit agreement, the Institute is subject to a number of covenants, including requirements to maintain a specified debt service coverage ratio at the end of each fiscal year. The Institute was not in compliance with two of the financial covenants for the year ended July 31, 2018, which was waived by the lender on January 30, 2019.

Note 8. Long-Term Debt

On September 26, 2016, the Institute closed on its purchase of land and building for \$10.3 million, which includes the space it previously leased. In connection with the purchase of the leased property, the Institute obtained partial financing through the issuance of \$8.5 million District of Columbia Revenue Bonds, Series 2016 (the Bonds). The Bonds were purchased by SunTrust (the Bank) and mature on October 1, 2041, and subject to mandatory repurchase on October 1, 2026. The Bonds are secured by all facilities of the Institute.

The Bonds bear interest at the Adjusted LIBOR, which is the per annum rate equal to the product of (x) 70%, multiplied by the sum of (i) LIBOR, plus (ii) 183 basis points and (y) the Margin Rate Factor, which is 1.0 and subject to adjustments based on changes in the Maximum Federal Corporate Tax Rate, which as of July 31, 2018 and 2017 was 4.93% and 3.5%, respectively. Principal and interest payments began November 1, 2016.

Notes payable, net, consists of the following at July 31, 2018 and 2017:

	2018	2017
Notes payable	\$ 8,057,000	\$ 8,314,000
Less unamortized debt issuance costs	(130,130)	(146,309)
	<u>\$ 7,926,870</u>	<u>\$ 8,167,691</u>

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Note 8. Long-Term Debt (Continued)

Annual principal payments on the Bonds are due in future years as follows:

	<u>Amount</u>
Years ending July 31:	
2019	\$ 262,000
2020	268,000
2021	275,000
2022	282,000
2023	289,000
Thereafter	6,681,000
	<u>\$ 8,057,000</u>

To protect the Institute against a rise in interest rates, the Institute executed an interest rate swap agreement, whereby the Institute receives a variable interest rate of 70% of LIBOR and pays a fixed rate of 1.073%. The all-in synthetic fixed rate is 2.354% after factoring in the bond credit spread of 1.281%. The notional amount is equal to the declining principal of the Bonds as required principal payments are made. The swap was effective on September 26, 2016, and terminates on October 1, 2026. The Institute recognized a gain of \$266,140 and \$215,605 under this swap contract for the years ended July 31, 2018 and 2017, respectively.

Under the Bond agreement, the Institute is subject to a number of covenants, including requirements to maintain a specified debt service coverage ratio and a minimum unrestricted liquidity of no less than \$1 million at the end of each fiscal year. The Institute was not in compliance with two of the financial covenants for the year ended July 31, 2018, which was waived by the lender on January 30, 2019.

Interest expense for the years ended July 31, 2018 and 2017, was \$249,856 and \$184,528, respectively.

Note 9. Commitments and Contingencies

Employment agreement: The Institute has in place a signed employment agreement with its President, which expires on July 31, 2023, subject to the termination provisions in the agreement. Under the agreement, the President is entitled to a one-year sabbatical, or alternatively, two half-year sabbatical leaves, during which he is entitled to all of the benefits and annual compensation provided under his agreement. As of July 31, 2018 and 2017, as it is determined that in the future, when the President takes the sabbatical leave, he will continue to perform work to benefit the Institute, the sabbatical benefit is not accrued.

Capital leases: The Institute has entered into three capital leases for purposes of acquiring office equipment, which expire at various dates through fiscal 2023. Future minimum lease payments due under the equipment leases in effect at July 31, 2018, are as follows:

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Note 9. Commitments and Contingencies (Continued)

	Amount
Years ending July 31:	
2019	\$ 16,801
2020	9,657
2021	9,478
2022	9,478
2023	5,529
Subtotal	50,943
Less imputed interest	(1,575)
	<u>\$ 49,368</u>

Federal program: The Institute participates in federally assisted programs (direct student loans), which are subject to financial and compliance audits by the grantors or their representatives. As such, there exists a contingent liability for potential questioned costs that may result from such audits. These grants are related to student financial aid. Management does not anticipate any significant adjustments as a result of such audits.

Note 10. Temporarily Restricted Net Assets

Temporarily restricted net assets include donor-restricted funds, which are only available for program activities or general support designated for future years. During the years ended July 31, 2018 and 2017, changes in temporarily restricted net assets were as follows:

	2018			
	July 31, 2017	Additions	Releases	July 31, 2018
Contributed instructional and administrative space	\$ -	\$ -	\$ -	\$ -
Institutional support	-	-	-	-
Aldona scholarship	200,000	100,000	(75,000)	225,000
PhD program	20,000	200,000	(60,000)	160,000
Time restricted pledges	2,444,033	5,614	(839,222)	1,610,425
Other	56,500	65,375	(54,500)	67,375
Endowment earnings	73,275	14,246	(18,211)	69,310
	<u>\$ 2,793,808</u>	<u>\$ 385,235</u>	<u>\$ (1,046,933)</u>	<u>\$ 2,132,110</u>

	2017				
	July 31, 2016	Additions	Releases	Reclass	July 31, 2017
Contributed instructional and administrative space	\$ 10,324	\$ -	\$ (10,324)	\$ -	\$ -
Institutional support	18,987	-	(18,987)	-	-
Aldona scholarship	-	200,000	-	-	200,000
PhD program	-	120,000	(100,000)	-	20,000
Time restricted pledges	2,741,251	850,000	(1,147,218)	-	2,444,033
Other	21,000	39,500	(4,000)	-	56,500
Endowment earnings	27,036	73,275	(14,878)	(12,158)	73,275
	<u>\$ 2,818,598</u>	<u>\$ 1,282,775</u>	<u>\$ (1,295,407)</u>	<u>\$ (12,158)</u>	<u>\$ 2,793,808</u>

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Note 11. Endowment

The Institute follows the FASB Codification topic related to endowments of nonprofit organizations, which provides guidance on the net asset classification of donor-restricted endowment funds for a nonprofit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA). UPMIFA is a model act approved by the Uniform Law Commission (ULC, formerly known as the National Conference of Commissioners on Uniform State Laws) that serves as a guideline for states to use in enacting legislation. In 2008, the District of Columbia enacted UPMIFA. Under UPMIFA, all unappropriated endowment fund assets are considered restricted.

The Board of Trustees 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 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 applicable donor gift instruments at the time the accumulation is added to the fund. 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 Institute in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Institute considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the fund
- The purposes of the Institute and the donor-restricted endowment fund
- General economic conditions
- The possible effects of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Institute
- The investment policies of the Institute

The Institute's endowment consists of five individually named endowments funds, three of which are permanently restricted with two others board-designated to function as endowments (quasi-endowment) to support mainly qualifying faculty appointments and scholarships. Assets related to the endowment funds are included in the investments and restricted cash in the statements of financial position. As required by GAAP, net assets associated with donor-restricted endowment funds are classified and reported based on the temporarily restricted unexpended endowment earnings and permanently restricted net assets.

Funds with deficiencies: 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 Institute to retain as a fund for perpetual duration. In accordance with GAAP, deficiencies of this nature are reported as a reduction of unrestricted net assets. There were no deficiencies as of July 31, 2018 and 2017.

Return objectives and risk parameters: Management of the endowment assets is designed to ensure a total return (income, plus capital change) necessary to preserve and enhance (in real dollar terms) the principal of the fund and, at the same time, provide a dependable source of support for current operations and programs. Therefore, the Institute's goal for its endowment funds is to preserve and enhance purchasing power after accounting for investment returns, spending and inflation (but excluding gifts).

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Note 11. Endowment (Continued)

Strategies employed for achieving objectives: Reasonable diversification is sought at all times. Experience has shown financial markets and inflation rates are cyclical and, therefore, control of volatility will be achieved through diversification of asset classes and selection of managers of diverse investment styles. The Board of Trustees examines the correlation of the investment portfolio and it has historically had positive returns.

Spending policy: The Institute's policy is to appropriate 3% of the average of the previous three fiscal years' beginning period endowment values each year.

The Institute's endowment balances, by net asset classification, are as follows as of July 31, 2018 and 2017:

	2018			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Board-designated endowment	\$ 355,401	\$ -	\$ -	\$ 355,401
Donor-restricted endowment	-	69,310	1,261,820	1,331,130
	<u>\$ 355,401</u>	<u>\$ 69,310</u>	<u>\$ 1,261,820</u>	<u>\$ 1,686,531</u>

	2017			Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	
Board-designated endowment	\$ 1,462,188	\$ -	\$ -	\$ 1,462,188
Donor-restricted endowment	-	73,275	1,045,735	1,119,010
	<u>\$ 1,462,188</u>	<u>\$ 73,275</u>	<u>\$ 1,045,735</u>	<u>\$ 2,581,198</u>

The change in endowment net assets for the years ended July 31, 2018 and 2017, is as follows:

	Board-Designated Endowment	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, as of July 31, 2016	\$ 2,276,005	\$ 27,036	\$ 1,658,095	\$ 3,961,136
Reclassification of endowment funds due to donor release:	762,158	(12,158)	(750,000)	-
Interest and dividends	52,894	13,077	-	65,971
Net appreciation in the fair value of investments (unrealized and realized)	266,812	60,198	-	327,010
Contributions	-	-	137,640	137,640
Releases	(1,895,681)	-	-	(1,895,681)
Amounts appropriated for expenditure	-	(14,878)	-	(14,878)
Endowment net assets, as of July 31, 2017	1,462,188	73,275	1,045,735	2,581,198
Interest and dividends	14,200	9,303	-	23,503
Net appreciation in the fair value of investments (unrealized and realized)	69,013	4,943	-	73,956
Contributions	-	-	216,085	216,085
Releases	(1,190,000)	-	-	(1,190,000)
Amounts appropriated for expenditure	-	(18,211)	-	(18,211)
Endowment net assets, as of July 31, 2018	<u>\$ 355,401</u>	<u>\$ 69,310</u>	<u>\$ 1,261,820</u>	<u>\$ 1,686,531</u>

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Note 12. Pension Plan

The Institute maintains a salary reduction defined contribution retirement plan pursuant to Section 403(b) of the IRC. The Institute, at its option, may contribute to the plan on behalf of its eligible employees. The Institute temporarily suspended employer contributions to the plan for all employees in March 2009. The Institute resumed its contribution during the year ended July 31, 2012, with a match up to 5% of employee salaries. Pension expense totaled \$96,493 and \$94,229 for the years ended July 31, 2018 and 2017, respectively.