



BEREA COLLEGE

FINANCIAL STATEMENTS
for the Year Ended June 30, 2017

Board of Trustees

HAROLD L. MOSES, Chair	NASHVILLE, TN
VICKI E. ALLUMS	RESTON, VA
CELESTE ARMSTRONG	PELHAM, AL
*JOHN ALDEN AUXIER	KNOXVILLE, TN
*JAMES T. BARTLETT	BOSTON, MA
CHARLOTTE F. BEASON	LOUISVILLE, KY
VANCE BLADE	LOUISVILLE, KY
NANCY BLAIR	STAMFORD, CT
ANNE BERRY BONNYMAN	ASHEVILLE, NC
JOSEPH "JOE" JOHN BRIDY	NEW YORK, NY
SCOTT CALDWELL	ST LOUIS, MO
DAVID H. CHOW	HOUSTON, TX
*MARTIN A. COYLE	BEMUS POINT, NY
CHARLES CROWE	OAK RIDGE, TN
M. ELIZABETH CULBRETH	WAYNESVILLE, NC
JOHN E. FLEMING	YELLOW SPRINGS, OH
MICHAEL D. FLOWERS	MORGANTOWN, WV
DONNA S. HALL	LEXINGTON, KY
ROBERT F. HAWKS	PEACHTREE CITY, GA
SCOTT M. JENKINS	ROSEMONT, PA
GLENN R. JENNINGS	BEREA, KY
SHAWN C. D. JOHNSON	BOSTON, MA
NANCY LAMPTON	LOUISVILLE, KY
EUGENE Y. LOWE, JR.	EVANSTON, IL
*ELISSA MAY-PLATTNER	CAMP SPRINGS, KY
BETTY H. OLINGER	BEREA, KY 40403
*THOMAS H. OLIVER	ST. HELENA ISLAND, SC
DOUGLAS M. ORR	BLACK MOUNTAIN, NC
THOMAS W. PHILLIPS	ONEIDA, TN
WILLIAM B. RICHARDSON	WHITESBURG, KY
LYLE D. ROELOFS	BEREA, KY
DENNIS R. ROOP	AURORA, CO
CHARLES WARD SEABURY, II	THOUSAND OAKS, CA
DAVID E. SHELTON	WILKESBORO, NC
*DAVID SWANSON	BRUNSWICK, ME
DAVID SLOAN	FT. MITCHELL, KY
TYLER S. THOMPSON	LOUISVILLE, KY
ROCKY S. TUAN	PITTSBURGH, PA
*R. ELTON WHITE	SARASOTA, FL
*DAWNEDA F. WILLIAMS	WISE, VA
ROBERT T. YAHNG	LARKSPUR, CA
STEPHANIE BOWLING ZEIGLER	ROWAYTON, CT

*Honorary Trustees

Officers

LYLE D. ROELOFS, President
CHAD BERRY, Academic Vice President and Dean of the Faculty
DERRICK SINGLETON, Vice President for Operations and Sustainability
JEFFREY S. AMBURGEY, Vice President for Finance
BERNADINE DOUGLAS, Vice President for Alumni and College Relations
VIRGIL BURNSIDE, Vice President for Labor and Student Life
LINDA STRONG-LEEK, Vice President for Diversity and Inclusion
JUDGE B. WILSON, II, Secretary

CONTENTS

	<u>Page</u>
Highlights	2
Report of the Vice President for Finance.....	3-4
Responsibility for the College's Financial Statements.....	5
Independent Auditors' Report.....	6-7
Statements of Financial Position.....	8-9
Statements of Activities	10-11
Statements of Cash Flows.....	12
Notes to Financial Statements.....	13-31

HIGHLIGHTS

	As of or for the Year Ended	
	June 30,	
	2017	2016
OPERATING REVENUE	\$ 116,334,643	\$ 114,135,168
OPERATING EXPENSES	\$ 104,699,869	\$ 102,374,199
OPERATING REVENUE IN EXCESS OF OPERATING EXPENSES	\$ 11,634,774	\$ 11,760,969
ADDITIONS TO PROPERTY, PLANT AND EQUIPMENT	\$ 38,387,123	\$ 18,251,377
LONG-TERM INVESTMENTS OF THE ENDOWMENT		
Original gift value	\$ 509,400,542	\$ 492,794,608
Investments at market	\$ 1,150,360,300	\$ 1,050,679,900
Interest and dividends, net	\$ 22,655,705	\$ 20,257,993
Return	2.2%	1.9%
Market price change	\$ 113,107,660	\$ (33,985,025)
Return	10.9%	-3.0%
Total return	\$ 135,763,365	\$ (13,727,032)
Percent - time weighted	13.1%	-1.1%
CASH AND IN-KIND CONTRIBUTIONS		
Cash gifts	\$ 28,970,867	\$ 47,082,791
Bequests	12,368,004	11,357,588
Total cash gifts	41,338,871	58,440,379
Gifts-in-kind	81,801	709,300
Total College gifts	41,420,672	59,149,679
Agency gifts	15,950	-
Total	\$ 41,436,622	\$ 59,149,679

REPORT OF THE VICE PRESIDENT FOR FINANCE

September, 2017

To the Board of Trustees, President Roelofs,
and Friends of Berea College,

As we have prepared the College's financial statements, we are reminded of the shared responsibility to be excellent stewards of the College's financial resources. For 162 years, Berea College has served men and women of many races from the Appalachian Region and beyond. Today, the College is a very diverse community. As we reflect on the great mission and accomplishments of the College, let us also pause to reflect on the many challenges that Berea has successfully faced over the years, and be mindful of the challenges that will undoubtedly be faced in the future.

With support from over 400 alumni and friends, almost \$168,000 was raised during Berea's first Giving Day, making it a huge success. During 2017, the dollar amount of gifts received from Berea College Advancement efforts was \$24.8 million compared to \$21.4 million in 2016. Not only did the dollar amount of gifts increase, the number of gifts increased from 23,840 to 27,269 and the number of donors increased from 10,334 to 11,297. In addition to the gift amounts noted above, a large external trust donated \$15.7 million and \$37.1 million in 2017 and 2016, respectively. External programs raised an additional \$0.9 million in 2017 and \$0.6 million in 2016. One of the most exciting giving statistics during the year was that approximately fifty-eight percent of Berea's students were 'Berea Patrons' (currently enrolled student donors) with student donors increasing from 839 to 933.

Construction continues on the Margaret A. Cargill Natural Sciences and Health Building. In April, 2017 we celebrated a milestone in the construction, the "topping off" ceremony. The audience watched as a crane lifted the structure's final beam—signed by donors and supporters of the project, and decorated with an American flag and Berea College pennants—and maneuvered it into position atop the building's steel framework. The construction remains on schedule and under budget. Move-in of the Division I departments is planned for the summer of 2018, and classes will be held in the building starting in the fall of 2018.

Residence hall renovations continue on campus. Renovation of Seabury Residence Hall was completed in August, 2017. The 9,800 square feet of interior existing Seabury Residence Hall was completely renovated and approximately 5,200 square feet of additions were constructed and included an expansion area for the residence rooms and common areas on the southwest side of the existing three-story building. The new 15,000 square foot facility will house 52 students.

College and university endowments continue to be in the national limelight. Berea College was invited, along with a few other schools, to testify at the House Ways and Means Oversight Subcommittee hearing in September, 2016 in Washington, DC. The hearing was entitled *Back to School: A Review of Tax-Exempt College and University Endowments* and was centered on the role and use of college and university endowments and their potential impact on areas such as college access and affordability. I had the privilege of representing the College at the hearing and being able to emphasize the importance of the endowment as the financial lifeblood that funds the extraordinary mission of access and affordability that Berea College provides to the lowest economic tier of students attending postsecondary education in the United States. Hopefully, no actions will ever be taken to reduce the dollars available to fund Tuition Promise Scholarships for Berea College students.

Financial Position

The market value of the endowment increased significantly during the year. The endowment increased from \$1,050.7 million on June 30, 2016 to \$1,150.4 million on June 30, 2017, an increase of \$99.7 million. The \$1,150.4 million is composed of cumulative original gifts and other additions of \$509.4 million and cumulative net market appreciation after endowment spending of \$641.0 million. The market value of the quasi endowment portion of the investments as of June 30, 2017, was \$520.9 million, or 45% of the total endowment investments. The net investment return for the total endowment was 13.1% for the fiscal year ending June 30, 2017. The average annual compound rates of return for the 20-year, 10-year, 5-year and 3-year periods ending June 30, 2017 are 6.9%, 3.7%, 7.6%, and 3.9%, respectively. During the year, \$16.6 million was added to the endowment as a result of new gifts, matured split-interest agreements and other additions, and \$52.7 million was distributed from the endowment in support of College operations.

Operating results and financial position of the College remain strong. Operating revenue in excess of operating expenses amounted to \$11.6 million. **Total Net Assets** (total assets less liabilities) of the College were \$1,464.1 million, increasing by \$129.0 million or 9.7 percent during the year. This change reflects an increase in the market value of total long-term investments during the year from \$1,106.2 million as of June 30, 2016 to \$1,208.9 million as of June 30, 2017.

At June 30, 2017, **Total Assets** of the College were \$1,544.0 million. Of this amount, long-term investments (including endowment funds, annuity and life income funds and other funds) comprised \$1,208.9 million; net property, plant and equipment totaled \$209.2 million; and current assets totaled \$107.6 million. Long-term contributions receivable and bequests in probate totaled \$16.7 million; non-current prepaid expenses totaled \$0.8 million; and long-term receivables totaled approximately \$0.8 million.

Total Liabilities decreased by \$1.1 million from \$80.9 million as of June 30, 2016 to \$79.8 million as of June 30, 2017. Most of this decrease was due to a \$4.3 million decrease in debt partially offset by an increase in accounts payable for capital construction projects.

Concluding Comments

While the U.S. economy continues to strengthen and financial markets respond positively, expected investment returns are projected to be relatively low compared to earlier periods. In April, 2017 the Board of Trustees dedicated a significant amount of time discussing the challenges of a low investment return environment and maintaining the purchasing power of the endowment over time while funding the College's operating budget on a fully sustainable basis.

However, throughout its history, Berea College has faced significant challenges and has emerged a stronger institution while remaining true to its core mission. We are confident that our investment in young lives of great promise will reap immeasurable results as our students develop their innate strengths through experiences at Berea and then move on to apply these strengths, as have our graduates before them, to serve others in valuable ways. Your legacy of thoughtful and generous support will live on in their aspirations and achievements.

Please visit us on campus whenever possible.

Respectfully submitted
Respectfully submitted,



Jeffrey S. Amburgey
Vice President for Finance

RESPONSIBILITY FOR THE COLLEGE'S FINANCIAL STATEMENTS

The Office of Financial Affairs of Berea College is directly responsible for the preparation, integrity and fair presentation of the financial statements and the other information included in this annual report. This office, through the Vice President for Finance, reports directly to the President of the College with oversight by the College's Board of Trustees.

The College maintains a system of internal controls over financial reporting, which is designed to provide reasonable assurance to the College's administration and Board of Trustees that the College's assets are protected and that transactions and events are recorded properly in the financial statements.

The College's financial statements have been audited by the independent accounting firm of Crowe Horwath LLP, which was given unrestricted access to all financial records and related data, including minutes of all meetings of trustees. The Vice President for Finance and personnel of the Office of Financial Affairs believe that the representations made to the independent auditors during their audit were valid and appropriate in all material respects.

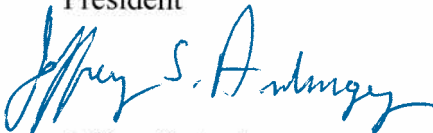
The Board of Trustees of Berea College, through the Audit Committee comprised of trustees not employed by the College, has adopted an Audit Committee Charter that includes engaging the independent auditors and meeting with the College administration, the College's internal auditor, and the independent auditors to ensure that each is carrying out its responsibilities and to discuss auditing, internal control, and financial reporting matters. The independent auditors have full and free access to the Audit Committee and meet with the Audit Committee at least annually.

We believe the following financial statements present fairly, in all material respects, the financial position of the College as of June 30, 2017 and 2016, and the changes in its net assets and cash flows for the years then ended.

September, 2017



Lyle D. Roelofs
President



Jeffrey S. Amburgey
Vice President for Finance

INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees
Berea College
Berea, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of Berea College, which comprise the statements of financial position as of June 30, 2017 and 2016, 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 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 Berea College as of June 30, 2017 and 2016, 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 Matter

Our audits were conducted for the purpose of forming an opinion on the 2017 and 2016 financial statements as a whole. The accompanying highlights and report of the Vice President for Finance, as noted on the table of contents, are presented for purposes of additional analysis and are not a required part of the financial statements. The 2017 and 2016 highlights and report of the Vice President for Finance have not been subjected to the auditing procedures applied in the audits of the 2017 and 2016 financial statements and accordingly, we do not express an opinion or provide any assurance on it.

Crowe Horwath LLP

Crowe Horwath LLP

Lexington, Kentucky
September 8, 2017

Berea College

STATEMENTS OF FINANCIAL POSITION

	June 30,	
	2017	2016
<u>ASSETS</u>		
CURRENT ASSETS		
Cash and cash equivalents	\$ 77,870,619	\$ 90,294,783
Accrued interest on investments	506,593	492,921
Accounts receivable - U.S. Government	5,868,345	6,144,262
Other accounts receivable	1,148,613	1,079,662
Inventories	1,207,698	1,212,416
Prepaid expenses and other assets	1,066,758	744,220
Contributions receivable and bequests in probate	19,898,012	18,632,214
Total current assets	107,566,638	118,600,478
PREPAID EXPENSES AND OTHER ASSETS	853,141	673,131
CONTRIBUTIONS RECEIVABLE AND BEQUESTS IN PROBATE	16,672,225	10,248,455
LONG-TERM RECEIVABLES		
Institutional student loans	779,914	1,138,787
Federal student loans	33,953	41,484
Total long-term receivables	813,867	1,180,271
LONG-TERM INVESTMENTS		
Donor restricted endowment	629,421,300	575,463,000
Board designated endowment	520,939,000	475,216,900
Annuity and life income	24,533,700	24,103,000
Funds held in trust by others	29,017,000	26,783,000
Other investments	4,954,000	4,662,500
Total long-term investments	1,208,865,000	1,106,228,400
NET PROPERTY, PLANT AND EQUIPMENT	209,194,467	179,098,114
Total assets	\$ 1,543,965,338	\$ 1,416,028,849

See notes to financial statements.

Berea College

STATEMENTS OF FINANCIAL POSITION

	June 30,	
	2017	2016
<u>LIABILITIES AND NET ASSETS</u>		
CURRENT LIABILITIES		
Accounts payable and accrued expenses	\$ 7,072,636	\$ 7,512,300
Accounts payable - capital construction projects	6,650,004	3,149,910
Accrued salaries and wages	3,695,135	3,576,988
Deposits and agency funds	660,872	606,141
Deferred income	150,743	228,241
Current portion of interest rate swap valuation	568,414	718,943
Current maturities of long-term debt	3,577,966	3,713,815
Total current liabilities	<u>22,375,770</u>	<u>19,506,338</u>
LONG-TERM LIABILITIES		
Actuarial liability for annuities payable and other liabilities	14,216,648	11,674,212
Deferred financing expense	(430,462)	(394,344)
Interest rate swap valuation	4,514,586	6,778,057
Long-term debt	39,146,807	43,319,772
Total long-term liabilities	<u>57,447,579</u>	<u>61,377,697</u>
Total liabilities	<u>79,823,349</u>	<u>80,884,035</u>
NET ASSETS		
Unrestricted -		
For current operations	99,760	99,680
Designated for specific purposes	56,388,869	49,703,671
Invested in property, plant and equipment	70,944,914	65,434,855
Support of future operations from:		
Contributions receivable and bequests in probate	8,622,710	8,719,058
Donor restricted endowment funds	(1,708,861)	(4,611,854)
Board designated endowment funds	520,939,000	475,216,900
Total unrestricted	<u>655,286,392</u>	<u>594,562,310</u>
Temporarily restricted -		
Unexpended contributions restricted for operations	23,863,657	15,718,097
Unexpended contributions restricted for plant renewals and replacement	19,685,034	38,740,998
Annuity and life income contracts	5,626,385	6,381,933
Expended contributions for long-lived assets being amortized	87,263,248	58,383,472
Donor restricted endowment funds	373,092,933	330,282,237
Total temporarily restricted	<u>509,531,257</u>	<u>449,506,737</u>
Permanently restricted -		
Loan funds	2,940,944	2,891,035
Annuity and life income contracts	6,069,715	7,365,867
Contributions receivable and bequests in probate	3,259,453	4,243,248
Funds held in trust by others	29,017,000	26,783,000
Donor restricted endowment funds	258,037,228	249,792,617
Total permanently restricted	<u>299,324,340</u>	<u>291,075,767</u>
Total net assets	<u>1,464,141,989</u>	<u>1,335,144,814</u>
Total liabilities and net assets	<u>\$ 1,543,965,338</u>	<u>\$ 1,416,028,849</u>

See notes to financial statements.

STATEMENTS OF ACTIVITIES

Changes in Unrestricted Net Assets

	Year Ended June 30.	
	2017	2016
OPERATING REVENUE		
Spendable return from long-term investments	\$ 47,250,668	\$ 46,518,168
Gifts and donations	6,952,098	5,982,880
Federal grants	27,162,529	31,103,217
Cost of education fees paid by federal and state scholarships	3,400,000	3,700,000
Fees paid by students	1,325,111	1,217,227
Other income	4,220,999	3,380,377
Residence halls and dining service	8,648,486	8,665,451
Student industries and rentals	4,465,037	4,419,676
Net assets released from restrictions	16,586,449	13,080,188
Gross operating revenue	120,011,377	118,067,184
Less: Student aid	(3,676,734)	(3,932,016)
Net operating revenue	116,334,643	114,135,168
OPERATING EXPENSES		
Program Services -		
Instruction	25,473,035	24,554,351
Public service	24,910,663	26,639,333
Academic support	10,136,305	10,130,073
Student services	10,726,530	10,127,496
Residence halls and dining service	9,850,044	9,539,534
Student industries and rentals	5,457,895	5,405,061
Total Program Services	86,554,472	86,395,848
Support Services, including fund raising expense of \$5,567,363 in 2017 and \$5,571,308 in 2016	18,145,397	15,978,351
Total operating expenses	104,699,869	102,374,199
Operating revenue in excess of operating expenses	11,634,774	11,760,969
OTHER UNRESTRICTED ACTIVITY		
Gain on sale of property, plant and equipment	40,738	172,131
Gain (loss) on valuation of interest rate swaps	2,414,000	(2,288,600)
Total other unrestricted activity	2,454,738	(2,116,469)
REVENUES DESIGNATED FOR LONG-TERM INVESTMENT		
Unrestricted bequests	6,014,208	9,028,924
Matured annuity and life income contracts	336,320	108,927
Investment return more (less) than amounts designated for current operations	40,284,042	(31,802,215)
Total increase (decrease) in revenues designated for long-term investment	46,634,570	(22,664,364)
Increase (decrease) in unrestricted net assets	\$ 60,724,082	\$ (13,019,864)

See notes to financial statements.

STATEMENTS OF ACTIVITIES

Changes in Total Net Assets

	Year Ended June 30,	
	2017	2016
UNRESTRICTED NET ASSETS		
Operating revenue in excess of operating expenses	\$ 11,634,774	\$ 11,760,969
Other unrestricted activity	2,454,738	(2,116,469)
Increase (decrease) in revenues designated for long-term investment	46,634,570	(22,664,364)
Increase (decrease) in unrestricted net assets	60,724,082	(13,019,864)
TEMPORARILY RESTRICTED NET ASSETS		
Restricted gifts and donations	29,702,093	40,421,432
Restricted spendable return on endowment investments	5,265,045	5,062,412
Investment return more (less) than amounts designated for current operations	42,790,425	(33,672,272)
Net adjustment of annuity payment and deferred giving liability	(517,614)	(496,744)
Reclassification of net assets released from restrictions	(16,586,449)	(13,080,188)
Reclassification of matured annuity and life income contracts to revenues designated for long-term investment	(336,320)	(108,927)
Reclassification of net assets	(292,660)	(221,037)
Increase (decrease) in temporarily restricted net assets	60,024,520	(2,095,324)
PERMANENTLY RESTRICTED NET ASSETS		
Gifts and donations	6,441,840	2,052,782
Restricted return on endowment investments	173,186	166,875
Restricted capital gain (loss) on funds held in trust by others	2,234,000	(1,213,200)
Net adjustment of annuity payment and deferred giving liability	(893,113)	(274,587)
Reclassification of net assets	292,660	221,037
Increase in permanently restricted net assets	8,248,573	952,907
Total increase (decrease) in net assets	128,997,175	(14,162,281)
NET ASSETS		
Beginning of year	1,335,144,814	1,349,307,095
End of year	\$ 1,464,141,989	\$ 1,335,144,814

See notes to financial statements.

STATEMENTS OF CASH FLOWS

	Year Ended June 30,	
	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Increase (decrease) in net assets	\$ 128,997,175	\$ (14,162,281)
Adjustments to reconcile decrease in net assets to net cash used in operating activities -		
Realized and unrealized (gain) loss on long-term investments	(117,954,188)	36,121,197
Restricted return on endowment funds	(173,186)	(166,875)
Gifts and bequests for financing activities	(25,928,344)	(46,036,056)
(Increase) decrease in contributions receivable and bequests in probate	(7,689,568)	1,663,661
Gift value of annuity contracts written	(146,119)	(582,921)
Depreciation	8,283,050	8,061,877
Gain on sale of property, plant and equipment	(40,738)	(172,131)
(Gain) loss on revaluation of interest rate swaps	(2,414,000)	2,288,600
(Increase) decrease in other current assets	(124,526)	19,190
Increase in non-current prepaid expenses and other assets other than cash payments for debt issuance costs	(180,010)	(98,740)
Decrease in current liabilities other than capital construction accounts payable and current maturities of long-term debt	(344,284)	(996,435)
Increase (decrease) in actuarial annuity payment liability and other liabilities	2,542,436	(471,606)
(Increase) decrease in deferred debt financing expenses	(36,118)	30,059
Net cash used in operating activities	(15,208,420)	(14,502,461)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of securities held for long-term investment	(93,770,288)	(186,103,645)
Proceeds from sales and maturities of investments	109,233,995	205,175,335
Purchase of property, plant and equipment	(38,387,123)	(18,251,377)
Increase in capital construction accounts payable	3,500,094	1,172,684
Proceeds from sale of property, plant and equipment	48,458	222,656
Decrease in long-term student loans	366,404	25,832
Net cash (used) in provided by investing activities	(19,008,460)	2,241,485
CASH FLOWS FROM FINANCING ACTIVITIES		
Gifts and bequests received for -		
Long-term investment	14,093,897	11,463,809
Property, plant and equipment	11,834,047	34,571,947
Student loans	400	300
Endowment return restricted for long-term investments	173,186	166,875
Repayment of indebtedness	(4,308,814)	(4,192,425)
Net cash provided by financing activities	21,792,716	42,010,506
Net (decrease) increase in cash and cash equivalents	(12,424,164)	29,749,530
Cash and cash equivalents, beginning of year	90,294,783	60,545,253
Cash and cash equivalents, end of year	\$ 77,870,619	\$ 90,294,783

See notes to financial statements.

NOTES TO FINANCIAL STATEMENTS

(1) ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES

General

Berea College (the College) is a not-for-profit institution providing liberal arts education to students with limited family financial resources primarily from the Southern Appalachian Mountain region. All students are provided a full tuition scholarship and, accordingly, the College is dependent on gifts and donations to help provide a low cost but high quality education. The College has one campus located in Berea, Kentucky with an enrollment of approximately 1,600 students and approximately 800 employees.

Basis of Presentation

The financial statements have been prepared on the accrual basis of accounting. The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and judgments that affect the reported amounts of assets, liabilities and disclosures of contingencies at the date of the financial statements and revenues and expenses recognized during the reporting period. Actual results could differ from those estimates.

Under established financial reporting standards for not-for-profit organizations, net assets and revenues, expenses, and gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

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

Temporarily restricted net assets - Net assets subject to donor-imposed stipulations that may or will be met by actions of the College and/or the passage of time.

Unrestricted net assets - Net assets not subject to donor-imposed stipulations. Unrestricted net assets may be designated by the Board of Trustees.

Revenues from sources other than contributions are reported as increases in unrestricted net assets. Contributions are reported as increases in the appropriate category of net assets, except that contributions which impose restrictions that are fully met in the same fiscal year they are recognized are included in unrestricted revenues. Expenses are reported as decreases in unrestricted net assets. Cumulative net appreciation associated with donor-restricted endowments is classified as temporarily restricted net assets (see Note 2). Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications from temporarily restricted net assets to unrestricted net assets.

Contributions, including unconditional promises to give and bequests, are recognized as revenues in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value at the date of the gift. Contributions to be received after one year are discounted at the June 30, five-year Daily Treasury Yield Curve Rate for the fiscal year the pledge was initially recorded, currently at rates ranging from 0.72% to 1.89%. Amortization of the discount is recorded as additional contribution revenue and used in accordance with donor-imposed restrictions, if any, on the contributions. Allowance is made for uncollectible contributions based upon management's judgment and analysis of the creditworthiness of the donors, past collection experience and other relevant factors.

Contributions of exhaustible long-lived assets, or of cash or other assets to be used to acquire them, without donor stipulations concerning the use of such long-lived assets, are reported as revenues of the temporarily restricted net asset class; the restrictions are considered to be released over the estimated useful lives of the long-lived assets using the College's depreciation policies.

NOTES TO FINANCIAL STATEMENTS

(1) ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES (continued)

All contributions of works of art, historical treasures and similar assets, whether held as part of a collection (for education, research or public exhibition rather than for sale) or for sale or other purposes, have been recognized at their estimated fair value at the date of receipt based upon appraisals or similar valuations. All such items, whether contributed or purchased, have been capitalized.

Cash and Cash Equivalents

For financial statement purposes, the College considers all investments (not held for long-term investment) with original maturities of three months or less as cash equivalents. The College maintains cash in bank accounts, which at times may exceed federally insured limits. The College has not experienced any losses on such accounts. The College believes that it is not exposed to any significant credit risk on cash and cash equivalents.

Inventories

Inventories are stated at the lower of cost (weighted average) or market.

Loans

The College makes uncollateralized loans to students based on financial need. At June 30, 2017 and 2016, student loans totaled \$1,073,867 (net of \$475,000 loan loss reserve) and \$1,434,271 (net of \$250,000 loan loss reserve), respectively, of which \$260,000 and \$254,000 for June 30, 2017 and 2016, respectively, are reflected in current assets. Of the net loan totals, \$1,039,914 and \$1,392,787 for June 30, 2017 and 2016, respectively, were funded from institutional resources and the remaining loans were funded through Federal government loan programs. Reserves for loan losses are established when no payments are received for over six months. Loan balances are written off when they are deemed to be permanently uncollectible. Recoveries of student loans receivable previously written off are recorded when received.

Investments

Investments are reported at their respective fair values. The values of publicly traded fixed income and equity securities are based upon quoted market prices. Private equities, including real estate partnerships, and certain other nonmarketable securities are valued using information provided by the general partner or investment manager, such as net asset value, for the respective funds. Other real estate investments are stated at cost on the date of acquisition or fair market value at date of receipt in the case of gifts. Net realized and unrealized gains and losses on investments are reflected in the statements of activities. Gains and losses on investments sold are determined on a specific identification basis.

The College's investments do not have a significant concentration of credit risk within any industry or specific institution.

The market risk inherent in certain College investments is primarily the potential loss arising from adverse changes in quoted market prices on equity securities and in interest rates on fixed income securities. Investment securities, in general, are exposed to various risks, such as interest rates, credit and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the statements of financial position. In an effort to mitigate this market risk, the College has adopted a policy of maintaining a diverse investment pool through the use of strategic allocation guidelines. These guidelines require that the College's investment pool be made up of a mix of publicly traded fixed income and equity securities, hedge funds, private equities and other nonmarketable securities, commodities, and real estate investments.

Derivatives

Derivative instruments, including certain derivative instruments embedded in other contracts, are valued at fair value and are included in the statements of financial position. The change in fair value of such instruments is included in the statements of activities

NOTES TO FINANCIAL STATEMENTS

(1) ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES (continued)

Fair Value of Financial Instruments

Cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and deferred income approximate fair value because of their short-term nature. Contributions receivable approximate fair value because of the present value discount included in the carrying amount. Investments are carried at fair value or approximate fair value as discussed in Note 2. The carrying amount of the annuity and trust liabilities approximates fair value based on life expectancies and the present value discount. The fair value of the College's long-term debt is disclosed in Note 8 and is based on quoted market prices for the same or similar issues, giving consideration to the interest rates, maturity and other factors.

The fair values of financial instruments other than investments, which include the items listed in the preceding paragraph, are based on a variety of factors. In some cases, fair values represent quoted market prices for identical or comparable instruments (Level 1 inputs - market approach). In other cases, fair values have been estimated based on assumptions about the amount and timing of estimated future cash flows and assumed discount rates reflecting varying degrees of risk (Level 2 inputs - income approach). Accordingly, the fair values may not represent actual values that could have been realized at year-end or that will be realized in the future.

Split-Interest Agreements and Interest in Trusts Held by Others

The College's split-interest agreements with donors consist primarily of irrevocable charitable remainder trusts, charitable gift annuities, and life income funds for which the College serves as trustee. Assets held in these split-interest agreements are included in investments. Contribution revenue is recognized at the dates the split-interest agreements are established, net of the liabilities for the present value of the estimated future payments to be made to the donors and/or other beneficiaries. Annually, the College records the change in value of split-interest agreements by marking to fair value the assets that are associated with each agreement and recalculating the liability for the present value of the estimated future payments to be made to the donors and/or other beneficiaries. The discount rate and actuarial assumptions used in calculating the annuity obligation are those provided in Internal Revenue Service guidelines and actuarial tables.

For agreements where the College is not the trustee, the College has recorded its beneficial interest in the agreements as an asset reported in the line item "Contributions Receivable and Bequests in Probate."

Property, Plant and Equipment

Property, plant and equipment are stated at cost at the date of acquisition or fair value at the date of the gift, less accumulated depreciation.

Depreciation on the property, plant and equipment owned by the College has been computed using the straight-line method based on the following composite depreciation guidelines:

Buildings and additions	30 - 75 years
Building improvements and renovations	15 - 30 years
Furniture, equipment and books	2 - 10 years

Using these guidelines, depreciation expense for the years ended June 30 was:

	<u>2017</u>	<u>2016</u>
Educational and general purposes	\$ 7,474,903	\$ 7,293,959
Student industries	<u>808,147</u>	<u>767,918</u>
	<u>\$ 8,283,050</u>	<u>\$ 8,061,877</u>

NOTES TO FINANCIAL STATEMENTS

(1) ORGANIZATION AND SUMMARY OF ACCOUNTING POLICIES (continued)

Equipment with a unit cost of \$5,000 or more and having an estimated useful life of greater than one year is capitalized. Renovations to buildings, infrastructure and land improvements that significantly increase the value or extend the useful life of the structure are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense is incurred. The College capitalizes, but does not depreciate, works of art and historical treasures that are held for education, research or public exhibition.

Unrestricted Bequests

The College follows the policy of designating all unrestricted bequests as additions to the tuition replacement funds. Such bequests are reported as revenues designated for long-term investment in the statements of activities.

Measure of Operations

In its statements of activities, the College includes in its definition of operations all revenues and expenses that are an integral part of its programs and supporting activities. Items excluded are permanently restricted contributions, gifts for capital construction, changes in the value of interest rate swap agreements, investment return less than amounts designated for current operations and certain other non-recurring items. Spendable return from the endowment is calculated using the spending formula adopted by the Board of Trustees. The amount designated for current operations is approved by the Board of Trustees annually.

Functional Allocation of Expenses

The costs of providing the various programs and supporting services have been summarized on a functional basis in the statements of activities. Certain items such as interest expense, depreciation expense and plant operation expenses have been allocated among the programs and supporting services benefited.

	<u>2017</u>	<u>2016</u>
Interest	\$ 1,441,641	\$ 1,493,561
Depreciation	8,283,050	8,061,877
Plant Operations	7,325,381	6,232,214

Reclassification

Certain reclassifications have been made to the 2016 financial statements to conform to the 2017 presentation with no effect on total net assets or the change in net assets.

Upcoming Accounting Pronouncements

In August 2016, the FASB issued (ASU) 2016-14, *Not-for-Profit Entities: Topic 958*. The amendments in this Update affect not-for-profit entities (NFPs) and the users of their general purpose financial statements. The amendments in this Update make certain improvements to the current net asset classification requirements and the information presented in financial statements and notes about a NFP's liquidity, financial performance, and cash flows. The amendments in the ASU are effective for annual financial statements issued for fiscal years beginning after December 15, 2017. The College has not yet implemented this ASU and is in the process of assessing the effect on its financial statements.

NOTES TO FINANCIAL STATEMENTS

(2) LONG-TERM INVESTMENTS

	June 30,	
	2017	2016
Endowment:		
Pooled Investments -		
U. S. equities	\$ 256,191,400	\$ 236,630,600
International equities	351,148,200	295,442,300
Corporate notes and bonds	67,662,500	65,940,900
U. S. Government securities	70,289,100	67,617,700
Private equity - venture capital	464,300	549,900
Private equity - buy out	20,252,200	25,290,600
Private equity - debt funds	18,900	102,800
Private equity - fund of funds	27,193,700	18,849,600
Hedge funds	143,645,500	145,173,600
Special opportunities	58,276,200	68,520,500
Commodities	54,519,300	50,891,600
Short-term investments and cash	95,764,100	70,723,100
Total	1,145,425,400	1,045,733,200
Non Pooled Investments -		
U. S. equities	88,500	103,200
Corporate notes and bonds	19,200	16,300
Real estate	2,766,700	2,766,700
Short-term investments and cash	2,060,500	2,060,500
Total	4,934,900	4,946,700
Total endowment	1,150,360,300	1,050,679,900
Annuity and Life Income:		
U. S. equities	8,219,200	8,169,300
International equities	5,000,900	4,779,800
Corporate notes and bonds	3,772,000	3,779,000
U. S. Government securities	2,418,700	2,410,500
International bonds	1,374,400	1,384,800
Real estate	3,165,900	3,227,300
Insurance policies	101,900	95,700
Short-term investments and cash	480,700	256,600
Total annuity and life income	24,533,700	24,103,000
Funds Held in Trust by Others , where Berea College receives all or a stipulated percent of income	29,017,000	26,783,000
Other Investments	4,954,000	4,662,500
Total long-term investments	\$ 1,208,865,000	\$ 1,106,228,400

NOTES TO FINANCIAL STATEMENTS

(2) LONG-TERM INVESTMENTS (continued)

Hedged equity investments are valued using the net asset value (“NAV”) per share times the number of units held at year end. The objectives of these funds are to achieve superior risk-adjusted returns with low volatility and low correlation to both the equity and fixed income markets by investing in a diversified group of pooled investment vehicles. These funds generally have quarterly liquidity provisions after minimum holding periods have been achieved. The College has satisfied all minimum holding periods. However, at least one of the funds does have “side-pocket” illiquid investments that do not provide for quarterly liquidity. Full liquidations are generally subject to a 10% hold-back to be received after the following fiscal year-end audit has been completed. The College considers the liquidity provisions when making new hedged equity investments.

Private equity and special opportunity investments are generally made through limited partnerships and may have a partnership life ranging from 5 to 15-year terms. Under the terms of such agreements, the College may be required to provide additional funding when capital calls are made by underlying fund managers. These partnerships have a limited existence, and they may provide for annual extensions for the purpose of disposing of portfolio positions and returning capital to investors. However, depending on market conditions, the inability to execute the fund’s strategy, or other factors, a manager may extend or reduce the terms of a fund. The College cannot anticipate such changes because they generally arise from unforeseeable events, but should they occur they could reduce liquidity or originally anticipated investment returns. Accordingly, the timing and amount of capital calls in future years are uncertain. The College invests in multiple private equity and special opportunity funds. The limited partnerships generally invest in the following: (1) buyout funds which invest in more established companies in need of some repair or growth, (2) debt funds which provide lending to companies that are being restructured or re-capitalized, (3) real estate funds which provide capital for new construction, renovation or change in property ownership or management, and (4) venture funds which invest in young companies with varying degrees of infrastructure, revenues and profits.

The College measures the fair value for these investments based on net asset value (“NAV”) as a practical expedient, without further adjustment, unless it is probable that the investment will be sold at a significantly different value. If not determined as of the College’s measurement date, NAV is adjusted to reflect any significant events that would materially affect the security’s value. Certain investments are carried at the latest valuation provided by the fund manager, adjusted by cash receipts and cash distributions through June 30, which approximates fair value. Some attributes that impact the security’s fair value may not be reflected in NAV, including, but not limited to, the investor’s ability to redeem the investment at the measurement date and unfunded purchase commitments. If the College sold all or a portion of its alternative investments, it is reasonably possible that the transaction value could differ significantly from the estimated fair value at the measurement date, because of the nature of the investments, changes in market conditions and the overall economic environment.

The College’s investment objective for its pooled long-term investments is to provide a predictable and growing stream of inflation-adjusted spendable return while maintaining the real (inflation-adjusted) value of the pooled investments. In connection with these investment objectives, the Board of Trustees has adopted a spending formula for determining that part of total return which can be expended annually.

A weighted-average endowment spending formula was adopted by the Board of Trustees effective July 1, 2011. Under the formula, the amount available for spending per unit from the pooled endowment funds is calculated by increasing the prior year’s spendable return by the annual change in the Consumer Price Index for all Urban Consumers compiled by the U. S. Department of Labor, Bureau of Labor Statistics (CPI) for the previous twelve month period plus 0.5% multiplied by a weighting factor of 70%. Added to this amount is 5% of the average market value of the pooled investments for the immediately preceding 6 calendar quarters multiplied by a weighting factor of 30%. To help maintain intergenerational equity and ensure a prudent level of spending, if the endowment spendable return calculated under this formula is less than 4.0% or more than 6.0% of the prior June 30 market value of the pooled endowment, the Board of Trustees determines whether to make any adjustments to the endowment spendable return.

For 2017 and 2016, spendable return under the formulas amounted to \$52,672,369 and \$51,738,600, respectively. In 2017, actual cash income earned on pooled investments, net of \$860,922 for investment management and custodial fees, amounted to \$22,639,175, or \$30,033,194 less than the spendable return provided by the formula. This difference was provided by the accumulated net appreciation earned on investments.

NOTES TO FINANCIAL STATEMENTS

(2) LONG-TERM INVESTMENTS (continued)

The College follows the policy of spending only cash income received on non-pooled endowment investments. Such income amounted to \$16,530 in 2017 and \$8,855 in 2016, while the market value of these investments of \$4,934,900 at June 30, 2017 and \$4,946,700 at June 30, 2016 decreased by \$15,300 in 2017 and increased by \$193,933 in 2016. Additions to non-pooled endowment investments during 2017 and 2016 amounted to \$3,500 and \$99,667, respectively.

Dividend and interest income of \$22,655,705 and \$20,257,993 reported net of external investment manager fees of \$860,922 and \$865,330 is included in the statements of activities for the years ended June 30, 2017 and 2016, respectively.

Effective July 15, 2010, the Commonwealth of Kentucky adopted legislation incorporating the provisions outlined in the Uniform Prudent Management of Institutional Funds Act (UPMIFA). The statutory guidelines relate to prudent management, investment and expenditure of donor-restricted endowments held by charitable organizations. The legislation specifies factors for fiduciaries to consider prior to making a decision to appropriate from or accumulate into an organization's endowment funds.

The College has interpreted the Kentucky enacted version of 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 College 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. Any 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 College in a manner consistent with the standard of prudence prescribed by UPMIFA. From time to time, the fair value of assets associated with an endowed fund may fall below its historical book value. The cumulative value of these deficiencies, totaling \$1,708,861 in 2017 and \$4,611,854 in 2016, is classified as unrestricted net assets.

The College interprets its fiduciary responsibility for donor-restricted endowments under UPMIFA, unless there are donor-specific provisions to the contrary, as preserving intergenerational equity to the extent possible. Under this broad guideline, future endowment beneficiaries should essentially receive at least the same level of economic support that the current generation enjoys. Endowment assets are invested to provide growth of the endowment through real investment return that exceeds spending over the long term. The overarching objective is to meet the College's goal of preserving and enhancing the real (inflation-adjusted) purchasing power of the endowment fund in perpetuity. Assets are invested to provide a stream of earnings to meet spending needs and attain long-term objectives without the assumption of undue risks.

In accordance with UPMIFA, the College considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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

NOTES TO FINANCIAL STATEMENTS

(2) LONG-TERM INVESTMENTS (continued)

During 2017, the unit value of pooled investments changed as follows:

	2016-17			2015-16
	Market Value	Number of Units	Value Per Unit	Time Weighted Return Net of Fees
Beginning Balance	\$ 1,045,733,200	756,319.645	\$ 1,382.660	\$ 1,096,822,800
Market price change	113,122,960		148.533	10.9%
Net income earned	22,639,175		29.933	2.2%
Spendable return	(52,672,369)		(69.643)	-
	<u>83,089,766</u>		<u>108.823</u>	<u>13.1%</u>
Additions	16,602,434	11,657.733	-	14,578,820
Ending Balance	<u>\$ 1,145,425,400</u>	<u>767,977.378</u>	<u>\$ 1,491.483</u>	<u>\$ 1,045,733,200</u>

The total return earned by the endowment investments for the years ended June 30, was:

	2017	2016
Pooled Investments -		
Cash income, net	\$ 22,639,175	\$ 20,249,138
Market price change	113,122,960	(34,178,958)
Non-Pooled Investments -		
Cash income	16,530	8,855
Market price change	(15,300)	193,933
Total Return	<u>\$ 135,763,365</u>	<u>\$ (13,727,032)</u>
Distributed to -		
Unrestricted Net Assets		
Spendable return	\$ 47,250,668	\$ 46,518,168
Long-term investments	40,284,042	(31,802,215)
Temporarily Restricted Net Assets		
Spendable return	5,265,045	5,062,412
Investment return more (less) than amounts designated for current operations	42,790,424	(33,672,272)
Permanently Restricted		
Restricted earnings	173,186	166,875
Total	<u>\$ 135,763,365</u>	<u>\$ (13,727,032)</u>

NOTES TO FINANCIAL STATEMENTS

(2) LONG-TERM INVESTMENTS (continued)

Endowment Investments Net Asset Composition by Type of Fund as of June 30, 2017:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor restricted endowment funds	\$ (1,708,861)	\$ 373,092,933	\$ 258,037,228	\$ 629,421,300
Board designated endowment funds	520,939,000	-	-	520,939,000
	<u>\$ 519,230,139</u>	<u>\$ 373,092,933</u>	<u>\$ 258,037,228</u>	<u>\$ 1,150,360,300</u>

Changes in Endowment Investments Net Assets for the Fiscal Year Ended June 30, 2017:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment investments net assets, beginning of year	\$ 470,605,046	\$ 330,282,237	\$ 249,792,617	\$ 1,050,679,900
Investment return:				
Investment income	22,655,705	-	-	22,655,705
Net gains (realized and unrealized)	50,923,138	62,184,522	-	113,107,660
Total investment return	<u>73,578,843</u>	<u>62,184,522</u>	<u>-</u>	<u>135,763,365</u>
Contributions	-	-	7,371,403	7,371,403
Other restricted additions	-	20,272	873,208	893,480
Board designated additions	8,341,051	-	-	8,341,051
Appropriation of endowment assets for expenditure	<u>(33,294,801)</u>	<u>(19,394,098)</u>	<u>-</u>	<u>(52,688,899)</u>
Endowment investments net assets, end of year	<u>\$ 519,230,139</u>	<u>\$ 373,092,933</u>	<u>\$ 258,037,228</u>	<u>\$ 1,150,360,300</u>

NOTES TO FINANCIAL STATEMENTS

(2) LONG-TERM INVESTMENTS (continued)

Endowment Investments Net Asset Composition by Type of Fund
as of June 30, 2016:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor restricted endowment funds	\$ (4,611,854)	\$ 330,282,237	\$ 249,792,617	\$ 575,463,000
Board designated endowment funds	475,216,900	-	-	475,216,900
	<u>\$ 470,605,046</u>	<u>\$ 330,282,237</u>	<u>\$ 249,792,617</u>	<u>\$ 1,050,679,900</u>

Changes in Endowment Investments Net Assets
for the Fiscal Year Ended June 30, 2016:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment investments net assets, beginning of year	\$ 491,393,318	\$ 363,935,225	\$ 246,147,357	\$ 1,101,475,900
Investment return:				
Investment income	20,257,993	-	-	20,257,993
Net losses (realized and unrealized)	(17,626,694)	(16,358,331)	-	(33,985,025)
Total investment return	<u>2,631,299</u>	<u>(16,358,331)</u>	<u>-</u>	<u>(13,727,032)</u>
Contributions	-	-	1,823,220	1,823,220
Other restricted additions	-	19,284	1,822,040	1,841,324
Board designated additions	11,013,943	-	-	11,013,943
Appropriation of endowment assets for expenditure	<u>(34,433,514)</u>	<u>(17,313,941)</u>	<u>-</u>	<u>(51,747,455)</u>
Endowment investments net assets, end of year	<u>\$ 470,605,046</u>	<u>\$ 330,282,237</u>	<u>\$ 249,792,617</u>	<u>\$ 1,050,679,900</u>

The College's endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As of June 30, 2017, the College has approximately 5,000 individual endowment funds of which approximately 2,000 are donor-restricted funds that are used to provide funding for cost of education for students, direct student aid, various academic support programs, and other restricted uses.

NOTES TO FINANCIAL STATEMENTS

(3) FAIR VALUE MEASUREMENTS

GAAP 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. One key component of the fair value measurement required by GAAP includes the development of a three-tiered fair value hierarchy. Assets and liabilities reported at fair value are placed in one of the three tiers, except as noted below, based upon the "inputs" used to determine fair value at the measurement date. These inputs are summarized in the three broad levels listed below:

Level 1 - quoted prices in active markets for identical assets or liabilities

Level 2 - other significant inputs (including quoted prices of similar securities, interest rates, prepayment spreads, credit risk, etc.)

Level 3 - significant unobservable inputs

The inputs or methodology used to value investments are not necessarily an indication of the risk associated with investing in those securities. For example, money market securities are valued using amortized cost and although amortized cost approximates the fair value of the securities the valuation is not obtained from a quoted price in an active market. Therefore, money market securities are reflected in Level 2.

The following summarizes the fair value of assets and liabilities and the Level 3 reconciliation at June 30, 2017:

	June 30, 2017 Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	NAV ¹
<u>Assets</u>					
Endowment investments:					
Short-term investments and cash	\$ 97,824,600	\$ -	\$ 97,824,600	\$ -	\$ -
U.S. equities	256,279,900	256,279,900	-	-	-
International equities	351,148,200	351,148,200	-	-	-
Fixed income	137,970,800	137,970,800	-	-	-
Private equity	47,929,100	-	-	-	47,929,100
Hedge funds	143,645,500	-	-	-	143,645,500
Commodities	54,519,300	54,519,300	-	-	-
Other endowment investments	61,042,900	-	15,813,500	2,766,700	42,462,700
Building maintenance investments	4,954,000	4,614,754	339,246	-	-
Certificates of deposit	450,301	-	450,301	-	-
Funds held in trust by others	29,017,000	-	-	29,017,000	-
Split-interest agreements	24,533,700	24,533,700	-	-	-
Total assets	<u>\$ 1,209,315,301</u>	<u>\$ 829,066,654</u>	<u>\$ 114,427,647</u>	<u>\$ 31,783,700</u>	<u>\$ 234,037,300</u>
<u>Liabilities</u>					
Interest rate swap agreements	<u>\$ 5,083,000</u>	<u>\$ -</u>	<u>\$ 5,083,000</u>	<u>\$ -</u>	<u>\$ -</u>

¹Investments using Net Asset Value (NAV) as a fair value expedient are not included in the fair value hierarchy, pursuant to the adoption of ASU 2015-07, *Fair Value Measurement*.

NOTES TO FINANCIAL STATEMENTS

(3) FAIR VALUE MEASUREMENTS (continued)

Level 3 Reconciliation

	Balances June 30, 2016	Net realized and unrealized gains and losses included in change in net assets	Purchases, sales, issuances and settlement, net	Net transfers in (out) of Level 3	Balances June 30, 2017
Endowment investments	\$ 2,766,700	\$ -	\$ -	\$ -	\$ 2,766,700
Funds held in trust by others	26,783,000	2,234,000	-	-	29,017,000
Total	<u>\$ 29,549,700</u>	<u>\$ 2,234,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 31,783,700</u>

The College's policy is to recognize transfers in and transfers out as of the actual date of the event or change in circumstance that caused the transfer.

The following summarizes the fair value of assets and liabilities and the Level 3 reconciliation at June 30, 2016:

	June 30, 2016 Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	NAV ¹
<u>Assets</u>					
Endowment investments:					
Short-term investments and cash	\$ 72,783,600	\$ -	\$ 72,783,600	\$ -	\$ -
U.S. equities	236,733,800	236,733,800	-	-	-
International equities	295,442,300	295,442,300	-	-	-
Fixed income	133,574,900	133,574,900	-	-	-
Private equity	44,792,900	-	-	-	44,792,900
Hedge funds	145,173,600	-	-	-	145,173,600
Commodities	50,891,600	50,891,600	-	-	-
Other endowment investments	71,287,200	-	9,656,100	2,766,700	58,864,400
Building maintenance investments	4,662,500	4,384,128	278,372	-	-
Certificates of deposit	450,301	-	450,301	-	-
Funds held in trust by others	26,783,000	-	-	26,783,000	-
Split-interest agreements	24,103,000	24,103,000	-	-	-
Total assets	<u>\$ 1,106,678,701</u>	<u>\$ 745,129,728</u>	<u>\$ 83,168,373</u>	<u>\$ 29,549,700</u>	<u>\$ 248,830,900</u>
<u>Liabilities</u>					
Interest rate swap agreements	<u>\$ 7,497,000</u>	<u>\$ -</u>	<u>\$ 7,497,000</u>	<u>\$ -</u>	<u>\$ -</u>

¹Investments using Net Asset Value (NAV) as a fair value expedient are not included in the fair value hierarchy, pursuant to the adoption of ASU 2015-07, *Fair Value Measurement*.

NOTES TO FINANCIAL STATEMENTS

(3) FAIR VALUE MEASUREMENTS (continued)

Level 3 Reconciliation

	Balances June 30, 2015	Net realized and unrealized gains and losses included in change in net assets	Purchases, sales, issuances and settlement, net	Net transfers in (out) of Level 3	Balances June 30, 2016
Endowment investments	\$ 2,493,300	\$ 273,400	\$ -	\$ -	\$ 2,766,700
Funds held in trust by others	27,996,200	(1,213,200)	-	-	26,783,000
Total	<u>\$ 30,489,500</u>	<u>\$ (939,800)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 29,549,700</u>

The College's policy is to recognize transfers in and transfers out as of the actual date of the event or change in circumstance that caused the transfer.

The following methods and assumptions were used to estimate the fair value for each class of financial instrument measured at fair value:

Endowment and other investments

Short-term investments - The fair value of short-term investments, consisting primarily of money market funds, is classified as Level 2 as these funds are not traded on a regular basis.

Domestic and international equities - Investments in equity mutual funds and equity securities are classified as Level 1 as these funds and securities are traded in active markets for which closing prices are readily available.

Fixed income - Fixed income mutual funds are classified as Level 1 as these funds are traded in an active market for which closing prices are readily available. Separately managed fixed income investments are classified as Level 2 because pricing is based on inputs such as interest rates and credit risk and not from quoted prices in active markets.

Alternative investments - Investments in hedge funds, private equity funds, and funds of funds are measured at fair value using the net asset value per share (or its equivalent) practical expedient and have not been classified in the fair value hierarchy.

Commodities - Classified as Level 1 as quoted prices from active markets are available for these investments.

Funds held in trust by others

The College's beneficial interest in perpetual trusts administered by a third party are classified as Level 3 as the fair values are based on a combination of Level 2 inputs (interest rates and yield curves) and significant unobservable inputs (entity specific estimates of cash flows). Since the College has an irrevocable right to receive the income earned from the trusts' assets, the fair value of the College's beneficial interest is estimated to approximate the fair value of the trusts' assets.

NOTES TO FINANCIAL STATEMENTS

(3) FAIR VALUE MEASUREMENTS (continued)

Split-interest agreements

The College's split-interest agreements in which the College serves as trustee are classified as Level 1 as the underlying assets are invested in publicly traded mutual funds with quoted prices in active markets.

Interest rate swap agreements

Interest rate swap agreements do not have observable market quotes. For these financial instruments the College's swap counterparty, The Bank of New York Mellon, provides an annual valuation using the difference between the fixed rate paid by the College and the counterparty's LIBOR interest rate forecast discounted at the swap yield curve. The model is based on observable inputs for forward interest rates and discount rates. As such, this derivative instrument is classified within Level 2 of the fair value hierarchy.

(4) DERIVATIVE FINANCIAL INSTRUMENTS

The College uses certain derivative financial instruments to maximize investment income to meet target investment returns and to adjust the duration of fixed income investment portfolios. The fair market value of these contracts is reported as a part of the fair value of the underlying financial instruments.

As a strategy to mitigate exposure to the risk of interest rate fluctuations, the College entered into an interest rate swap agreement on the Series 2002A bonds during 2004. This interest rate swap has been designated as a cash flow hedge of long-term debt and provides for the College to receive interest from the counterparty at 70% of one-month LIBOR and to pay interest to the counterparty at a fixed rate of 3.45% on a fixed notional amount of \$18,110,000. Although there are no required principal payments on the 2002A bonds until the June 1, 2032 final maturity date, optional annual principal payments have reduced the outstanding principal balance to \$10,960,000 and \$11,555,000 at June 30, 2017 and 2016, respectively. The average rate received from the interest rate swap counterparty during 2017 and 2016 was 0.52% and 0.24%, respectively, and the average interest rate paid by the College for 2017 and 2016 was 3.45%. The interest rate swap matures in 2032. Total net interest expensed during 2017 and 2016 was \$530,405 and \$583,163 respectively, and is allocated to various expenses by function in the statements of activities. The expected fair value of the swap to be amortized in the next fiscal year is \$413,083.

During 2004 the College entered into an additional interest rate swap agreement on the Series 2003B bonds. The interest rate swap has been designated as a cash flow hedge of long-term debt and provides for the College to receive interest from the counterparty at 70% of one-month LIBOR and to pay interest to the counterparty at a fixed rate of 3.746% on a notional amount of \$6,120,000 and \$6,515,000 at June 30, 2017 and 2016, respectively. The notional amount of the swap agreement amortizes at the same rate as the underlying bond series. The average rate received during from the interest rate swap counterparty during 2017 and 2016 was 0.52% and 0.24%, respectively, and the average interest rate paid by the College for 2017 and 2016 was 3.746%. The interest rate swap matures in 2029. Total net interest expensed during 2017 and 2016 was \$209,141 and \$241,349, respectively, and is allocated to various expenses by function in the statements of activities. The expected fair value of the swap to be amortized in the next fiscal year is \$155,331.

Under the agreements, the College pays or receives the net interest amount monthly, with the monthly settlements included in interest expense. The agreements are recorded at fair value with subsequent changes in fair value included in the changes in net assets in the statements of activities. The valuation of the two interest rate swaps at June 30, 2017 and 2016 resulted in a liability of \$5,083,000 and \$7,497,000, respectively. If the agreements remain in force until maturity, the College will have no remaining liability related to swaps.

NOTES TO FINANCIAL STATEMENTS

(5) DEFINED CONTRIBUTION RETIREMENT PLAN

The College has a defined contribution retirement plan covering all eligible employees with one or more years of service. Costs of the plan are expensed as incurred and aggregated \$2,578,383 in 2017 and \$2,429,966 in 2016.

(6) PROPERTY, PLANT AND EQUIPMENT

The major categories of property, plant and equipment as of June 30 were:

<u>Property, Plant and Equipment</u>	<u>2017</u>	<u>2016</u>
Educational property, plant and equipment	\$ 247,078,908	\$ 234,690,423
Student industry plant and equipment	22,255,952	21,225,119
Rental property	3,319,314	3,319,314
Forest and farms	2,850,449	2,850,449
Collections and works of art	4,437,745	4,437,745
Construction in process	39,699,546	14,835,604
Less accumulated depreciation	(110,447,447)	(102,260,540)
	<u>\$ 209,194,467</u>	<u>\$ 179,098,114</u>

(7) CONDITIONAL ASSET RETIREMENT OBLIGATIONS

Obligations associated with the retirement of long-lived assets are recorded when there is a legal obligation to incur such costs and the fair value of the liability can be reasonably estimated. This amount is accounted for as an additional element of cost and is depreciated over the useful life of the asset. The College's 2017 and 2016 accounting for costs associated with asbestos abatement is as follows:

	<u>2017</u>	<u>2016</u>
Beginning balance	\$ 973,414	\$ 983,584
Accretion expense	24,164	16,786
Liabilities settled during the year	-	(26,956)
Ending balance	<u>\$ 997,578</u>	<u>\$ 973,414</u>

NOTES TO FINANCIAL STATEMENTS

(8) LONG-TERM DEBT

	June 30,	
	2017	2016
Variable Rate Demand Educational Facilities Revenue Bonds, Series 2002A - Issued August 29, 2002; due June 1, 2032; variable interest rate, 0.83% as of June, 2017 with synthetic fixed rate of 3.45%; proceeds used for various capital projects	\$ 10,960,000	\$ 11,555,000
Variable Rate Demand Educational Facilities Revenue Bonds, Series 2003B - Issued December 11, 2003; annual payments through June 1, 2029; variable interest rate, 0.83% as of June, 2017 with synthetic fixed rate of 3.746%; proceeds used for various capital projects	6,120,000	6,515,000
Industrial Building Revenue Refunding Bonds, Series 2010 - Issued December, 2010; private bank placement through JP Morgan Chase Bank, National Association; annual payments through June 1, 2020 at fixed 2.25% rate; proceeds used for refunding Series 1997, 1998 and 2000 bonds	1,205,000	2,210,000
Industrial Building Revenue and Revenue Refunding Bonds, Series 2012 - Issued September, 2012; private bank placement through PNC Bank, National Association; monthly payments at fixed rate of 1.58% through September 21, 2022; proceeds used for construction of new residence hall and refunding of Series 2008 bonds	5,446,516	6,433,728
Educational Facilities Revenue Refunding Bonds, Series 2012 - Issued December, 2012; private bank placement through Fifth Third Bank; annual payments at fixed rate of 1.58% through June 1, 2024; proceeds used for refunding Series 2003A bonds	4,998,830	5,667,918
Educational Facilities Revenue Refunding Bonds, Series 2013 - Issued April, 2013; annual payments through June 1, 2033; at rates from 1.25% to 3.00% with 2.74% average coupon; proceeds used for refunding 2003A bonds	8,735,000	8,795,000
Educational Facilities Revenue Refunding Bonds, Series 2015 - Issued May, 2015; private bank placement through Fifth Third Bank; annual payments at fixed rate of 2.12% through June 1, 2025; proceed used for refunding Series 2005A bonds	5,259,427	5,856,941
	42,724,773	47,033,587
Less current portion	3,577,966	3,713,815
	\$ 39,146,807	\$ 43,319,772

NOTES TO FINANCIAL STATEMENTS

(8) LONG-TERM DEBT (continued)

Principal payments on long-term debt are required to be made in each of the following fiscal years: \$3,577,966 in 2018; \$3,016,804 in 2019; \$3,085,328 in 2020; \$2,942,539 in 2021; \$3,004,254 in 2022 and \$27,097,882 in subsequent years thereafter.

The fair value of the College's long-term debt at June 30, 2017 and 2016 was estimated to be approximately \$42,654,000 and \$47,391,000, respectively, based upon rates available to the College for debt with similar terms and remaining maturities.

Cash payments for interest amounted to \$1,454,732 in 2017 and \$1,503,864 in 2016.

(9) CONTRIBUTIONS RECEIVABLE AND BEQUESTS IN PROBATE

	June 30, 2017 Total	Due In			June 30, 2016 Total
		One Year or Less	One Year to Five Years	Over Five Years	
Unconditional Promises for -					
Unrestricted ¹	\$ 1,203,939	\$ 429,700	\$ 774,239	-	\$ 576,058
Restricted ²	11,898,200	4,225,590	7,672,610	-	5,101,510
Buildings and equipment ³	13,104,494	11,995,277	1,109,217	-	10,998,052
Endowment	9,451	2,100	7,351	-	-
Reserve for unfulfilled promises	(129,315)	(82,083)	(47,232)	-	(144,239)
Total	<u>26,086,769</u>	<u>16,570,584</u>	<u>9,516,185</u>	-	<u>16,531,381</u>
Bequests in Probate	6,743,317	3,287,078	3,456,239	-	8,711,061
External Charitable Remainder Trusts	3,581,092	-	-	3,581,092	3,229,612
Charitable Lead Trusts	<u>484,200</u>	<u>40,350</u>	<u>161,400</u>	<u>282,450</u>	<u>552,478</u>
Total	<u>\$ 36,895,378</u>	<u>\$ 19,898,012</u>	<u>\$ 13,133,824</u>	<u>\$ 3,863,542</u>	<u>\$ 29,024,532</u>
Present Value of Estimated Future Cash Flows	<u>\$ 36,570,237</u>	<u>\$ 19,898,012</u>	<u>\$ 12,813,290</u>	<u>\$ 3,858,935</u>	<u>\$ 28,880,669</u>

¹ June 30, 2017 balance includes \$1,085,000 commitment from an external charitable trust (\$375,000 due in one year or less, \$710,000 due in one year to five years).

² June 30, 2017 balance includes \$11,898,200 commitment from an external charitable trust (\$4,225,590 due in one year or less, \$7,672,610 due in one year to five years).

³ June 30, 2017 balance includes \$10,000,000 commitment from an external charitable trust, due in one year or less.

* Discounted beneficial interest in trusts

NOTES TO FINANCIAL STATEMENTS

(10) COMMITMENTS AND CONTINGENCIES

During the normal course of business, the College is involved in various claims and lawsuits. In the opinion of the College's administration, the potential loss on all claims and lawsuits, net of insurance proceeds, will not be significant to the College's financial position, results of operations, or liquidity.

The College receives grants and contracts from certain federal, state, and local agencies to fund various activities. The costs, both direct and indirect, that have been charged to the grants or contracts are subject to examination and approval by the granting agency. It is the opinion of the College's administration that any disallowance or adjustment of such costs would not have a material effect on the financial statements.

At June 30, 2017, the College was committed under various contracts with alternative investment managers to fund \$115,257,335 of capital calls for these investments. These capital calls will occur over the term of the respective agreements, which is generally no more than a ten-year period. As these capital calls are made, funds will be reallocated from investments in fixed-income securities. These investments are consistent with the strategic asset allocation guidelines for long-term investments as established by the College's Board of Trustees. The capital calls are summarized by the type of investment below:

Buy out	\$ 5,605,326
Fund of funds	84,873,823
Special opportunities	<u>24,778,186</u>
Total	<u>\$ 115,257,335</u>

The College has purchase commitments relating to construction projects of approximately \$39,630,000 as of June 30, 2017.

(11) CONCENTRATIONS

The College's operations are heavily dependent upon the spendable return from endowment investments. Therefore, an extended downturn in financial markets could have an adverse effect on the College's programs and activities.

Many of the College's students receive support from state and federal student financial assistance programs. A significant reduction in the level of this support, if it were to occur, might have an adverse effect on the College's programs and activities.

NOTES TO FINANCIAL STATEMENTS

(12) NET ASSETS RELEASED FROM RESTRICTIONS

Donor-imposed restrictions expired on temporarily restricted net assets during the years ended June 30, as follows:

	2017	2016
Purpose Restricted Contributions for -		
Instruction	\$ 1,783,621	\$ 1,768,206
Public service	2,229,668	1,651,758
Academic support	2,289,815	1,617,764
Student services	1,505,706	1,126,997
Residence halls	497,045	319,387
Student aid	2,734,621	2,802,699
Support services	2,397,323	1,262,907
Student industries	881	-
Plant operations	376,972	203,366
	\$ 13,815,652	\$ 10,753,084
Time-Restricted Contributions - Amortization of Restricted Gifts to Acquire Long-Lived Assets	2,770,797	2,327,104
Total Net Assets Released from Restriction	\$ 16,586,449	\$ 13,080,188
Matured Annuity and Life Income Contracts -		
Temporarily Restricted Agreements Reclassified to Tuition Replacement Funds in Unrestricted Net Assets	\$ 336,320	\$ 108,927

(13) TAX STATUS

Berea College has a determination from the IRS that it is a not-for-profit organization exempt from Federal income tax under Section 501(c)(3) of the Internal Revenue Code. However, the College is subject to federal income tax on any unrelated business income. No provision for income tax has been made in the accompanying financial statements.

GAAP requires the College to evaluate tax positions taken by the College and recognize a tax liability (or asset) if the College has taken an uncertain position that more likely than not would be sustained upon examination by the IRS. The College has analyzed the tax positions taken by the College and has concluded that there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements. The College would recognize interest and penalties related to uncertain tax positions in interest and income tax expense, respectively. The College does not have an amount accrued for interest or penalties as of June 30, 2017 or 2016. The College is subject to routine audits by taxing jurisdictions; however there are currently no audits for any tax periods in progress. The College believes it is no longer subject to income tax examinations for years prior to 2014.

(14) SUBSEQUENT EVENTS

We evaluate events and transactions that occur after the statement of financial position date as potential subsequent events. We performed this evaluation through September 8, 2017, the date on which we issued our financial statements. There were no events occurring during the evaluation period that would require recognition or disclosure in the financial statements.

BEREA
COLLEGE