

# **Horatio Alger Association of Distinguished Americans, Inc. and Affiliate**

Consolidated Financial Report  
December 31, 2017

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## Independent Auditor's Report

To the Board of Directors  
Horatio Alger Association of Distinguished Americans, Inc.

### Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Horatio Alger Association of Distinguished Americans, Inc. and Affiliate (the Association), which comprise the consolidated statement of financial position as of December 31, 2017, the related consolidated statements of activities and cash flows for the year then ended, and the related notes to the consolidated financial statements (collectively, 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Horatio Alger Association of Distinguished Americans, Inc. and Affiliate as of December 31, 2017, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**Report on Summarized Comparative Information**

We have previously audited the Association's 2016 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated August 9, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2016, is consistent in all material respects, with the audited financial statements from which it has been derived.

*RSM US LLP*

McLean, Virginia  
August 29, 2018

Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

**Consolidated Statement of Financial Position**  
**December 31, 2017**  
**(With Comparative Totals for 2016)**

	2017	2016
<b>Assets</b>		
Cash and cash equivalents	\$ 36,404,069	\$ 48,293,171
Prepaid expenses and other assets	1,711,075	1,186,649
Contributions receivable, net	23,766,000	27,236,967
Investments	215,555,650	147,213,259
Investments in deferred compensation assets	515	2,089,029
Furniture, equipment and leasehold improvements, net	52,020	28,194
Beneficial interest in perpetual trust	1,838,732	1,674,387
	<u>\$ 279,328,061</u>	<u>\$ 227,721,656</u>
<b>Liabilities and Net Assets</b>		
Liabilities:		
Accounts payable and accrued expenses	\$ 495,514	\$ 462,163
Scholarships payable, net	25,664,192	22,857,647
Deferred compensation plan obligations	515	2,089,029
Deferred rent	92,826	82,739
<b>Total liabilities</b>	<u>26,253,047</u>	<u>25,491,578</u>
Commitments (Notes 9 and 11)		
Net assets:		
Unrestricted:		
Unrestricted – undesignated	11,812,763	18,341,291
Board-designated endowment assets	210,100,550	148,812,482
	<u>221,913,313</u>	<u>167,153,773</u>
Temporarily restricted	26,215,146	30,294,095
Permanently restricted	4,946,555	4,782,210
	<u>253,075,014</u>	<u>202,230,078</u>
	<u>\$ 279,328,061</u>	<u>\$ 227,721,656</u>

See notes to consolidated financial statements.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Consolidated Statement of Activities Year Ended December 31, 2017 (With Comparative Totals for 2016)

	2017				2016 Total
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	
Support and revenue:					
Contributions:					
Horatio Alger Membership Programs and Induction Ceremonies	\$ 8,910,865	\$ 3,790,620	\$ -	\$ 12,701,485	\$ 11,845,253
Scholarships and other	726,887	6,455,925	-	7,182,812	10,797,597
Capital campaign	-	29,296,100	-	29,296,100	7,391,227
Giving clubs	-	2,111,598	-	2,111,598	1,769,252
Release of scholarship liability	1,368,099	-	-	1,368,099	-
Video and book sales	117,072	-	-	117,072	31,540
Net assets released from restrictions:					
Satisfaction of program restrictions:					
Scholarships and other	6,445,033	(6,445,033)	-	-	-
Induction ceremony	3,330,382	(3,330,382)	-	-	-
Capital campaign	26,836,427	(26,836,427)	-	-	-
Satisfaction of time restrictions:					
Capital campaign	7,643,377	(7,643,377)	-	-	-
Giving clubs	1,477,973	(1,477,973)	-	-	-
<b>Total support and revenue</b>	<b>56,856,115</b>	<b>(4,078,949)</b>	<b>-</b>	<b>52,777,166</b>	<b>31,834,869</b>
Expenses:					
Program services:					
State Scholarship Program	9,300,369	-	-	9,300,369	6,833,336
Horatio Alger Membership programs and induction ceremonies	6,169,116	-	-	6,169,116	5,157,599
National Scholars' Program	2,508,024	-	-	2,508,024	2,479,707
American Spirit Bridge	2,420,000	-	-	2,420,000	-
Other scholarship programs	6,799,450	-	-	6,799,450	7,491,377
Membership meeting	1,295,671	-	-	1,295,671	1,306,199
National Scholars' Conference	572,865	-	-	572,865	509,555
Educational materials	359,301	-	-	359,301	469,606
Scholars' alumni programs	151,489	-	-	151,489	113,225
State of Our Nation's Youth	75,574	-	-	75,574	363,743
Field directors meeting	71,101	-	-	71,101	323,926
Collegiate Partners Program	94,144	-	-	94,144	85,462
<b>Total program services</b>	<b>29,817,104</b>	<b>-</b>	<b>-</b>	<b>29,817,104</b>	<b>25,133,735</b>
Supporting services:					
Administration and general	1,041,757	-	-	1,041,757	1,047,788
Fundraising	604,494	-	-	604,494	695,509
Uncollectable pledges	552,887	-	-	552,887	-
<b>Total supporting services</b>	<b>2,199,138</b>	<b>-</b>	<b>-</b>	<b>2,199,138</b>	<b>1,743,297</b>
<b>Total expenses</b>	<b>32,016,242</b>	<b>-</b>	<b>-</b>	<b>32,016,242</b>	<b>26,877,032</b>
<b>Change in net assets before other changes</b>	<b>24,839,873</b>	<b>(4,078,949)</b>	<b>-</b>	<b>20,760,924</b>	<b>4,957,837</b>
Investment income, net	29,919,667	-	-	29,919,667	15,558,109
Change in value of beneficial interest in perpetual trust	-	-	164,345	164,345	40,255
<b>Change in net assets</b>	<b>54,759,540</b>	<b>(4,078,949)</b>	<b>164,345</b>	<b>50,844,936</b>	<b>20,556,201</b>
Net assets:					
Beginning	167,153,773	30,294,095	4,782,210	202,230,078	181,673,877
Ending	<b>\$ 221,913,313</b>	<b>\$ 26,215,146</b>	<b>\$ 4,946,555</b>	<b>\$ 253,075,014</b>	<b>\$ 202,230,078</b>

See notes to consolidated financial statements.

Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

**Consolidated Statement of Cash Flows**  
**Year Ended December 31, 2017**  
**(With Comparative Totals for 2016)**

	2017	2016
Cash flows from operating activities:		
Change in net assets	\$ 50,844,936	\$ 20,556,201
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Unrealized and realized gain on investments, net	(27,199,451)	(12,160,737)
Bad debt expense for contributions receivable	552,887	-
Decrease in discount on contributions receivable	(301,928)	(301,069)
Depreciation and amortization	15,769	26,225
Forfeitures on scholarships payable	(3,010,831)	(874,660)
Increase in allowance for scholarship forfeitures	(220,835)	(261,220)
Increase in discount on scholarships payable	(41,861)	(142,683)
Change in beneficial interest in perpetual trust	(164,345)	(40,255)
Change in deferred rent	10,087	7,719
Contributions restricted for long-term investment	(500,000)	(500,000)
Changes in assets and liabilities:		
(Increase) decrease in:		
Prepaid expenses and other assets	(524,426)	268,108
Contributions receivable	3,220,008	1,870,110
Increase in:		
Accounts payable and accrued expenses	33,351	172,584
Scholarships payable	6,080,072	6,049,389
Deferred compensation plan obligations	2,088,514	499,898
<b>Net cash provided by operating activities</b>	<b>30,881,947</b>	<b>15,169,610</b>
Cash flows from investing activities:		
Purchases of investments	(239,527,199)	(116,020,720)
Purchases of deferred compensation assets	-	(499,898)
Proceeds from sale of deferred compensation assets	(2,088,514)	-
Proceeds from sales and maturities of investments	198,384,259	128,828,176
Purchases of furniture, equipment and leasehold improvements	(39,595)	(10,438)
<b>Net cash (used in) provided by investing activities</b>	<b>(43,271,049)</b>	<b>12,297,120</b>
Cash flows from financing activities:		
Contributions restricted for long-term investment	500,000	500,000
<b>Net cash provided by financing activities</b>	<b>500,000</b>	<b>500,000</b>
<b>Net (decrease) increase in cash and cash equivalents</b>	<b>(11,889,102)</b>	<b>27,966,730</b>
Cash and cash equivalents:		
Beginning	48,293,171	20,326,441
Ending	<b>\$ 36,404,069</b>	<b>\$ 48,293,171</b>

See notes to consolidated financial statements.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### Note 1. Nature of Activities and Significant Accounting Policies

**Nature of activities:** Horatio Alger Association of Distinguished Americans, Inc. and Affiliate (the Association) consists of two entities: Horatio Alger Association of Distinguished Americans, Inc. (Horatio) and Horatio Alger Endowment Fund (the Fund).

Horatio is a nonprofit organization established to promote and advance the American tradition of success through scholarships for young Americans, educational programs, research, publications and events.

The Fund holds and manages the endowment funds previously held by Horatio and takes actions, as appropriate, to grow the funds of the endowment to support the educational and scholarship programs of Horatio.

The Association operates the following programs:

**State Scholarship Program:** Scholarships are awarded to provide financial assistance to students in particular states who have exhibited integrity and perseverance in overcoming personal adversity and who aspire to pursue higher education. The programs annually award scholarships ranging from \$2,500 to \$10,500 to deserving students, as well as provide educational and financial counseling towards obtaining a college degree.

**Horatio Alger Membership programs and induction ceremonies:** The Horatio Alger Award (the Award) is recognized as one of the nation's most prestigious honors. The Award is presented during the annual Membership program and induction ceremonies held in Washington, D.C. each year during a multi-day program for Members, Life Partners and Friends of Distinction, held in conjunction with the National Scholars' Conference. The programs focus on Member achievements, interviews with new Members, opportunities for Member networking, mentoring of the National Scholars and educational programs regarding the future of the American Dream.

**American Spirit Bridge Program:** In 2017, the Association underwrote construction of the American Spirit Bridge at the National World War II Museum in New Orleans. Funded by individual member contributions, this sponsorship honors members who have served in the armed forces and loved ones who fought in World War II.

**National Scholars' Program:** This program allows more than 100 students each year from high schools across the United States and Puerto Rico to receive Horatio Alger National Scholarships. These students, known as National Scholars, receive a \$25,000 scholarship to apply to a college of their choice. The Association's Horatio Alger National Scholarship award of \$25,000 is available to scholars for a four-year period, during which the scholars may request a maximum of \$6,250 per year. Awards may be used only for tuition, fees, room, board, books and supplies. Horatio Alger National Scholarships are awarded on the basis of a student's overcoming adversity, critical financial need, personal potential and academic achievement, school and community, work history, character and promise of future contributions to society.

**Other scholarship programs:** These programs include the internship and placement program, the cost of scholar services such as financial advising, the Alumni Advisory Council, the Scholarship Selection Committee and the members' forum meetings. The Association also offers grants to scholars pursuing graduate studies through the Dennis R. Washington Achievement Scholarships program.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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

**Membership meeting:** The Association convenes the Lifetime Members and Life Partners to advance the mission, programs and services of the Association on a regular basis including, but not limited to, the Annual Board of Directors Meeting, Annual Awards Week in Washington and at specialized forums, such as the International Forum, alumni summits and regional convenings, such as the Association's concert series. These activities include ongoing communications with members, such as Forum; the biennial report, *Only in America*; and other online and printed materials that keep the members connected to the Association's mission and work.

**National Scholars' Conference:** This program allows recipients of the Horatio Alger National Scholarship to attend the annual four-day conference in Washington, D.C. The conference provides National Scholars the opportunity to meet with Association members to gain a better understanding of the American free enterprise system. They also meet with congressional leaders to gain deeper insight into the operation of the federal government. The goal of the conference is to awaken the scholars to the possibilities that are available to them as American citizens and to encourage their participation and interest in building a strong future for our nation.

**Educational materials:** This program provides information about the Association's mission and programs through a variety of sources. Publications are printed for members, National Scholars, education partners, friends and the general public. The educational documents reinforce the message of Horatio Alger's original characters that success as an adult is within the reach of every young person with a dream and a commitment to hard work and integrity.

**Scholars' alumni programs:** As the scholarship programs have grown, the number of students considered alumni of the program, both those in undergraduate school and those who have graduated, has grown rapidly. The alumni programs include the Association's ongoing work with scholars as they pursue their undergraduate degrees; the alumnus of the year program that recognizes outstanding alumni each year; the semiannual newsletter, *Strive and Succeed*; an online message board for scholars to communicate; and the Scholars Alumni Summit meeting.

**State of Our Nation's Youth:** Conducted every four years in collaboration with Peter Hart and Associates and New York University, this longstanding program and publication surveys the attitudes of 14- through 23-year old American youth regarding education, politics and the issues shaping their lives. The report is released at a national press conference and distributed to media, education leaders and Association Members.

**Field directors' meeting:** The Association has volunteer field directors throughout the United States who serve as ambassadors to private, parochial and public schools in promoting the scholarships, programs and services of the Association. Most field directors are secondary or higher education professionals and some are alumni of the Association's scholarship programs. Field directors convene for training on occasion and communicate regularly with the headquarters staff.

**Collegiate Partners Program:** This program is a unique program under which private and public colleges and universities unite with the Association to form a consortium for the purpose of providing special financial assistance to National and State Scholars to reduce their educational costs. Collegiate partner institutions usually match the amount the scholar brings to the school and then offer aid through campus scholarships, grants and work-study programs. This program has grown rapidly to include over 280 institutions of higher learning.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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

**Career/technical scholarships:** This program provides scholarships to attend community colleges for training and certification in a range of career and technical fields leading to associate degrees or certification for students to enter careers. Students in these programs will also be given an opportunity to further advance their education in the future through scholarship assistance. Expenses for this program are included in other scholarship programs in the consolidated statement of activities.

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

**Basis of accounting:** The accompanying consolidated financial statements are presented in accordance with 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:** The consolidated financial statement presentation follows the recommendations of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (the Codification). As required by the Not-for-Profit topics of the Codification, Balance Sheet and Income Statement, the Association is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets and permanently restricted net assets.

Net assets, support and revenue, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Association are classified and reported as follows:

**Unrestricted:** Net assets that are not subject to donor-imposed stipulations.

**Temporarily restricted:** Net assets subject to donor-imposed stipulations that will be met either by actions of the Association and/or the passage of time.

**Permanently restricted:** Net assets subject to donor-imposed stipulations that neither expire by the passage of time nor can be fulfilled or otherwise removed by the actions of the Association. Generally, the donors of these assets permit the Association to use all or part of the income earned on related investments for general or specific purposes.

Unconditional contributions are reported as increases in the appropriate category of net assets when received. Unconditional contributions with donor-imposed restrictions related to awards activities that are met in the same fiscal year they are received are included in unrestricted support. Unconditional contributions for other programs with donor-imposed restrictions that are met in the same fiscal year they are received are included in temporarily restricted net assets. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments are reported as increases or decreases in unrestricted net assets, unless their use is restricted by explicit donor stipulations or by law. Expirations of temporary restrictions recognized on net assets are reported as reclassifications from temporarily restricted net assets to unrestricted net assets.

**Principles of consolidation:** The accompanying consolidated financial statements include the accounts of Horatio and the Fund. All significant intercompany accounts and transactions have been eliminated in consolidation.

**Measure of operations:** The Association considers operations to include all changes in net assets, exclusive of investment income and changes in value of its beneficial interest in perpetual trust.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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

**Cash and cash equivalents:** The Association considers all highly liquid investments purchased with an initial maturity of three months or less to be cash equivalents.

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

The Association invests in a professionally managed portfolio that contains various securities that are exposed to risks, such as interest, 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 risks in the near term could materially affect investment balances and the amounts reported in the consolidated financial statements. The money market funds and cash held within the portfolio are presented with cash and cash equivalents.

**Contributions:** Unconditional contributions, which include unconditional promises to give, are recognized as support in the period received net of allowance for estimated uncollectible amounts and net of discount to present value for pledges expected to be received in future periods greater than one year. Unconditional contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. Amortization of the discount is recorded as support and is used in accordance with donor-imposed restrictions, if any, on the contributions. Contributions of assets other than cash are recorded at their estimated fair value at the date of gift. Management determines the allowance for doubtful contributions receivable based on historical experience regarding collections. Contributions are written off when deemed uncollectible.

**Investments:** Investments in corporate fixed income, partnership and hedge funds, equity mutual funds, common stock, and money market funds are reported at fair value. Fair value is determined by using quoted market prices on marketable securities. The partnerships and hedge funds are reported at estimated fair values based on a practical expedient, the net asset value per share or equivalent, provided by the investment managers. The Association believes the carrying amount of these financial instruments is a reasonable estimate of fair value. Because these investments are not readily marketable, their estimated value is subject to additional uncertainty and, therefore, values realized upon disposition may vary significantly from currently reported values.

Investment income, recorded in the consolidated statement of activities, consists of unrealized and realized gains and losses and interest and dividends.

**Furniture, equipment and leasehold improvements:** Furniture, equipment and leasehold improvements are stated at cost, less accumulated depreciation and amortization. Depreciation and amortization are computed on a straight-line basis over the shorter of the estimated useful lives or lease terms of the assets, which range from two to ten years. The Association capitalizes all property and equipment purchased with a cost of \$1,000 or more.

**Beneficial interest in perpetual trust:** The Association recorded its beneficial interest in a perpetual trust as a permanently restricted contribution in the period in which it was notified of the irrevocable nature of the trust. The Association determines the fair value of its trust interest based on the fair value of the underlying assets within the trust. Changes in the value of the Association's interest are recorded in each subsequent period in the permanently restricted change in net assets. Support received on this trust, which is paid annually, is classified as unrestricted support in the accompanying consolidated statement of activities. For the year ended December 31, 2017, the gain incurred on this trust was \$164,345.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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

**Valuation of long-lived assets:** Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of long-lived assets is measured by a 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 reportable at the lower of the carrying amount or fair value, less cost to sell.

**Scholarships:** The Association records an expense and payable when a scholarship is awarded to a student and the likelihood of payment of the scholarship is considered probable. The Association records an estimate for forfeitures at the time the scholarship is awarded. Scholarships expected to be paid in future periods greater than one year are discounted to present value based on expected future cash flows at an appropriate discount rate commensurate with the risks involved.

**Income tax:** Horatio and the Fund have been recognized as exempt from federal income taxes by the Internal Revenue Service under Section 501(c)(3) of the Internal Revenue Code and each has been classified as an organization that is not-a-private foundation.

Management evaluated the tax positions and concluded that Horatio and the Fund have taken no uncertain tax positions that require adjustment to the consolidated financial statements to comply with the provisions of this guidance.

**Functional allocation of expenses:** The costs of providing the Association's programs and activities have been summarized on a functional basis in the consolidated statement of activities. Expenses that can be identified with a specific program or supporting service are allocated directly. Certain other costs have been allocated among the programs and supporting services benefited.

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

**Pending accounting pronouncements:** In August 2016, the FASB issued 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 will be effective for the fiscal year ending December 31, 2018.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. A lessee is required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months. Leases with a term of 12 months or less will be accounted for similar to existing guidance for operating leases today. The ASU is expected to impact the Association's consolidated financial statements as the Association has certain operating lease arrangements for which it is the lessee. The standard is effective on January 1, 2020, with early adoption permitted.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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

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*, which provides additional guidance on characterizing grants and similar contracts with resource providers as either exchange transactions or contributions, as well as distinguishing between conditional contributions and unconditional contributions. The updated standard will be effective for resource recipients for annual reporting periods beginning after December 15, 2018 and resource providers one year later. Management is currently evaluating the effect on the consolidated financial statements.

**Prior year information:** The consolidated financial statements include certain prior year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP). Accordingly, such information should be read in conjunction with the Association's consolidated financial statements for the year ended December 31, 2016, from which the summarized information was derived.

**Subsequent events:** The Association evaluated subsequent events through August 29, 2018, which is the date the consolidated financial statements were available to be issued.

#### Note 2. Contributions Receivable

Contributions receivable represent the uncollected balance of unconditional promises to give. The majority of the Association's contributions are made by Board members, former Board members, and members and represent giving club contributions, awards activities and scholarship funds/capital campaign contributions. The balance of contributions receivable, net of discount and allowance for uncollectible contributions, consists of the following at December 31, 2017:

	Giving Clubs	Awards Activities	Scholarships/ Capital Campaign	Total
Amounts due in:				
Less than one year	\$ 1,095,000	\$ 3,068,500	\$ 3,095,751	\$ 7,259,251
One to five years	2,250,000	-	15,219,551	17,469,551
Greater than five years	-	-	454,000	454,000
Gross contributions receivable	3,345,000	3,068,500	18,769,302	25,182,802
Less unamortized discount on contributions receivable (4%)	(166,375)	-	(745,111)	(911,486)
Less allowance for uncollectible contributions	(66,900)	(61,380)	(377,036)	(505,316)
Contributions receivable, net	\$ 3,111,725	\$ 3,007,120	\$ 17,647,155	\$ 23,766,000

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### **Note 3. Fair Value Measurements**

The Association follows the Codification topic, Fair Value Measurement. The topic applies to all assets and liabilities that are being measured and reported on a fair value basis. The topic establishes a framework for measuring fair value in accordance with U.S. GAAP, and expands disclosure about fair value measurements. The topic enables the reader of the consolidated financial statements to assess the inputs used to develop those measurements by establishing a hierarchy for ranking the quality and reliability of the information used to determine fair values. The topic requires that assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

**Level 1:** Quoted market prices in active markets for identical assets or liabilities

**Level 2:** Observable market-based inputs or unobservable inputs corroborated by market data

**Level 3:** Unobservable inputs not corroborated by market data

In determining the appropriate levels, the Association performs a detailed analysis of the assets and liabilities that are subject to the topic. At each reporting period, all assets and liabilities for which the fair value measurement is based on significant unobservable inputs are classified as Level 3.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

#### Note 3. Fair Value Measurements (Continued)

The table below presents the balances of assets measured at fair value on a recurring basis by level within the hierarchy:

	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Equity mutual funds:				
Large blend	\$ 30,186,370	\$ -	\$ -	\$ 30,186,370
Total equity mutual funds	30,186,370	-	-	30,186,370
Corporate fixed income:				
Consumer	-	19,574,996	-	19,574,996
Industrial	-	17,536,909	-	17,536,909
Services	-	16,748,088	-	16,748,088
Technology	-	13,287,293	-	13,287,293
Healthcare	-	5,183,187	-	5,183,187
Financial	-	4,424,394	-	4,424,394
Basic materials	-	3,053,637	-	3,053,637
Real estate	-	2,093,756	-	2,093,756
Total corporate fixed income	-	81,902,260	-	81,902,260
Common stock:				
Financial	10,881,042	-	-	10,881,042
Consumer goods	5,144,850	-	-	5,144,850
Healthcare	4,031,779	-	-	4,031,779
Technology	3,223,819	-	-	3,223,819
Industrial	3,203,427	-	-	3,203,427
Energy	3,010,855	-	-	3,010,855
Basic materials	1,424,365	-	-	1,424,365
Real estate	1,299,598	-	-	1,299,598
Utilities	1,033,276	-	-	1,033,276
Services	630,288	-	-	630,288
Total common stock	33,883,299	-	-	33,883,299
Alternative investments valued using a net asset value per share or equivalent as a practical expedient (a)				
	-	-	-	69,583,721
Total investments at fair value	64,069,669	81,902,260	-	215,555,650
Money market funds in cash and cash equivalents	5,368,024	-	-	5,368,024
Beneficial interest in perpetual trust	-	-	1,838,732	1,838,732
Total assets at fair value	\$ 69,437,693	\$ 81,902,260	\$ 1,838,732	\$ 222,762,406

(a) In accordance with the Association's previous adoption of ASU No. 2015-07, certain investments that were measured at a net asset value per share (or its equivalent) have not been classified in the fair value hierarchy. The fair value amounts of those investments presented in this table are intended to permit reconciliation of the fair value hierarchy to the line item presented in the consolidated statement of financial position.

The equity mutual funds, common stock and money market funds are classified as Level 1 instruments, as they are actively traded on public exchanges with identical assets.

The corporate fixed income securities are classified as Level 2 instruments, as there are not quoted market prices in active markets for identical assets. Their value is determined using models and other valuation methodologies, which are corroborated by market data.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### Note 3. Fair Value Measurements (Continued)

The beneficial interest in perpetual trust is classified as a Level 3 instrument, as there is no market for the Association's interest in the trust. Further, the Association's asset is the right to receive cash flows from the trust, not the assets of the trust themselves. Although the trust assets may be investments for which quoted prices in an active market are available, the Association does not control those investments.

For assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3), the Codification requires reconciliation of the beginning and ending balances separately for each major category of assets and liabilities, except for derivative assets and liabilities, which may be presented net. The table below represents the reconciliation of the Association's assets measured at fair value on a recurring basis using significant unobservable inputs:

	<u>Beneficial Interest in Perpetual Trust</u>
Beginning balance of assets, January 1, 2017	\$ 1,674,387
Change in value of beneficial interest in perpetual trust	164,345
Ending balance of assets, December 31, 2017	<u>\$ 1,838,732</u>

For fair value measurements categorized within Level 3 of the fair value hierarchy, the Association is required to provide quantitative information about significant unobservable inputs used in the fair value measurement. The following table provides the required information for the Association:

Type	Fair Value at December 31, 2017	Valuation Technique	Unobservable Inputs	Range
Beneficial interest in trust	\$ 1,838,732	Percentage of assets held by custodian	Market activity	5%

Investment income, net, for the year ended December 31, 2017, consists of the following:

Interest and dividends	\$ 3,347,222
Unrealized and realized gain, net	27,199,451
Investment fees	(627,006)
	<u>\$ 29,919,667</u>

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### Note 3. Fair Value Measurements (Continued)

The following presents further information regarding the composition of the partnerships and hedge funds at December 31, 2017:

Strategy Category	Fair Value	Redemption Frequency	Redemption Notice Period
International (a)	\$ 30,827,658	See note (a) below	See note (a) below
Emerging markets (b)	25,258,420	See note (b) below	See note (b) below
Global equity – long-term growth (c)	7,241,364	See note (c) below	See note (c) below
Global equity – small/micro cap (d)	3,448,652	See note (d) below	See note (d) below
International long-term growth – mid/small cap (e)	2,644,465	See note (e) below	See note (e) below
Distressed (f)	90,502	See note (f) below	See note (f) below
Multi-strategy (g)	72,660	See note (g) below	See note (g) below
	<u>\$ 69,583,721</u>		

**International:** (a) This category includes a diversified portfolio of international equities to afford participants an opportunity to obtain long-term capital gains and income from a diversified portfolio of equity securities generally located in any country other than the United States. 100% of the investments in this category are liquid as the capital contributed to the fund is redeemable on the last business day of the month. The participant must notify the investment manager at least ten business days before the withdrawal date.

**Emerging markets:** (b) This category includes a diversified portfolio of foreign commingled funds for the purpose of trading and investing in securities. This category employs a long-term strategy for all of its investments. 100% of the investments in this category are liquid as the capital contributed to the fund is redeemable on a monthly basis. Withdrawals can be made from the fund on the last day of each month. The participant must notify the investment manager in writing at least 30 days before the prior month-end to make a withdrawal request.

**Global equity – long-term growth:** (c) This category includes a diversified portfolio of global equity investments with the primary goal of achieving long-term growth. 100% of the investments in this category are liquid as the capital contributed to the fund is redeemable on a monthly basis. Participants must notify the investment manager at least six business days before the month-end to make a withdrawal request. Withdrawal legal documents must be returned to the investment manager and the custodial trustee at least four business days before the month-end.

**Global equity – small/micro cap:** (d) This category includes a diversified portfolio of global equities with a strong bias towards small and micro cap companies. Investments include companies based in the U.S., developed foreign countries and emerging/frontier markets. 100% of the investments in this category are liquid as the capital contributed to the fund is redeemable on a monthly basis. Participants must notify the investment manager at least 30 business days before the month-end to make a withdrawal request.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### Note 3. Fair Value Measurements (Continued)

**International long-term growth – mid/small cap:** (e) This category includes a diversified portfolio of international equities to afford participants an opportunity to obtain long-term capital gains and income from a diversified portfolio of mid and small capitalization equity securities generally located in any country other than the United States and Canada. 100% of the investments in this category are liquid as the capital contributed to the fund is redeemable on a monthly basis. The participant must notify the investment manager at least ten business days before the prior month-end to make a withdrawal request. Withdrawal legal documents must be returned to the investment manager and the custodial trustee at least four business days before the month-end.

**Distressed:** (f) This category includes investments made into distressed or stressed companies. The manager can invest in any instrument across a company's capital structure, including equity, debt, bank loans, dips (debtor in possession), convertible bonds and more. The companies can be in various stages of stress or distress, including bankruptcy and post-bankruptcy reorganization. 100% of the investments in this category are considered illiquid, as the capital contributed to the partnership is not redeemable for a period of ten years from the initial closing date of the fund, which was in March 2007. The Association expects to redeem the remaining funds during the year ending December 31, 2018.

**Multi-strategy:** (g) This category includes a combination of strategies. Managers have the flexibility to invest across all asset classes and to change their allocations to various strategies and instruments as they see fit. Instruments include equities, options, futures, bonds, loans, derivatives and others. In addition, the fund may pursue the value-oriented strategy through short-selling and investments in private or less liquid instruments. This fund is currently in liquidation.

The Association has no unfunded commitments to the funds described above.

#### Note 4. Furniture, Equipment and Leasehold Improvements

At December 31, 2017, furniture, equipment and leasehold improvements consist of the following:

Furniture and equipment	\$ 488,971
Leasehold improvements	338,180
	<u>827,151</u>
Less accumulated depreciation and amortization	775,131
	<u><u>\$ 52,020</u></u>

Depreciation and amortization expense for the year ended December 31, 2017, was \$15,769.

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### Note 5. Scholarships

During the year ended December 31, 2017, the Association awarded \$16,639,589 of scholarships, with forfeitures of \$3,010,831. The scholarships are recorded as State Scholarship Program, National Scholars' Program and other scholarship programs expenses in the accompanying consolidated statement of activities. At December 31, 2017, \$25,664,192 of scholarships, net of the allowance and discount of \$1,661,907 and \$549,021, respectively, remained to be disbursed. The expected future payments on the awarded scholarships at December 31, 2017, are as follows:

Years ending December 31:	
2018	\$ 16,718,704
2019	7,913,574
2020	3,242,842
	<u>\$ 27,875,120</u>

#### Note 6. Employee Benefit Plans

The Association has a tax deferred annuity plan available to all full-time employees. Participating employees may defer up to 50% of their gross salary, and after one year of employee service, the Association will match the amount of deferral up to 10%. The amount of the expense incurred under this plan was \$88,254 for the year ended December 31, 2017.

The Association maintains a deferred compensation plan. Assets and obligations under this plan at December 31, 2017, were \$515. For the year ended December 31, 2017, the Association paid out \$2,088,928 under this plan.

The Association also has a deferred compensation plan in accordance with the provisions of Section 457(f) of the Internal Revenue Code. Elective deferrals can be made by the employee up to the maximum amount permitted by law.

#### Note 7. Temporarily Restricted Net Assets

Changes in temporarily restricted net assets during the year ended December 31, 2017, are as follows:

	December 31, 2016	Additions	Releases	December 31, 2017
Purpose and time restricted:				
Scholarships and other	\$ 8,346,727	\$ 6,455,925	\$ (6,445,033)	\$ 8,357,619
Horatio Alger Membership Programs and Induction Ceremonies	3,330,382	3,790,620	(3,330,382)	3,790,620
Capital campaign	-	26,836,427	(26,836,427)	-
Time restricted:				
Capital campaign	15,551,436	2,459,673	(7,643,377)	10,367,732
Giving clubs	3,065,550	2,111,598	(1,477,973)	3,699,175
	<u>\$ 30,294,095</u>	<u>\$ 41,654,243</u>	<u>\$ (45,733,192)</u>	<u>\$ 26,215,146</u>

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### Note 8. Board-Designated Endowment and Permanently Restricted Net Assets

The Association follows the Codification Subtopic, Reporting Endowment Funds. The Codification addresses accounting issues related to guidelines in the Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA).

The Association has adopted investment and spending policies for permanently restricted cash contributions that attempt to provide a predictable stream of funding to programs while maintaining purchasing power. Permanently restricted net assets consist of three endowments held by the Association and a perpetual trust held by a third party. The balance as of December 31, 2017, was \$4,946,555. Annual investment income earned on the endowments held by the Association is to be used to fund educational programs and scholarships in current and future years.

Distributions of income earned on the perpetual trust are to be used by the Association to fund scholarships or promote other Association goals.

The Association may utilize up to 5% and additional amounts as determined by the Board of Directors of the endowment fund cash and investment balance to underwrite educational programs and scholarship expenses. The previous end-of-year endowment fund balance shall be the basis for determining the allowable withdrawal, and this process shall be incorporated into the Association's annual budget presentation to the Board of Directors. If any of the funds are not needed by the end of the fiscal year, they will remain in the endowment.

The Association considers all capital campaign contributions to be part of the Association's board-designated endowment. Capital campaign contributions received by the Association not fully collected when received are temporarily restricted due to time and are included in the temporarily restricted portion of the donor-restricted endowment. When the Association collects the cash related to these contributions, and therefore satisfies the time restriction, the funds are released from the temporary restriction. At that time, the funds are included in the board-designated endowment. Capital campaign contributions collected in full when received are temporarily restricted for purpose. These contributions are included in the temporary restricted portion of the donor-restricted endowment and are released into the board designated endowment. Temporarily restricted capital campaign contributions received during the year ended December 31, 2017, were \$29,496,100.

Transfers from temporarily restricted net assets relating to capital campaign contributions during the year ended December 31, 2017, were comprised of cash collections and write-offs totaling \$34,479,804.

The Association's endowment funds consist of the following at December 31, 2017:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ 10,367,732	\$ 4,946,555	\$ 15,314,287
Board-designated endowment funds	210,100,550	-	-	210,100,550
	<u>\$ 210,100,550</u>	<u>\$ 10,367,732</u>	<u>\$ 4,946,555</u>	<u>\$ 225,414,837</u>

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### Note 8. Board-Designated Endowment and Permanently Restricted Net Assets (Continued)

For the year ended December 31, 2017, the Association had the following endowment-related activities:

	Board- Designated Endowment	Temporarily Restricted	Permanently Restricted	Total
Net assets, December 31, 2016	\$ 148,812,482	\$ 15,551,436	\$ 4,782,210	\$ 169,146,128
Contributions	-	29,296,100	-	29,296,100
Current year designations	10,000	-	-	10,000
Transfers from temporarily restricted net assets	34,479,804	(34,479,804)	-	-
Net investment income	29,359,788	-	-	29,359,788
Change in value of beneficial interest in perpetual trust	-	-	164,345	164,345
Appropriation of endowment assets for expenditure	(2,561,524)	-	-	(2,561,524)
Net assets, December 31, 2017	<u>\$ 210,100,550</u>	<u>\$ 10,367,732</u>	<u>\$ 4,946,555</u>	<u>\$ 225,414,837</u>

The board-designated and permanently restricted endowment assets are primarily comprised of the Association's investments, as detailed in Note 3. The remaining board-designated endowment assets are comprised of money market funds, which are included in cash and cash equivalents in the accompanying consolidated statement of financial position. The ending balance of temporarily restricted endowment assets are comprised of outstanding capital campaign contributions at December 31, 2017.

#### Note 9. Leases

The Association has a lease for office and parking spaces that runs through April 2026. The lease is subject to annual escalations of 3%. Rent expense for the year ended December 31, 2017, was approximately \$240,000.

Future minimum lease payments for this operating lease at December 31, 2017, are due as follows:

Years ending December 31:	
2018	\$ 291,250
2019	300,003
2020	304,478
2021	286,996
2022	295,614
Thereafter	1,080,116
	<u>\$ 2,558,457</u>

## Horatio Alger Association of Distinguished Americans, Inc. and Affiliate

### Notes to Consolidated Financial Statements

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#### **Note 10. Related Party Transactions**

The Association receives significant support in the form of contributions from Board members. During the year ended December 31, 2017, total gross support from Board members was \$36,544,584 and as of December 31, 2017, total gross contributions receivable from Board members was \$16,541,773.

Horatio Alger Association of Canada (HAA – Canada) is a charitable organization dedicated to the belief that hard work, honesty and determination can conquer all obstacles. The Board of Directors of HAA – Canada is comprised of six individuals, two of which are also on the Board of Directors of the Association. The Association has no financial interest in HAA – Canada and, thus, there is no consolidation. During the year ended December 31, 2017, the Association provided HAA – Canada approximately \$202,600 of contributions, of which approximately \$176,000 was unpaid at December 31, 2017 and is included within accounts payable on the consolidated statement of financial position. During the year ended December 31, 2017, the Association additionally provided HAA – Canada approximately \$30,700 of donated services.

#### **Note 11. Commitments**

The Association has in place a signed employment agreement with its Executive Director, which includes a severance package to be paid if employment is terminated without cause. The employment agreement with the Executive Director of the Association also provides certain deferred compensation benefits.

The Association has entered into several agreements for meeting space through 2019. In the event of cancellation, the Association is required to pay various costs as stipulated in the contracts, the amounts of which are dependent upon the date of cancellation. This amount is not accrued in the accompanying consolidated financial statements, as management does not believe any losses will be incurred under these contracts.