

CONSOLIDATED FINANCIAL STATEMENTS

The Cleveland Foundation
Years Ended December 31, 2018 and 2017
With Report of Independent Auditors

Ernst & Young LLP



The Cleveland Foundation

Consolidated Financial Statements

Years Ended December 31, 2018 and 2017

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Report of Independent Auditors

The Board of Directors
The Cleveland Foundation

We have audited the accompanying consolidated financial statements of The Cleveland Foundation, which comprise the consolidated statements of financial position as of December 31, 2018 and 2017, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management’s Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of 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 consolidated financial position of The Cleveland Foundation at December 31, 2018 and 2017, and the consolidated changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

July 18, 2019

The Cleveland Foundation

Consolidated Statements of Financial Position

	December 31	
	2018	2017
Assets		
Cash and cash equivalents	\$ 15,693,360	\$ 16,326,088
Short-term investments	239,158,869	267,539,949
Investments	2,003,809,546	2,141,565,949
Other investments	20,821,504	20,184,751
Property and other assets	8,658,326	7,746,328
Total assets	<u>\$2,288,141,605</u>	<u>\$2,453,363,065</u>
 Liabilities and net assets		
Accounts payable, accrued expenses and payable for unsettled trades	\$ 7,913,834	\$ 2,874,602
Grants payable	29,560,067	30,610,342
Organizational funds and other obligations	136,812,978	133,597,191
Total liabilities	<u>174,286,879</u>	167,082,135
 Net assets:		
Without donor restrictions	924,671,180	1,009,796,597
With donor restrictions	1,189,183,546	1,276,484,333
Total net assets	<u>2,113,854,726</u>	<u>2,286,280,930</u>
Total liabilities and net assets	<u>\$2,288,141,605</u>	<u>\$2,453,363,065</u>

See accompanying notes.

The Cleveland Foundation

Consolidated Statements of Activities

December 31, 2018

	Without Donor Restrictions	With Donor Restrictions	Total
Revenues, gains, and other support			
Contributions	\$ 44,584,060	\$ 20,825,502	\$ 65,409,562
Net investment income	34,142,714	280,855	34,423,569
Net realized and unrealized gains (loss) on investments	(49,834,576)	(106,557,085)	(156,391,661)
Other income	951,791	37,708	989,499
Net assets released resulting from satisfaction of donor and program restrictions	1,887,767	(1,887,767)	–
Total revenues, gains, and other support	<u>31,731,756</u>	<u>(87,300,787)</u>	<u>(55,569,031)</u>
Expenses			
Grants expensed	101,172,153	–	101,172,153
Program services	7,742,694	–	7,742,694
Management and general	2,747,164	–	2,747,164
Fundraising and development	5,195,162	–	5,195,162
Total expenses	<u>116,857,173</u>	<u>–</u>	<u>116,857,173</u>
Decrease in net assets	(85,125,417)	(87,300,787)	(172,426,204)
Net assets at beginning of year	<u>1,009,796,597</u>	<u>1,276,484,333</u>	<u>2,286,280,930</u>
Net assets at end of year	<u>\$ 924,671,180</u>	<u>\$ 1,189,183,546</u>	<u>\$ 2,113,854,726</u>

See accompanying notes.

The Cleveland Foundation

Consolidated Statements of Activities

December 31, 2017

	Without Donor Restrictions	With Donor Restrictions	Total
Revenues, gains, and other support			
Contributions	\$ 55,513,362	\$ 11,254,863	\$ 66,768,225
Net investment income	29,122,242	253,205	29,375,447
Net realized and unrealized gains on investments	158,444,273	127,596,790	286,041,063
Other income	832,746	99,781	932,527
Net assets released resulting from satisfaction of donor and program restrictions	3,355,350	(3,355,350)	—
Total revenues, gains, and other support	247,267,973	135,849,289	383,117,262
Expenses and losses			
Grants expensed	97,396,952	—	97,396,952
Program services	7,057,918	—	7,057,918
Management and general	3,070,411	—	3,070,411
Fundraising and development	5,027,604	—	5,027,604
Total expenses	112,552,885	—	112,552,885
Increase in net assets	134,715,088	135,849,289	270,564,377
Net assets at beginning of year	875,081,509	1,140,635,044	2,015,716,553
Net assets at end of year	\$1,009,796,597	\$1,276,484,333	\$2,286,280,930

See accompanying notes.

The Cleveland Foundation

Consolidated Statements of Cash Flows

	Year Ended December 31	
	2018	2017
Operating activities		
(Decrease) increase in net assets	\$ (172,426,204)	\$ 270,564,377
Adjustments to reconcile (decrease) increase in net assets to net cash (used in) provided by operating activities:		
Depreciation	228,082	227,070
Net realized and unrealized losses (gains) on investments	156,391,661	(286,041,063)
Contributions restricted for investment in perpetual endowment	(18,918,126)	(9,984,630)
Increase in other assets	(1,098,652)	(3,586,130)
Increase in accounts payable, organizational funds and accrued expenses	5,075,490	43,874,850
Decrease in grants payable	(1,050,275)	(1,151,788)
Net cash (used in) provided by operating activities	(31,798,024)	13,902,686
Investing activities		
Purchases of property and equipment	(41,428)	(69,532)
Proceeds from sale or maturity of investments	845,928,484	1,363,790,311
Purchases of investments	(833,639,886)	(1,382,727,500)
Net cash provided by (used in) investing activities	12,247,170	(19,006,721)
Financing activities		
Contributions restricted for investment in perpetual endowment	18,918,126	9,984,630
Net cash provided by financing activities	18,918,126	9,984,630
Net (decrease) increase in cash and cash equivalents	(632,728)	4,880,595
Cash and cash equivalents at beginning of year	16,326,088	11,445,493
Cash and cash equivalents at end of year	\$ 15,693,360	\$ 16,326,088

The Cleveland Foundation

Notes to Consolidated Financial Statements

December 31, 2018

1. Description and Purpose of The Foundation

The Cleveland Foundation (The Foundation) is a not-for-profit organization established in 1914. The mission statement of The Foundation is “to enhance the lives of all residents of Greater Cleveland, now and for generations to come, by working together with our donors to build community endowment, address needs through grantmaking, and provide leadership on key community issues.”

The accompanying consolidated financial statements include the accounts of The Cleveland Foundation (charitable corporation), The Greater Cleveland Foundation, The Cleveland Foundation (community trust approved by Resolutions of Trust), and the following affiliated supporting organizations: The City of Cleveland’s Cable Television Minority Arts and Education Fund, The Higley Fund, The Billie Howland Steffee Family Fund, Medical Mutual of Ohio Charitable Foundation, Sullivan Scholars Foundation, The Thatcher Family Fund, the Frank Hadley and Cornelia Root Ginn Foundation and the Sally and John Morley Family Fund. The affiliated supporting organizations were established under the provisions of Section 509(a)(3) of the Internal Revenue Code. The Foundation is responsible for expenditures of these affiliated supporting organizations for specific charitable purposes. All significant interorganizational balances and transactions have been eliminated in the preparation of the accompanying consolidated financial statements.

The Internal Revenue Service has ruled that the charitable corporation, The Greater Cleveland Foundation, the community trust, and the affiliated supporting organizations are tax-exempt organizations that are exempt from federal income taxation under Section 501(c)(3) of the Internal Revenue Code.

2. Summary of Significant Accounting Policies

Basis of Accounting – The accompanying consolidated financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP). The Financial Accounting Standards Board (FASB) has established the Accounting Standards Codification (ASC) as the source of authoritative accounting principles to be applied in the preparation of financial statements in accordance with GAAP.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Net Assets

Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions.

Net assets without donor restrictions are used to differentiate resources, the use of which is restricted by donors or grantors to a specific time period or purpose, from resources on which no restrictions have been placed or that arise from the general operations of The Foundation.

The Resolutions and Declaration of Trusts establishing The Foundation include a variance power provision giving the Board of Directors of The Foundation the power to modify any restriction or condition on the distribution of funds for any specific charitable purpose or to specified organizations if, in the sole judgment of the Board of Directors of The Foundation, such restriction or condition becomes, in effect, unnecessary, undesirable, impractical, incapable of fulfillment, or inconsistent with the charitable needs of the community or area served. Based on this provision, The Foundation's net assets without donor restriction include funds designated for donor-advised grants. The Board of Directors of The Foundation is also granted the authority to distribute 20% of the principal of the donated trust assets over a five-year period.

The Foundation's net assets with donor restrictions include 80% of the principal of The Foundation's endowment assets (these net assets with donor-imposed restrictions are perpetual and are expected to be maintained in perpetuity in accordance with the Resolutions and Declaration of Trusts establishing The Foundation), charitable remainder unitrusts (CRUT), charitable remainder annuity trusts (CRAT), charitable lead annuity trusts (CLAT), charitable gift annuities (CGA) and The Foundation's special projects.

Revenues are reported as increases in net assets without donor restrictions unless use of the related asset is limited by donor-imposed restrictions. Expenses are reported as decreases in net assets without donor restrictions, since the use of restricted contributions in accordance with donor's stipulations results in the release of restriction. Gains or losses on investments and other assets or liabilities are reported as increase or decreases in net assets without donor restrictions unless their use is restricted by explicit donor stipulation or by law. Expirations of donor-imposed 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 between the applicable classes of net assets.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Concentration of Credit Risk

Financial instruments that potentially expose The Foundation to concentrations of credit risk include cash and cash equivalents and investments. As a matter of policy, The Foundation only maintains cash balances with financial institutions having a high credit quality. Concentration of credit risk for investments is mitigated by both the distribution of investment funds among asset managers and the overall diversification of managed investment portfolios.

Cash and Cash Equivalents

The Foundation considers all highly liquid investments purchased with original maturities of three months or less, excluding amounts limited to use by the Board of Directors of The Foundation or other arrangements, to be cash and cash equivalents.

Short-Term Investments

Short-term investments represent investments with maturities of one year or less, are recorded at fair value, and consist from time to time of money market funds, short-term collective funds, mutual funds, certificates of deposit, commercial paper, short-term corporate bonds, variable rate demand notes, U.S. Treasury bills, and U.S. Treasury or agency notes or bonds with maturities under one year.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Investments and Investment Income

Investments are recorded at fair value.

Realized investment gains or losses are the differences between the carrying value of an investment and net proceeds received on the trade date. Unrealized investment gains or losses are the differences between carrying value and fair value of an investment at each statement of financial position date. These amounts are reported in the consolidated statements of activities as net realized and unrealized investment gains and losses.

Dividend and interest income are reported in the consolidated statements of activities as net investment income. Net unrealized and realized investment gains and losses are reported as net assets without donor restrictions or net assets with donor restrictions based upon the absence or presence of a restriction of the underlying assets.

Organizational Funds

The Foundation acts as fiduciary agent for various not-for-profit organizations. The Foundation's responsibilities as fiduciary agent include, but are not limited to, safeguarding of assets, record-keeping of transactions, investment management, and ensuring appropriate fund distributions. The Foundation's policy as fiduciary agent is to record funds received as an investment and an equal liability. The Foundation, as fiduciary agent, has recorded \$131,563,645 and \$129,078,852 at December 31, 2018 and 2017, respectively, related to organizational funds in investments and an equal liability in organizational funds and other obligations in the consolidated statements of financial position. The Foundation does not include the change in investments and related liability for organizational funds in the consolidated statements of activities.

Recent Accounting Pronouncements

In August 2016, the FASB issued Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities*. This ASU intends to make certain improvements to the reporting requirements for not-for-profit entities. This standard sets forth changes to net asset classification requirements and the information presented about a not-for-profit entity's liquidity, financial performance and cash flows. The Foundation adopted ASU 2016-14 in its consolidated financial statements in 2018 applying retrospectively to all periods presented. The adoption changes the classification of net assets on the consolidated statements of financial

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

position and consolidated statements of activities from three classes of net assets to two classes of net assets. Funds designated for donor-advised grants which were previously included in temporarily restricted net assets are included in net assets without donor restriction due to the variance powers provision. In addition, direct internal investment expense and trustee and management fees were netted against net investment income. The Foundation also added disclosure for the liquidity and availability of financial assets at the statement of financial position date to meet cash needs for general expenditures within one year and disaggregated functional expense classifications by their natural expense classification. The adoption of ASU 2016-14 had no impact to total net assets.

In February 2016, the FASB issued ASU 2016-02, *Leases*. This ASU requires lessees to recognize assets and liabilities on the balance sheet for leases with lease terms greater than 12 months. The recognition, measurement and presentation of expenses and cash flows from a lease by a lessee primarily will depend on its classification as a finance or operating lease. This amends current guidance that requires only capital leases to be recognized on the lessee balance sheet. ASU 2016-02 will also require additional disclosures on the amount, timing and uncertainty of cash flows arising from leases. The guidance is effective for The Foundation for reporting periods beginning after December 15, 2019 with early adoption permitted. The Foundation is currently evaluating the impact that ASU 2016-02 will have on its consolidated financial statements and will adopt the provisions upon the effective date.

In June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities, Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. This ASU intends to clarify and improve current accounting guidance to determine when a transaction should be accounted for as a contribution or as an exchange transaction and provides additional guidance about how to determine whether a contribution is conditional. The ASU is effective for The Foundation for annual reporting periods beginning after December 15, 2018. The Foundation is currently assessing the impact that ASU 2018-08 will have on its consolidated financial statements and will adopt the provisions upon the effective date.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement, Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement*. This ASU intends to improve the effectiveness of disclosures in the notes to financial statements by modifying disclosure requirements for fair value measurements. The ASU is effective for The Foundation for annual and interim reporting periods beginning after December 15, 2019 with early adoption permitted. The Foundation is currently assessing the impact that ASU 2018-13 will have on its consolidated financial statements and will adopt the provisions upon the effective date.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

3. Endowment Assets

The Foundation's endowment consists of more than 500 individual donor-restricted funds established for a variety of purposes. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions. The Foundation believes that these endowment funds are not subject to the Uniform Prudent Management of Institutional Funds Act adopted by the state of Ohio in 2009.

The endowment funds of The Foundation are the portion of The Foundation's net assets without donor restrictions and net assets with donor restrictions that are governed by the Resolutions and Declaration of trusts establishing The Foundation. The endowment funds are the result of trusts established by donors with the intention that the funds will exist in perpetuity. Endowment funds are reported in accordance with the stipulations of the governing instruments of The Foundation. Per the governing instruments, the Board of Directors of The Foundation may distribute 20% of the principal of the donated trust assets over a five-year period. This amount is recognized as net assets without donor restrictions, with the remainder of net assets recognized as net assets with donor restrictions

Return Objectives

The endowment funds are actively managed by four trustee banks in collaboration with the Board of Directors of The Foundation. An Investment Committee comprised of board members and volunteers has established a set of investment policies that guide investment decisions. The Investment Committee is responsible for establishing an asset allocation strategy and monitoring the performance of investment managers. The Investment Committee reports to the Board of Directors of The Foundation on a quarterly basis. The investment policies of The Foundation describe the type of investments that may be employed to achieve the total return objectives identified in the policies.

The long-term return objective is to maintain the purchasing power of The Foundation's investments by earning a return to cover The Foundation's spending policy (for both grants and administrative expenses) and inflation over time. Investment performance is monitored by the Investment Committee against the long-term return objective and a set of standard market benchmark indexes. Actual rates of return may vary from the long-term return objective.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

3. Endowment Assets (continued)

Investment Strategy

The Foundation implements an investment strategy that is diversified among equities, fixed income and alternative investments. The Foundation is diversified not only in terms of asset class, but also by employing a broad number of investment managers that provide diversity in investment styles and approach. The Foundation believes a well-diversified strategy will help the investment portfolio reach its long-term return objective with lower overall investment risk.

Spending Policy

The Foundation has an annual spending policy for grant-making and administrative expense that is based upon the investment return over a longer-term horizon. The intent is to tie spending to investment performance and limit volatility in spending while maintaining the purchasing power of the endowment assets over time. The policy includes a formula that applies a percentage rate to the average market value of the endowment assets for the 12 quarters ending the previous June 30. The Board of Directors of The Foundation approves the rate annually within a range of 4.5% to 5.5% and approved 5.0% for 2018 and 2017.

Changes in endowment net assets are as follows:

	2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, January 1, 2018	\$ 352,173,272	\$ 1,266,717,324	\$ 1,618,890,596
Investment return:			
Net investment income	23,174,348	–	23,174,348
Net depreciation (realized and unrealized)	(9,414,339)	(105,579,072)	(114,993,411)
Total investment return	13,760,009	(105,579,072)	(91,819,063)
Contributions	–	18,918,126	18,918,126
Grant distributions and expenses	(106,566,737)	–	(106,566,737)
Endowment net assets, December 31, 2018	\$ 259,366,544	\$ 1,180,056,378	\$ 1,439,422,922

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

3. Endowment Assets (continued)

	2017		
	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, January 1, 2017	\$ 322,277,818	\$ 1,130,594,050	\$ 1,452,871,868
Investment return:			
Net investment income	19,495,730	934	19,496,664
Net appreciation (realized and unrealized)	85,819,919	126,137,710	211,957,629
Total investment return	105,315,649	126,138,644	231,454,293
Contributions	–	9,984,630	9,984,630
Grant distributions and expenses	(75,420,195)	–	(75,420,195)
Endowment net assets, December 31, 2017	\$ 352,173,272	\$ 1,266,717,324	\$ 1,618,890,596

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the entity to retain as a fund of perpetual duration. There were no such deficiencies as of December 31, 2018 and 2017.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

4. Investments

Investments and short-term investments are comprised of the following:

	December 31			
	2018		2017	
Short-term investments (primarily money market funds):	\$ 239,158,869	\$ 239,158,869	\$ 267,539,949	\$ 267,539,949
U.S. government obligations:				
U.S. treasuries	22,294,869		15,978,147	
U.S. government agencies and asset-backed	7,749,340	30,044,209	10,773,950	26,752,097
Bonds:				
Corporate	51,766,694		45,256,676	
Corporate asset-backed and other	4,742,979	56,509,673	5,293,139	50,549,815
Common and preferred stocks:				
Domestic	95,361,964		102,502,741	
International	19,892,941	115,254,905	14,490,138	116,992,879
Common trust funds:				
Domestic and other equity	157,936,018		169,483,110	
International equity	15,711,984		342,631,861	
Fixed income	273,303,488	446,951,490	15,114,121	527,229,092
Mutual and exchange-traded funds:				
Domestic equity and other	363,503,661		435,624,068	
International equity	128,908,439		174,024,690	
Fixed income	141,166,232	633,578,332	97,449,144	707,097,902
Alternative investments:				
Absolute return	202,369,643		208,140,024	
Hedged equity	319,317,452		330,184,001	
Private equity	135,442,929		135,757,840	
Real assets	16,127,599		13,593,785	
Other	48,213,314	721,470,937	25,268,514	712,944,164
 Total investments		<u>\$ 2,242,968,415</u>		<u>\$ 2,409,105,898</u>

The primary investment objectives of short-term investments are liquidity and preservation of principal, with a secondary objective of earning a competitive market rate of return.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

4. Investments (continued)

Common trust funds include The Foundation's interest in non-publicly traded, liquid commingled funds. The investment objective for common trust funds is long-term total return equal to or better than market returns.

Alternative investments are comprised principally of limited partnership interests in absolute return, hedged equity, private equity, and real assets funds. The funds' investment managers employ both traditional strategies (long only) in marketable securities and less traditional strategies (long- and short-equity or fixed income, event-driven, macro, relative value, and arbitrage strategies) that may include the use of options, futures, and other derivative instruments.

The investment objective for absolute return funds is long-term capital appreciation with less volatile and/or uncorrelated returns. Absolute return funds include investment strategies where a majority of the underlying securities may or may not be traded on public exchanges. This asset class includes a variety of active strategies, including arbitrage, event-driven, market neutral, long-short equity and distressed investing.

The investment objective for hedged equity is long-term capital appreciation with low volatility. Hedged equity funds include investment strategies where the majority of the underlying securities are traded on public exchanges. Managers in this asset class may hold long or short equity positions and utilize options, futures, and other derivatives.

The investment objective for private equity is long-term capital appreciation in excess of what is available in the public markets. Private equity funds generally hold illiquid debt and equity securities of public and/or privately held companies. This asset class includes venture capital, secondary, mezzanine, buyout, and distressed funds.

The investment objective for real assets is to protect against inflation and increase long-term returns. Real assets include liquid and illiquid investments in funds that own real estate, commodities, oil and gas, inflation-protected fixed income securities, and other assets.

At December 31, 2018, The Foundation has outstanding capital contribution commitments with several alternative investment funds of approximately \$132,425,419.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

4. Investments (continued)

At December 31, 2018, The Foundation's alternative investments are subject to various withdrawal restrictions as follows:

Available for redemption:	
Monthly	\$ 295,480,875
Quarterly	102,025,332
Annually	<u>70,114,844</u>
Subtotal	467,621,051
Subject to distribution	163,337,559
Subject to lock-up provisions:	
One to three years	<u>90,512,327</u>
Total alternative investments	<u>\$ 721,470,937</u>

Investments that are available for redemption may be redeemed by The Foundation generally with 30- to 60-day advance notice on a monthly, quarterly, or annual basis subject to the terms of the investment agreement.

Investments subject to distribution cannot be redeemed by The Foundation but rather will be distributed by the investment fund or limited partnership upon the liquidation of the underlying assets of the fund or limited partnership. Distributions are generally expected, but not guaranteed, over the next three to ten years.

Investments subject to lock-up provisions cannot be redeemed by The Foundation currently. After expiration of the lock-up provisions, the funds may be redeemed by The Foundation on a monthly, quarterly, or annual redemption basis subject to the terms of the investment agreement.

Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the consolidated statements of financial position.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

5. Fair Value Measurement

Fair value is the price to sell an asset or transfer a liability in an orderly transaction between market participants. It represents an exit price at the measurement date. Market participants are buyers and sellers who are independent, knowledgeable, and willing and able to transact in the principal, or most advantageous, market for the asset or liability being measured. Current market conditions, including imbalances between supply and demand, are considered in determining fair value.

The carrying values of cash and cash equivalents, accounts payable, accrued expenses, and grants payable are reasonable estimates of fair value due to the short-term nature of these financial instruments. The carrying value of other investments, primarily notes receivable, are reasonable estimates of fair value due to the interest rates on notes receivable approximating current lending rates.

ASC 820, *Fair Value Measurement*, establishes a fair value hierarchy that distinguishes between market participant assumptions developed based on market data obtained from sources independent of the reporting entity, observable inputs, and the reporting entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances and unobservable inputs. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

Fair value for Level 1 is based upon quoted market prices that are comprised of publicly traded securities, registered money markets, and mutual and exchange-traded funds. Investments in securities traded on a national securities exchange are valued at the last reported sales price each day as reported by a recognized pricing service. Securities traded in the over-the-counter market and listed securities for which no sale was reported on that date are valued at fair value, based on the mean of the most recent bid and ask price and other market information available.

Fair value for non-registered money market funds and common trust funds are valued at net asset value as a practical expedient. Fair value for Level 2 American Depositary Receipts (ADRs) of foreign common and preferred stocks are valued at quoted market prices (adjusted for currency rates).

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

5. Fair Value Measurement (continued)

Fair value for Level 2 U.S. government obligations and bonds is based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant inputs are observable in the market or can be corroborated by observable market data for substantially the full term of the assets. Inputs are obtained from various sources, including market participants, dealers, and brokers.

Level 3 inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Total investments are reflected in the consolidated statements of financial position as follows:

	<u>2018</u>	<u>2017</u>
Short-term investments	\$ 239,158,869	\$ 267,539,949
Investments	2,003,809,546	2,141,565,949
Total	<u>\$ 2,242,968,415</u>	<u>\$ 2,409,105,898</u>

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

5. Fair Value Measurement (continued)

Total investments subject to fair value measurement, aggregated by the level in the fair value hierarchy, are as follows:

	December 31, 2018		
	Total	Level 1	Level 2
Short-term investments (primarily money market funds)*	\$ 239,158,869	\$ 78,104,924	\$ —
U.S. government obligations	30,044,209	—	30,044,209
Bonds	56,509,673	—	56,509,673
Common and preferred stocks	115,254,905	115,254,905	—
Common trust funds*	446,951,490	—	—
Mutual and exchange-traded funds	633,578,332	633,578,332	—
Alternative investments*:			
Absolute return	202,369,644	—	—
Hedged equity	319,317,451	—	—
Private equity	135,442,929	—	—
Real assets	16,127,599	—	—
Other	48,213,314	—	21,213,314
Total	\$ 2,242,968,415	\$ 826,938,161	\$ 107,767,196

	December 31, 2017		
	Total	Level 1	Level 2
Short-term investments (primarily money market funds)*	\$ 267,539,949	\$ 66,422,842	\$ —
U.S. government obligations	26,752,097	—	26,752,097
Bonds	50,549,815	—	50,549,815
Common and preferred stocks	116,992,879	116,927,429	65,450
Common trust funds*	527,229,092	—	—
Mutual and exchange-traded funds	707,097,902	707,097,902	—
Alternative investments*:			
Absolute return	208,140,024	—	—
Hedged equity	330,184,001	—	—
Private equity	135,757,840	—	—
Real assets	13,593,785	—	—
Other	25,268,514	—	25,268,514
Total	\$ 2,409,105,898	\$ 890,448,173	\$ 102,635,876

*In accordance with ASC Subtopic 820-10, certain investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been classified in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the consolidated statements of financial position.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

5. Fair Value Measurement (continued)

The Foundation believes its valuation methods are appropriate and consistent with other market participants and represent a reasonable estimate of fair value. The use of different methodologies or assumptions to determine the fair value of certain financial instruments, particularly alternative investments, could result in a different estimate of fair value.

6. Liquidity and Availability of Resources

Financial assets available for grant-making, general expenditures, liabilities or other obligations, that is within one year of the statement of financial position date, are comprised of the following:

	<u>2018</u>
Cash and cash equivalents	\$ 15,693,360
Short-term investments	161,696,346
Total	<u>\$ 177,389,706</u>

The Board of Directors of The Foundation has approved an annual spending policy rate of 5% for 2018 and 2017. As described in Note 3, a spending policy is created to maintain sustainable grant-making over a long period of time. Although, the Foundation does not intend to spend amounts above the annual spending policy, these amounts could be made available if necessary.

As part of The Foundation's liquidity management, it has a policy to structure its financial assets to be available as its grants, general expenditures, liabilities and other obligations become due. The Foundation invests cash in excess of daily requirements in short-term investments and money market funds. Other investments are excluded as they are not normally used for grant-making, general expenditures, liabilities or other obligations.

7. Partial Benefit Funds

Partial benefit funds provide, each in varying amounts, payment of annuities to certain individuals, trustees' fees and other expenses of the trusts, prior to payment of the balance of the corpus to The Foundation. The Foundation received income from partial benefit funds of \$10,783,642 and \$10,761,558 in 2018 and 2017, respectively, which is recorded in net assets without donor restrictions net investment income within the consolidated statements of activities. This represented approximately 99% of the income from partial benefit funds in 2018 and 2017. At December 31, 2018 and 2017, the fair value of partial benefit funds included in investments on the consolidated statements of financial position was \$229,509,089 and \$248,969,870, respectively.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

8. Contributions

The Foundation receives contributions from various sources. Donor contributions received are recorded on the consolidated statements of activities. Receipts of organizational funds are not included on the consolidated statements of activities, but are reflected in investments and in organizational funds and other obligations in the consolidated statements of financial position. Total contributions received are as follows:

	2018	2017
Donor contributions	\$ 65,409,562	\$ 66,768,225
Organizational funds	17,132,805	45,530,115
	\$ 82,542,367	\$ 112,298,340

9. Grants and Distributions

The Board of Directors of The Foundation authorized grants of \$104,770,326 and \$141,016,535 in 2018 and 2017, respectively, and program-related investments of \$11,500,000 and \$1,250,000 in 2018 and 2017, respectively. In addition, distributions from organizational funds of \$10,628,151 and \$3,463,348 were made in 2018 and 2017, respectively, and are not included in grants expensed in the consolidated statements of activities.

Unconditional grants are expensed upon approval by the Board of Directors of The Foundation. Conditional grants, which are approved by the Board of Directors of The Foundation and payable upon the performance of specified conditions by the grantees, are expensed when the specified conditions are satisfied.

Changes in grants payable are as follows:

	2018	2017
Grants payable at beginning of year	\$ 30,610,342	\$ 31,762,130
Unconditional grants expensed	101,172,153	97,396,952
Payments made	(102,222,428)	(98,548,740)
Grants payable at end of year	\$ 29,560,067	\$ 30,610,342

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

9. Grants and Distributions (continued)

Grants payable at December 31, 2018, are scheduled to be disbursed as follows: 2019 – \$25,578,984, 2020 – \$3,052,925, and 2021 and thereafter – \$928,158. At December 31, 2018 and 2017, total authorized conditional grants were \$974,277 and \$1,661,258, respectively.

10. Affiliated Supporting Organizations

The total assets of affiliated supporting organizations included in the consolidated financial statements are as follows:

	December 31	
	2018	2017
The City of Cleveland’s Cable Television		
Minority Arts and Education Fund	\$ 4,315,168	\$ 4,696,593
The Higley Fund	34,634,882	37,964,704
The Billie Howland Steffee Family Fund	–	6,563,551
Medical Mutual of Ohio Charitable Foundation	2,272,116	2,498,032
Sullivan Scholars Foundation	3,917,400	4,292,821
The Thatcher Family Fund	6,727,141	7,522,914
Frank Hadley and Cornelia Root Ginn Foundation	2,694,006	3,105,271
Sally and John Morley Family Fund	4,282,478	4,893,431
	\$ 58,843,191	\$ 71,537,317

The Treu-Mart Fund is a supporting organization of both The Foundation and the Jewish Federation of Cleveland. Financial transactions and account balances of The Treu-Mart Fund are not included in the accompanying consolidated financial statements because The Foundation does not have control over the distribution of The Treu-Mart Fund. Fair value of investments held by The Treu-Mart Fund at December 31, 2018 and 2017, were \$16,567,244 and \$18,671,464, respectively.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

11. Other Investments

Other investments of \$20,821,504 and \$20,184,751 in 2018 and 2017, respectively, primarily include program-related investments (notes receivable and investments in limited partnerships that support certain program initiatives). Notes receivable are due at various dates from 2018 through 2025, except for one loan for which the due date is 2033. The loans carry fixed interest rates between 2% and 4%; principal and interest payment arrangements vary by note.

12. Operating Lease

The Foundation leases office space under a primary operating lease agreement, which expires in 2020. Rental expense was \$1,055,830 and \$1,010,939 in 2018 and 2017, respectively. Future minimum rental commitments under the non-cancelable primary operating lease at December 31, 2018, are \$912,000 in 2019, and \$608,000 in 2020.

13. Retirement Plan

The Foundation has defined contribution retirement plans. The Foundation made contributions based upon specified percentages of salary for all employees. Retirement plan expense was \$743,641 and \$658,180 in 2018 and 2017, respectively. All contributions under the plan are fully vested at the time the contributions are made.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

14. Functional Allocation of Expenses

The following table represents expenses by both their nature and function for the years ended December 31, 2018 and 2017.

	2018				
	Program Services		Management and General	Fundraising and Development	Total
	Grants	Other			
Grants expended	\$ 101,172,153	\$ –	\$ –	\$ –	\$ 101,172,153
Salaries	–	4,165,377	1,092,296	2,776,055	8,033,728
Benefits	–	1,340,238	355,085	903,551	2,598,874
Professional fees and consulting	–	488,953	520,288	318,543	1,327,784
Office and occupancy	–	740,499	147,746	296,331	1,184,576
Equipment and supplies	–	411,321	95,733	250,421	757,475
Travel and expense	–	99,762	14,143	53,408	167,313
Depreciation and amortization	–	126,804	31,043	70,235	228,082
Other expenses	–	369,740	490,830	526,618	1,387,188
Total	\$ 101,172,153	\$ 7,742,694	\$ 2,747,164	\$ 5,195,162	\$ 116,857,173

	2017				
	Program Services		Management and General	Fundraising and Development	Total
	Grants	Other			
Grants expended	\$ 97,396,952	\$ –	\$ –	\$ –	\$ 97,396,952
Salaries	–	3,780,469	1,046,023	2,619,959	7,446,451
Benefits	–	1,212,560	331,828	855,983	2,400,371
Professional fees and consulting	–	226,949	475,844	219,531	922,324
Office and occupancy	–	709,293	141,763	284,396	1,135,452
Equipment and supplies	–	468,768	119,754	322,404	910,926
Travel and expense	–	85,582	16,963	57,470	160,015
Depreciation and amortization	–	121,638	32,506	72,926	227,070
Other expenses	–	452,659	905,730	594,935	1,953,324
Total	\$ 97,396,952	\$ 7,057,918	\$ 3,070,411	\$ 5,027,604	\$ 112,552,885

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

14. Functional Allocation of Expenses (continued)

The costs of providing the various program and supporting services have been summarized on a functional basis in the consolidated statements of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

The consolidated financial statements report expenses that are attributed to more than one program or supporting function. Therefore, expenses require allocation on a reasonable basis that is consistently applied. Certain expenses, excluding grants expensed, are allocated on a reasonable basis.

15. Subsequent Events

In preparing these consolidated financial statements, The Foundation evaluated subsequent events through the time the financial statements were available to be issued on July 18, 2019 in compliance with applicable accounting standards. All material subsequent events have been either recognized in the consolidated financial statements or disclosed in the notes to the consolidated financial statements.

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