

CONSOLIDATED FINANCIAL STATEMENTS

The Cleveland Foundation
Years Ended December 31, 2016 and 2015
With Report of Independent Auditors

Ernst & Young LLP



Building a better
working world

The Cleveland Foundation

Consolidated Financial Statements

Years Ended December 31, 2016 and 2015

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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, 2016 and 2015, 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, 2016 and 2015, and the changes in its consolidated net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

August 7, 2017

The Cleveland Foundation

Consolidated Statements of Financial Position

	December 31	
	2016	2015
Assets		
Cash	\$ 11,445,493	\$ 14,630,431
Short-term investments	178,887,018	147,913,228
Investments	1,926,789,704	1,916,283,775
Other investments	18,635,675	17,930,801
Property and other assets	4,317,736	6,831,265
	<u>\$2,140,075,626</u>	<u>\$2,103,589,500</u>
Liabilities and net assets		
Accounts payable, accrued expenses, and payable for unsettled trades	\$ 15,641,417	\$ 13,903,605
Grants payable	31,762,130	27,812,798
Organizational funds and other obligations	76,955,526	106,148,806
Total liabilities	<u>124,359,073</u>	<u>147,865,209</u>
Net assets:		
Unrestricted:		
For grant-making purposes	4,302,462	4,275,237
Board-designated:		
Administrative purposes	15,639,816	13,910,433
Property	1,071,023	1,249,657
Total unrestricted	<u>21,013,301</u>	<u>19,435,327</u>
Temporarily restricted	864,109,202	842,782,400
Permanently restricted	1,130,594,050	1,093,506,564
	<u>2,015,716,553</u>	<u>1,955,724,291</u>
	<u>\$2,140,075,626</u>	<u>\$2,103,589,500</u>

See accompanying notes.

The Cleveland Foundation

Consolidated Statements of Activities

Year Ended December 31, 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains, and other support				
Donor contributions	\$ 68,258	\$ 25,453,179	\$ 696,554	\$ 26,217,991
Dividend and interest income	45,321	34,528,066	-	34,573,387
Net realized and unrealized investment gains (losses)	5,197,640	67,803,235	36,390,932	109,391,807
Net assets released from restrictions	107,166,439	(107,166,439)	-	-
Other income	85,911	708,761	-	794,672
Total revenue, gains and other support	112,563,569	21,326,802	37,087,486	170,977,857
Expenses				
Grants expensed	91,670,352	-	-	91,670,352
Trustee bank and investment management fees	4,662,702	-	-	4,662,702
Other expenses	552,664	-	-	552,664
Administrative expenses:				
Program	7,112,488	-	-	7,112,488
Development	4,671,134	-	-	4,671,134
Fund management	2,316,255	-	-	2,316,255
Total administrative expenses	14,099,877	-	-	14,099,877
Total expenses	110,985,595	-	-	110,985,595
Increase in net assets	1,577,974	21,326,802	37,087,486	59,992,262
Net assets at beginning of year	19,435,327	842,782,400	1,093,506,564	1,955,724,291
Net assets at end of year	\$ 21,013,301	\$ 864,109,202	\$ 1,130,594,050	\$ 2,015,716,553

See accompanying notes.

The Cleveland Foundation

Consolidated Statements of Activities

Year Ended December 31, 2015

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenues, gains, and other support				
Donor contributions	\$ 102,290	\$ 61,212,594	\$ 1,369,957	\$ 62,684,841
Dividend and interest income	30,173	36,829,578	-	36,859,751
Net realized and unrealized investment gains (losses)	9,609,417	13,861,241	(74,750,898)	(51,280,240)
Net assets released from restrictions	120,199,334	(120,199,334)	-	-
Other income	89,388	553,587	-	642,975
Total revenue, gains (losses), and other support	130,030,602	(7,742,334)	(73,380,941)	48,907,327
Expenses				
Grants expensed	106,643,918	-	-	106,643,918
Trustee bank and investment management fees	6,542,766	-	-	6,542,766
Other expenses	2,265,992	-	-	2,265,992
Administrative expenses:				
Program	6,583,407	-	-	6,583,407
Development	4,460,290	-	-	4,460,290
Fund management	2,223,793	-	-	2,223,793
Total administrative expenses	13,267,490	-	-	13,267,490
Total expenses	128,720,166	-	-	128,720,166
Increase (decrease) in net assets	1,310,436	(7,742,334)	(73,380,941)	(79,812,839)
Net assets at beginning of year	18,124,891	850,524,734	1,166,887,505	2,035,537,130
Net assets at end of year	\$ 19,435,327	\$ 842,782,400	\$ 1,093,506,564	\$ 1,955,724,291

See accompanying notes.

The Cleveland Foundation

Consolidated Statements of Cash Flows

	Year Ended December 31	
	2016	2015
Operating activities		
Increase (decrease) in net assets	\$ 59,992,262	\$ (79,812,839)
Adjustments to reconcile increase (decrease) in net assets to net cash (used in) provided by operating activities:		
Depreciation	232,422	226,318
Net unrealized investment (gains) losses	(92,121,594)	90,506,727
Permanently restricted contributions	(696,554)	(1,369,957)
Decrease (increase) in other assets	2,334,896	(2,191,057)
Decrease in accounts payable, organizational funds and accrued expenses	(27,521,975)	(4,251,644)
Increase in grants payable	3,949,332	781,587
Net cash (used in) provided by operating activities	<u>(53,831,211)</u>	3,889,135
Investing activities		
Purchases of property and equipment	(53,789)	(187,339)
Proceeds from sale or maturity of investments	934,037,307	1,154,783,476
Purchases of investments	(884,033,799)	(1,158,679,687)
Net cash provided by (used in) investing activities	<u>49,949,719</u>	(4,083,550)
Financing activities		
Permanently restricted contributions	696,554	1,369,957
Net cash provided by financing activities	<u>696,554</u>	1,369,957
Net (decrease) increase in cash and cash equivalents	(3,184,938)	1,175,542
Cash at beginning of year	14,630,431	13,454,889
Cash at end of year	<u>\$ 11,445,493</u>	<u>\$ 14,630,431</u>

See accompanying notes.

The Cleveland Foundation

Notes to Consolidated Financial Statements

December 31, 2016

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 Davis Fund, The Higley Fund, The Billie Howland Steffee Family Fund, Medical Mutual of Ohio Charitable Foundation, Sullivan Scholars Foundation and The Thatcher 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. Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

2. Significant Accounting Policies (continued)

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 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.

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 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 generated from temporarily or permanently restricted net assets is reported as temporarily restricted until the program restriction is met. Net unrealized and realized investment gains and losses are reported as unrestricted, temporarily restricted, or permanently restricted based upon the absence or presence of a restriction of the underlying assets.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

2. Significant Accounting Policies (continued)

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 \$72,687,186 and \$101,946,973 at December 31, 2016 and 2015, 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 the change in organizational funds in the consolidated statements of activities.

Recent Accounting Pronouncements

In August 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, which requires an entity's management to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued. This update is effective for annual periods ending after December 15, 2016. The Foundation adopted ASU 2014-15 in 2016. The adoption of this standard had no impact on the consolidated financial statements.

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 twelve months. The recognition, measurement and presentation of expenses and cash flows arising 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, 2018 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.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

2. Significant Accounting Policies (continued)

In August 2016, the FASB issued ASU 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities*. This standard intends to make certain improvements to the current 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. ASU 2016-14 is effective for the Foundation for reporting periods beginning after December 15, 2017. The Foundation is currently evaluating the impact that ASU 2016-14 will have on its financial statements and will adopt the provisions upon the effective date.

3. Unrestricted, Temporarily and Permanently Restricted Net Assets

Unrestricted net assets are assets that have no restrictions, or that arise from the general operations of The Foundation. Temporarily restricted net assets are assets that are restricted by donors or grantors for a specific time period or purpose, which include arts and culture, economic development, education, environment, health, human services, neighborhoods and housing, and philanthropic sector, or for the general support of The Foundation. Temporarily restricted gifts, grants, and bequests are recorded as an addition to temporarily restricted net assets in the period received. Assets restricted by donors or grantors for specific operating purposes are reported in unrestricted revenue, gains, and other support to the extent expended within the period. Permanently restricted net assets consist of amounts held in perpetuity and include stipulations by the donor or grantor that the amounts be invested to provide a permanent source of income to support, as described below, arts and culture, economic development, education, environment, health, human services, neighborhoods and housing, and philanthropic sector, or for the general support of The Foundation.

When a donor restriction expires, that is, when a stipulated time restriction ends or program restriction is accomplished, temporarily restricted net assets are transferred to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions.

Unconditional promises to give cash and other assets to The Foundation are reported on the consolidated statements of activities as temporarily or permanently restricted contributions at their net realizable value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date assets are received.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

3. Unrestricted, Temporarily and Permanently Restricted Net Assets (continued)

The Foundation's endowment consists of more than 500 individual donor-restricted funds established for a variety of purposes. 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 temporarily restricted net assets and permanently restricted net assets that are governed by the resolutions of the trusts establishing The Foundation. The 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 Trustees of The Foundation may distribute 20% of the principal of the donated trust assets over a five-year period. This amount is recognized as temporarily restricted net assets, with the remainder of net assets recognized as permanently restricted net assets.

Return Objectives

The endowment funds are actively managed by five 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 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. Unrestricted, Temporarily and Permanently Restricted Net Assets (continued)

Investment Strategy

To achieve the long-term return objective, 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 portfolio construction. By using this portfolio theory, The Foundation is attempting to mitigate risk factors while still taking advantage of return objectives presented within various market cycles.

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 approves the rate annually within a range of 4.5% to 5.5% and approved 5.0% for 2016 and 2015.

Changes in endowment net assets are as follows:

	2016		
	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, January 1, 2016	\$ 315,758,554	\$ 1,093,506,564	\$ 1,409,265,118
Investment return:			
Investment income	22,138,894	–	22,138,894
Net appreciation (realized and unrealized)	53,164,417	36,390,932	89,555,349
Total investment return	75,303,311	36,390,932	111,694,243
Contributions	18,700	696,554	715,254
Released from restriction	(68,802,747)	–	(68,802,747)
Endowment net assets, December 31, 2016	<u>\$ 322,277,818</u>	<u>\$ 1,130,594,050</u>	<u>\$ 1,452,871,868</u>

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

3. Unrestricted, Temporarily and Permanently Restricted Net Assets (continued)

	2015		
	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, January 1, 2015	\$ 341,043,329	\$ 1,166,887,505	\$ 1,507,930,834
Investment return:			
Investment income	22,730,862	–	22,730,862
Net appreciation (depreciation) (realized and unrealized)	31,059,394	(74,750,898)	(43,691,504)
Total investment return	53,790,256	(74,750,898)	(20,960,642)
Contributions	287,860	1,369,957	1,657,817
Released from restriction	(79,362,891)	–	(79,362,891)
Endowment net assets, December 31, 2015	<u>\$ 315,758,554</u>	<u>\$ 1,093,506,564</u>	<u>\$ 1,409,265,118</u>

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the entity to retain as a fund of perpetual duration. There were no such deficiencies as of December 31, 2016 and 2015.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

4. Investments

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

	December 31			
	2016		2015	
Short-term investments (primarily money market funds):	\$ 178,887,018	\$ 178,887,018	<u>\$ 147,913,228</u>	<u>\$ 147,913,228</u>
U.S. government obligations:				
U.S. treasuries	27,106,672		31,720,576	
U.S. government agencies and asset-backed	31,481,212	58,587,884	<u>32,634,254</u>	64,354,830
Bonds:				
Corporate	39,876,118		40,861,118	
Corporate asset-backed and other	6,043,221	45,919,339	<u>7,963,296</u>	48,824,414
Common and preferred stocks:				
Domestic	159,369,889		193,239,488	
International	17,787,059	177,156,948	<u>33,918,848</u>	227,158,336
Common trust funds:				
Domestic and other equity	148,914,108		123,466,936	
International equity	283,003,817		257,066,241	
Fixed income	14,200,758	446,118,683	<u>13,944,241</u>	394,477,418
Mutual and exchange-traded funds:				
Domestic equity and other	338,161,176		269,694,594	
International equity	105,423,434		109,524,739	
Fixed income	60,335,500	503,920,110	<u>88,479,098</u>	467,698,431
Alternative investments:				
Absolute return	216,637,569		234,802,640	
Hedged equity	297,587,494		231,339,909	
Private equity	147,003,460		156,049,656	
Real assets	15,984,907		22,349,394	
Other	17,873,310	695,086,740	<u>18,013,284</u>	662,554,883
Pending purchases of alternative investments	–	–	51,215,463	51,215,463
Total investments	<u>\$ 2,105,676,722</u>		<u>\$ 2,064,197,003</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, 2016, The Foundation has outstanding capital contribution commitments with several alternative investment funds of approximately \$66,745,000.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

4. Investments (continued)

At December 31, 2016, The Foundation's alternative investments are subject to various withdrawal restrictions as follows:

Available for redemption:	
Monthly	\$ 284,999,957
Quarterly	97,073,038
Annually	<u>116,179,042</u>
Subtotal	498,252,037
Subject to distribution	172,281,745
Subject to lock-up provisions:	
One to three years	<u>24,552,958</u>
Total alternative investments	<u><u>\$ 695,086,740</u></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, 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.

Accounting Standards Codification (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 Level 2 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>2016</u>	<u>2015</u>
Short-term investments	\$ 178,887,018	\$ 147,913,228
Investments	1,926,789,704	1,916,283,775
Total	<u>\$ 2,105,676,722</u>	<u>\$ 2,064,197,003</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, 2016		
	Total	Level 1	Level 2
Short-term investments (primarily money market funds)	\$ 178,887,018	\$ 101,576,533	\$ —
U.S. government obligations	58,587,884	—	58,587,884
Bonds	45,919,339	—	45,919,339
Common and preferred stocks	177,156,948	171,588,881	5,568,067
Common trust funds*	446,118,683	—	—
Mutual and exchange-traded funds	503,920,110	503,920,110	—
Alternative investments*:			
Absolute return	216,637,569	—	—
Hedged equity	297,587,494	—	—
Private equity	147,003,460	—	—
Real assets	15,984,907	—	—
Other	17,873,310	—	17,873,310
Pending purchases of alternative investments	—	—	—
Total	\$ 2,105,676,722	\$ 777,085,524	\$ 127,948,600

	December 31, 2015		
	Total	Level 1	Level 2
Short-term investments (primarily money market funds)	\$ 147,913,228	\$ 76,966,885	\$ —
U.S. government obligations	64,354,830	—	64,354,830
Bonds	48,824,414	—	48,824,414
Common and preferred stocks	227,158,336	213,371,465	13,786,871
Common trust funds*	394,477,418	—	—
Mutual and exchange-traded funds	467,698,431	467,698,431	—
Alternative investments*:			
Absolute return	234,802,640	—	—
Hedged equity	231,339,909	—	—
Private equity	156,049,656	—	—
Real assets	22,349,394	—	—
Other	18,013,284	—	18,013,284
Pending purchases of alternative investments	51,215,463	—	—
Total	\$ 2,064,197,003	\$ 758,036,781	\$ 144,979,399

* 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. 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 \$11,227,118 and \$10,607,636 in 2016 and 2015, respectively, which is recorded within temporarily restricted dividend and interest income within the consolidated statements of activities. This represented approximately 99% of the income from partial benefit funds in 2016 and 2015. At December 31, 2016 and 2015, the fair value of partial benefit funds included in investments on the consolidated statements of financial position was \$224,411,419 and \$231,118,484, respectively.

7. 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:

	<u>2016</u>	<u>2015</u>
Donor contributions	\$ 26,217,991	\$ 62,684,841
Organizational funds	10,657,738	5,886,812
	<u>\$ 36,875,729</u>	<u>\$ 68,571,653</u>

Donor contributions include approximately \$955,250 and \$653,500 in 2016 and 2015, respectively, received from other foundations and not-for-profits to jointly fund certain grants.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

8. Grants and Distributions

The Board of Directors authorized grants of \$93,595,511 and \$95,019,320 in 2016 and 2015, respectively, and program-related investments of \$0 and \$2,650,000 in 2016 and 2015, respectively. In addition, distributions from organizational funds of \$46,315,862 and \$5,337,628 were made in 2016 and 2015, 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. Conditional grants, which are approved by the Board of Directors 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:

	<u>2016</u>	<u>2015</u>
Grants payable at beginning of year	\$ 27,812,798	\$ 27,031,211
Unconditional grants expensed	91,670,352	106,643,918
Payments made	(87,721,020)	(105,862,331)
Grants payable at end of year	<u>\$ 31,762,130</u>	<u>\$ 27,812,798</u>

Grants payable at December 31, 2016, are scheduled to be disbursed as follows: 2017 – \$25,362,079, 2018 – \$4,785,429, and 2019 and thereafter – \$1,614,622. At December 31, 2016 and 2015, total authorized conditional grants were \$6,975,981 and \$5,871,407, respectively.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

9. Affiliated Supporting Organizations

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

	December 31	
	2016	2015
The City of Cleveland's Cable Television		
Minority Arts and Education Fund	\$ 4,205,023	\$ 4,194,926
The Davis Fund	2,259,454	2,189,742
The Higley Fund	33,718,061	33,597,535
The Billie Howland Steffee Family Fund	6,196,166	6,005,831
Medical Mutual of Ohio Charitable Foundation	2,147,388	2,058,634
Sullivan Scholars Foundation	3,858,707	3,653,528
The Thatcher Family Fund	6,287,055	5,688,565
	\$ 58,671,854	\$ 57,388,761

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, 2016 and 2015, were \$16,435,149 and \$16,094,249, respectively.

10. Other Investments

Other investments of \$18,635,675 and \$17,930,801 in 2016 and 2015, 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 2017 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.

The Cleveland Foundation

Notes to Consolidated Financial Statements (continued)

11. Administrative Expenses

Administrative expenses include the following:

	<u>2016</u>	<u>2015</u>
Staff expense, including salaries, benefits, and other	\$ 9,916,779	\$ 9,189,985
Office expense, including rent, systems, and supplies	2,381,797	2,380,466
Other expense	1,801,301	1,697,039
	<u>\$ 14,099,877</u>	<u>\$ 13,267,490</u>

12. Operating Lease

The Foundation leases office space under a primary operating lease agreement, which expires in 2020. Rental expense was \$946,021 and \$929,113 in 2016 and 2015, respectively. Future minimum rental commitments under the non-cancelable primary operating lease at December 31, 2016, are \$912,000 in 2017, \$912,000 in 2018, \$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 \$678,572 and \$648,933 in 2016 and 2015, respectively. All contributions under the plan are fully vested at the time the contributions are made.

14. 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 August 7, 2017; 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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