



Cato Institute
Financial Statements
and Independent Auditor's Report
March 31, 2017 and 2016

Cato Institute

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Independent Auditor's Report

To the Board of Directors
Cato Institute
Washington, DC

We have audited the accompanying financial statements of Cato Institute ("Cato"), which comprise the statements of financial position as of March 31, 2017 and 2016, the related statements of activities and change in net assets and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits 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 financial position of Cato Institute as of March 31, 2017 and 2016, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.



Bethesda, Maryland
August 25, 2017

Cato Institute

**Statements of Financial Position
March 31, 2017 and 2016**

Assets

	2017	2016
Current assets		
Cash and cash equivalents	\$ 8,336,551	\$ 9,327,629
Investments, short-term	27,493,916	17,208,751
Pledges, bequests and accounts receivable, current portion, net	1,653,407	3,019,981
Inventory	258,707	213,818
Prepaid expenses, deposits and other current assets	699,428	282,276
Total current assets	38,442,009	30,052,455
Property and equipment, net	34,332,073	35,687,668
Pledges receivable, net of discount and current portion	1,989,460	1,711,028
Investments, long-term	3,769,040	3,702,164
Remainder interests	1,832	29,471
	\$ 78,534,414	\$ 71,182,786

Liabilities and Net Assets

Current liabilities		
Capital lease obligations, current portion	\$ 117,081	\$ 117,046
Accounts payable and accrued expenses	2,383,826	1,599,940
Grants payable	-	125,000
Deferred revenue	83,166	61,167
Annuities payable, current portion	20,954	20,954
Total current liabilities	2,605,027	1,924,107
Long-term liabilities		
Annuities payable, net of current portion	92,587	96,606
Capital lease obligations, net of current portion	122,199	187,382
Total liabilities	2,819,813	2,208,095
Net assets		
Unrestricted	65,617,999	58,184,230
Temporarily restricted	7,086,505	7,780,364
Permanently restricted	3,010,097	3,010,097
Total net assets	75,714,601	68,974,691
	\$ 78,534,414	\$ 71,182,786

See Notes to Financial Statements.

Cato Institute

**Statement of Activities and Change in Net Assets
Year Ended March 31, 2017**

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Public support and revenue				
Contributions	\$ 33,313,006	\$ 3,250,522	\$ -	\$ 36,563,528
Books and other publications	405,574	-	-	405,574
Conference fees	586,846	-	-	586,846
Change in split-interest agreements	(18,879)	-	-	(18,879)
Interest and dividends	300,826	74,397	-	375,223
Realized and unrealized gain on investments	7,284	8,723	-	16,007
Other income	276,904	-	-	276,904
Net assets released from restrictions - satisfaction of program restrictions	4,027,501	(4,027,501)	-	-
Total public support and revenue	<u>38,899,062</u>	<u>(693,859)</u>	<u>-</u>	<u>38,205,203</u>
Expenses				
Program services	24,720,811	-	-	24,720,811
Supporting services				
Management and general	2,237,241	-	-	2,237,241
Fundraising	4,507,241	-	-	4,507,241
Total expenses	<u>31,465,293</u>	<u>-</u>	<u>-</u>	<u>31,465,293</u>
Change in net assets	7,433,769	(693,859)	-	6,739,910
Net assets, beginning of year	<u>58,184,230</u>	<u>7,780,364</u>	<u>3,010,097</u>	<u>68,974,691</u>
Net assets, end of year	<u>\$ 65,617,999</u>	<u>\$ 7,086,505</u>	<u>\$ 3,010,097</u>	<u>\$ 75,714,601</u>

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**Statement of Activities and Change in Net Assets
Year Ended March 31, 2016**

	Unrestricted	Temporarily restricted	Permanently restricted	Total
Public support and revenue				
Contributions	\$ 24,385,866	\$ 3,030,640	\$ -	\$ 27,416,506
Books and other publications	369,790	-	-	369,790
Conference fees	704,032	-	-	704,032
Change in split-interest agreements	63,403	-	-	63,403
Interest and dividends	198,962	67,645	-	266,607
Realized and unrealized gain (loss) on investments	13,113	(34)	-	13,079
Other income	12,137	-	-	12,137
Net assets released from restrictions - satisfaction of program restrictions	3,869,023	(3,869,023)	-	-
Total public support and revenue	29,616,326	(770,772)	-	28,845,554
Expenses				
Program services	22,563,018	-	-	22,563,018
Supporting services				
Management and general	2,278,089	-	-	2,278,089
Fundraising	5,299,725	-	-	5,299,725
Total expenses	30,140,832	-	-	30,140,832
Change in net assets	(524,506)	(770,772)	-	(1,295,278)
Net assets, beginning of year	58,708,736	8,551,136	3,010,097	70,269,969
Net assets, end of year	\$ 58,184,230	\$ 7,780,364	\$ 3,010,097	\$ 68,974,691

See Notes to Financial Statements.

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**Statements of Cash Flows
Years Ended March 31, 2017 and 2016**

	2017	2016
Cash flows from operating activities		
Change in net assets	\$ 6,739,910	\$ (1,295,278)
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Loss on disposal of property and equipment	13,645	-
Depreciation and amortization	1,523,886	1,563,314
Realized and unrealized gain on investments, net	(16,007)	(13,079)
Loss on write-off of pledge receivable	-	7,774
Bad debt expense	-	27,904
Change in discount on pledges receivable	61,568	(73,815)
Annuities payable	16,935	(83,151)
Changes in		
Pledges, bequests and accounts receivable	826,574	2,956,513
Inventory	(44,889)	130,744
Prepaid expenses, deposits and other current assets	(417,152)	(158,430)
Remainder Interests	27,639	56,033
Accounts payable and accrued expenses	783,886	(297,945)
Grants payable	(125,000)	125,000
Deferred revenue	21,999	14,944
Other accrued expenses	-	(31,250)
	9,412,994	2,929,278
Net cash provided by operating activities		
Cash flows from investing activities		
Purchases of property and equipment	(97,912)	(257,736)
Proceeds from sales of investments	721,388	2,343,034
Purchases of investments	(11,057,422)	(17,751,629)
	(10,433,946)	(15,666,331)
Net cash used in investing activities		
Cash flows from financing activities		
Principal payments on capital lease obligations	(149,172)	(137,764)
Payments on annuities	(20,954)	(46,098)
Contributions restricted for long-term purposes - endowment	200,000	200,000
	29,874	16,138
Net cash provided by financing activities		
Net decrease in cash and cash equivalents	(991,078)	(12,720,915)
Cash and cash equivalents, beginning of year	9,327,629	22,048,544
Cash and cash equivalents, end of year	\$ 8,336,551	\$ 9,327,629
Supplemental cash flow information		
Interest paid	\$ (7,379)	\$ (10,974)
Noncash investing activities		
Equipment acquired under capital lease obligation	\$ 84,024	\$ -

See Notes to Financial Statements.

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Notes to Financial Statements March 31, 2017 and 2016

Note 1 - Organization

Cato Institute ("Cato") is a nonpartisan public policy research organization incorporated under the laws of the State of Kansas. During 2013, Cato underwent a change in the composition of its board and was reorganized from a stock-based corporation to a member organization, incorporated under the laws of the State of Kansas. The mission of Cato Institute is to originate, disseminate and increase understanding of public policies based on the principles of individual liberty, limited government, free markets and peace. Cato's vision is to create Societies that are civil, free, open and founded on libertarian principles.

Note 2 - Summary of significant accounting policies

Basis of accounting

The accompanying financial statements are presented on the accrual basis of accounting, and in accordance with FASB Accounting Standards Codification ("FASB ASC") Topic 958, *Not-for-Profit Entities*.

Cash and cash equivalents

Cash equivalents at March 31, 2017 and 2016 consist of short-term investments with original maturities of 90 days or less, except for funds held within the investment portfolios. Cato occasionally receives contributions of marketable securities. It is the policy of Cato to convert such securities to cash as soon as practical, always within 30 days. Consequently, all such securities are included in cash and cash equivalents and to the extent they are not donor restricted for long-term purposes they are classified as operating cash flows.

Pledges and accounts receivable

Cato records pledges and accounts receivable, which include bequests receivable, net of an allowance for doubtful accounts when necessary. The allowance is determined based on a review of the estimated collectibility of the specific accounts, plus a general provision based on historical loss experience and existing economic conditions. Uncollectible amounts are charged off against the allowance for doubtful accounts once management determines an account, or a portion thereof, to be worthless.

Unconditional promises to give that are expected to be collected within one year are recorded as current pledges receivable at their net realizable values in the period in which Cato is notified by the donor of his or her commitment to make a contribution. Unconditional promises to give that are expected to be collected in future years are reflected as long-term pledges in temporarily restricted net assets at the net present value of their estimated future cash flows using risk-adjusted interest rates (1 to 3 percent). Amortization of the discount on long-term pledges receivable are reflected as contribution revenue. Conditional promises to give are recognized when conditions on which they depend are substantially met.

Inventory

Inventory, which consists of published books totaling \$248,656 and \$207,512, and merchandise totaling \$10,051 and \$6,306, at March 31, 2017 and 2016, respectively, is stated at the lower of cost or estimated net realizable value on a first-in, first-out basis. Obsolete inventory is expensed and recorded to program expenses on the statements of activities and changes in net assets.

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Notes to Financial Statements March 31, 2017 and 2016

Property and equipment

Cato capitalizes all property and equipment with a cost of \$2,500 and an expected useful life of greater than one year. Property and equipment are recorded at historical cost and depreciated on the straight-line method over estimated useful lives as follows:

Building	25 - 40 years
Building improvements	5 - 25 years
Office furniture and equipment	3 - 10 years

Investments

Short-term investments consist of money market funds, and short-term investment-grade fixed income securities, and are held for operating purposes.

Long-term investments, which consist of charitable gift annuities and permanently restricted funds, are recorded at fair value. The investments, including the money market funds within the portfolio, are restricted and, therefore, are presented as long-term on the accompanying statements of financial position.

Remainder interests

Cato is the remainder beneficiary of trusts. Upon the death of the donor, remaining trust assets will be distributed to Cato. Remainder interests are classified as temporarily restricted assets and values are stated at the net present value of future benefits expected to be received, based upon the life expectancy of the donor, fair value of the trust assets and a discount rate of 6 percent.

Deferred revenue

Revenue received in advance for certain functions is recorded as deferred revenue. In addition, revenue received in advance for monthly subscriptions to various publications and recordings is recorded as deferred revenue based on the time period remaining on the subscription.

Net assets

Cato's net assets are classified into three categories: unrestricted, temporarily restricted and permanently restricted. All contributions are considered to be available for unrestricted use unless specifically restricted by the donor or by law.

Temporarily restricted net assets are contributions with temporary, donor-imposed time or purpose restrictions. Temporarily restricted net assets become unrestricted when the time restrictions expire or when the contributions are used for their restricted purposes, at which time they are reported in the statements of activities and change in net assets as net assets released from restrictions.

Permanently restricted net assets are contributions with donor-imposed restrictions that do not expire with the passage of time and cannot be removed or fulfilled by Cato's actions. However, income earned on permanently restricted net assets is used for temporarily restricted purposes, based upon the donors' specifications. Temporarily restricted endowment income is reclassified to unrestricted net assets upon appropriation for expenditure by the Board of Directors and satisfaction of timing or purpose restrictions, whichever occurs later.

Contributions

Contributions and pledges of cash and other assets are recorded at estimated fair value as unrestricted, temporarily restricted or permanently restricted support depending on the existence or absence of donor-imposed restrictions. Contributions and pledges reported as temporarily restricted

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Notes to Financial Statements March 31, 2017 and 2016

are reclassified to unrestricted upon expiration of the stipulated time restriction or accomplishment of the purpose restriction.

Donated securities are recorded at fair value as of the date of the contribution. Gains or losses on sale of donated securities converted to cash nearly immediately upon receipt are recorded as other income on the statements of activities and change in net assets since the donated securities are not investments but are considered cash flows from operating activities.

Donated property and equipment is recorded at fair value as of the date of contribution.

Donated services

Contributions of services are recognized in the financial statements as in-kind contributions if the services enhance or create non-financial assets or require specialized skills, are provided by individuals possessing those skills, and would typically be purchased if not provided by donation. These services are recorded at their estimated fair values at the date of donation and are recognized in the statements of activities and change in net assets as donated services expense with an offsetting credit to contributions revenue.

Allocations

The costs of supporting the various programs and other activities have been summarized on a functional basis in the statements of activities and change in net assets. Certain costs have been allocated among the program and supporting service categories based on various methods, including time spent.

Tax status

Cato has been granted tax-exempt status as a public charity within the meaning of Section 501(c)(3) of the Internal Revenue Code ("IRC"). Although Cato is generally exempt from income tax, Cato is subject to unrelated business income taxes under Section 512 of the IRC, as well as subject to excise tax on excess lobbying expenses. There was no unrelated business income or excess lobbying expenses for the years ended March 31, 2017 and 2016; therefore, no provision for income tax has been recorded in the financial statements. Cato believes it has appropriate support for any tax position taken and, as such, does not have any uncertain tax positions that are material to the financial statements. Cato recognizes interest expense and penalties related to income taxes on uncertain tax positions in management and general expenses on the statements of activities and change in net assets and accounts payable and accrued expenses in the statements of financial position. No interest expense and penalties related to income taxes on uncertain tax positions were recognized for the years ended March 31, 2017 and 2016. Tax years prior to 2013 are no longer subject to examination by the Internal Revenue Service or the tax jurisdictions of Kansas and the District of Columbia.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

Subsequent events

Cato has evaluated events and transactions for potential recognition or disclosure through August 25, 2017, the date the financial statements were available to be issued.

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**Notes to Financial Statements
March 31, 2017 and 2016**

Note 3 - Pledges, bequests and accounts receivable

Pledges, bequests and accounts receivable at March 31, 2017 and 2016 consist of the following:

	2017	2016
Accounts, contributions and other receivables	\$ 523,161	\$ 606,084
Bequests receivable	-	936,671
Pledges receivable	3,265,246	3,280,000
 Total pledges, bequests and accounts receivable	 3,788,407	 4,822,755
Less: Allowance for uncollectible pledges	-	(7,774)
Less: Discounts to net present value	(145,540)	(83,972)
 Net receivables	 3,642,867	 4,731,009
Less: Long-term pledges receivable due in one to five years	1,989,460	1,711,028
 Current pledges, bequests and accounts receivable	 \$ 1,653,407	 \$ 3,019,981

Note 4 - Property and equipment

Property and equipment at March 31, 2017 and 2016 and are summarized as follows:

	2017	2016
Land	\$ 9,656,037	\$ 9,656,037
Buildings and improvements	35,147,850	35,103,470
Audio visual systems	1,564,387	1,546,759
Office furniture and equipment	3,713,207	3,894,879
 Accumulated depreciation and amortization	 50,081,481 (15,749,408)	 50,201,145 (14,513,477)
 Property and equipment, net	 \$ 34,332,073	 \$ 35,687,668

Depreciation and amortization expense for the years ended March 31, 2017 and 2016 was \$1,523,886 and \$1,563,314, respectively.

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**Notes to Financial Statements
March 31, 2017 and 2016**

Note 5 - Investments

Investments are stated at fair value and consist of the following at March 31, 2017 and 2016:

	2017	2016
Short-term investments		
Money market funds	\$ 5,026,272	\$ 5,005,388
Mutual funds - fixed income	22,467,644	12,203,363
Investments, short-term	\$ 27,493,916	\$ 17,208,751
	2017	2016
Long-term investments		
Money market funds	\$ 5,165	\$ 24,494
Exchange-traded funds - equity	383,258	302,234
Exchange-traded funds - fixed income	90,744	131,964
Mutual funds - equity	297,029	464,447
Mutual funds - fixed income	2,992,844	2,779,025
Investments, long-term	\$ 3,769,040	\$ 3,702,164

Investments include endowments which had a fair value of \$3,029,956 and \$2,835,090 at March 31, 2017 and 2016, respectively.

Investment income for the years ended March 31, 2017 and 2016 is as follows:

	2017	2016
Interest and dividends - investments	\$ 367,438	\$ 255,628
Interest and dividends - cash and cash equivalents	7,785	10,979
	375,223	266,607
Realized and unrealized gain on investments, net	16,007	13,079
	\$ 391,230	\$ 279,686

Note 6 - Annuities payable

As part of a planned giving program, Cato has a charitable gift annuity arrangement in which donors contribute assets to Cato in exchange for a promise by Cato to pay a fixed amount for a specified period of time to the donor, individuals or organizations designated by the donor. The assets received by Cato are held in a separate investment account, with a fair value of \$367,713 and \$543,790 at March 31, 2017 and 2016, respectively. The annuity liability is a general obligation of Cato. The unrestricted net assets of Cato are available for payment of annuity liabilities.

Contributions received under the charitable gift annuity arrangement are recognized as unrestricted revenue in the year the annuity contract is executed. Assets received are recorded at fair value when received, and the annuity payment liability is recognized at the present value of estimated

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**Notes to Financial Statements
March 31, 2017 and 2016**

future payments to the annuitant. Contribution revenue is recognized as the difference between the fair value of the assets received and the annuity payment liability.

Annuities are based on interest rates ranging from 5.8 percent to 11.0 percent, and the payment term is the annuitant's life expectancy. The adjustments to the annuity liability relating to the decrease in liability due to a deceased annuitant and the passage of time and other factors have been recorded as change in split-interest agreements income in the accompanying statements of activities and change in net assets. Following is a summary of the changes in the annuities payable for the years ended March 31, 2017 and 2016:

	2017	2016
Beginning balance	\$ 117,560	\$ 246,809
Payments made to annuitants	(20,954)	(46,098)
Decrease in liability due to deceased annuitant	-	(122,802)
Adjustments to liability relating to passage of time and other factors	16,935	39,651
	113,541	117,560
Less: Current portion	20,954	20,954
	\$ 92,587	\$ 96,606

Note 7 - Line of credit

Cato has a \$5,000,000 unsecured guidance line of credit with a bank. The line of credit is subject to an annual renewal by the bank with interest due monthly at the LIBOR rate plus 1 percent and outstanding principal due at maturity. The line of credit matures on February 28, 2018. There was no amount outstanding on the line of credit at March 31, 2017 and 2016.

Note 8 - Capital leases

Cato leases certain equipment under capital leases that expire at various dates through 2020. The future minimum lease payments under capital leases in each of the years subsequent to March 31, 2017 are as follows:

	2018	\$ 113,564
	2019	112,410
	2020	21,154
	2021	484
		247,612
Minimum lease payments		247,612
Less amounts representing interest		8,332
		239,280
Present value of net minimum lease payments		239,280
Less current portion		117,081
		\$ 122,199
Long-term portion		\$ 122,199

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**Notes to Financial Statements
March 31, 2017 and 2016**

Capitalized leased equipment of \$546,714 and \$726,459 is included with property and equipment at March 31, 2017 and 2016, with accumulated depreciation of \$316,124 and \$430,301, respectively. Interest expense incurred totaled \$7,379 and \$10,974 at March 31, 2017 and 2016, respectively.

Note 9 - Temporarily restricted net assets

Temporarily restricted net assets consist of the unexpended portion of restricted contributions received by Cato. Contributions restricted for the following programs at March 31, 2017 and 2016 is as follows:

	2017	2016
Academic Research and Programs	\$ 96,456	\$ 325,603
Center for Constitutional Studies	1,493,469	-
Center for Educational Freedom	94,752	66,731
Center for Global Liberty and Prosperity	151,327	241,870
Center for Monetary and Financial Alternatives	3,426,637	4,393,437
Center for Representative Government	41,500	30,000
Center for the Study of Science	125,000	-
Defense and Foreign Policy Studies	46,184	46,184
Documentary Series - School, Inc.	-	75,000
Economic Studies	145,346	-
Friedman Prize	397,466	693,557
Herbert A. Stiefel Center for Trade Policy Studies	375,898	693,328
Information Policy Studies	-	133,279
Liberating the Future Capital Campaign	-	200,000
Remainder interests	1,832	29,471
Student programs	80,090	86,182
Time restricted	610,548	765,722
	\$ 7,086,505	\$ 7,780,364

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**Notes to Financial Statements
March 31, 2017 and 2016**

Net assets were released from donor restrictions when expenses satisfying the restricted purposes were incurred or by occurrence of other events specified by the donor for the years ended March 31, 2017 and 2016 is as follows:

	2017	2016
Academic Research and Programs	\$ 259,147	\$ 424,714
Center for Constitutional Studies	129,033	163,538
Center for Educational Freedom	161,979	73,369
Center for Global Liberty and Prosperity	365,543	147,014
Center for Monetary and Financial Alternatives	1,365,938	1,327,729
Center for Representative Government	-	8,000
Center for the Study of Science	100,200	100,000
Conference and Events	44,550	60,344
Criminal Justice Project	10,000	37,500
Defense and Foreign Policy Studies	-	64,747
Documentary Series - School, Inc.	-	214,734
Economic Studies	51,504	-
Fiscal Policy Studies	25,000	25,000
Friedman Prize	422,916	56,731
Health and Welfare Studies	-	187,000
Herbert A. Stiefel Center for Trade Policy Studies	352,430	246,091
Information Policy Studies	133,279	41,721
Liberating the Future Capital Campaign	200,000	205,221
Remainder Interests	27,639	56,033
Student programs	184,169	251,839
Time Restricted	194,174	177,698
	\$ 4,027,501	\$ 3,869,023

Note 10 - Permanently restricted net assets

Permanently restricted net assets consist of the B. Kenneth Simon Endowment, and the Richard C. and Deborah L. Young Endowment. Use of the assets by Cato is limited by donor-imposed restrictions that neither expire by the passage of time nor can be fulfilled or otherwise removed by actions of Cato. The income earned from the B. Kenneth Simon Endowment must be used for Constitutional Studies. Through December 2016, the Richard C. and Deborah L. Young Endowment must have been used for student programs, and starting January 2017 the funds must be used for Cato's foreign policy and national policy group. The earnings are considered temporarily restricted until expenses have been incurred, thus releasing the income from restriction.

Permanently restricted net assets - interpretation of relevant law

The Board of Directors has interpreted the State Prudent Management of Institutional Funds Act ("SPMIFA"), which became effective in Kansas in July 2008, as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, Cato classifies as permanently restricted net assets (a) the original value of gifts to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment

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fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Cato in a manner consistent with the standard prudence prescribed by SPMIFA. In accordance with SPMIFA, Cato considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- (1) The duration and preservation of the funds
- (2) The purposes of Cato and the donor-restricted endowment funds
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The expected total return from income and the appreciation of investments
- (6) Other resources of Cato
- (7) The investment policies of Cato

Permanently restricted net assets - return objectives and risk parameters

Cato has adopted a conservative investment and spending policy for endowment assets that attempts to provide a predictable stream of funding to programs supported by its endowments. The investment objectives of managing endowment assets are the preservation of capital, liquidity, and to optimize the investment return within the constraints of the previously mentioned objectives. Endowment assets include those assets of donor-restricted funds that Cato must hold in perpetuity or for a donor-specified period.

Permanently restricted net assets - strategies employed for achieving objectives

To satisfy its long-term rate-of-return objectives, Cato relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends).

Spending policy and how the investment objectives relate to spending policy

Cato has a policy of appropriating for expenditure each year the earnings of the endowments. For the B. Kenneth Simon Endowment, spending is not to exceed 7 percent of the endowment's total asset value. In establishing this policy, Cato considered the long-term expected return on its endowment net assets and operating costs of the Constitutional Studies program. For the Richard C. and Deborah L. Young Endowment, spending per quarter is not to exceed \$10,000, or 1 percent of the endowment's total asset value, whichever is higher.

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Notes to Financial Statements March 31, 2017 and 2016

The changes in the donor-restricted endowment net assets for the years ended March 31, 2017 and 2016 are as follows:

	Unrestricted	Temporarily restricted	Permanently restricted
Endowment net assets, April 1, 2015	\$ -	\$ 5,821	\$ 3,010,097
Dividend income	-	67,645	-
Realized and unrealized gain, net	-	(34)	-
Total investment return	-	73,432	3,010,097
Appropriation based on spending policy	-	(62,619)	-
Endowment net assets, March 31, 2016	-	10,813	3,010,097
Dividend income	-	74,397	-
Realized and unrealized loss, net	-	8,722	-
Total investment return	-	93,932	3,010,097
Appropriation based on spending policy	-	(74,073)	-
Endowment net assets, March 31, 2017	<u>\$ -</u>	<u>\$ 19,859</u>	<u>\$ 3,010,097</u>

Note 11 - Employee benefit plans

Cato maintained a 403(b) plan (defined-contribution plan) that allows employees to defer a portion of their wages. Employees are eligible for the 403(b) plan upon hiring. Cato does not match employee contributions. The 403(b) plan was terminated effective December 31, 2016.

In addition, Cato maintains a 401(k) plan that allows employees to defer a portion of their wages. Cato matches 25 percent of each employee's contributions, up to 8 percent of participants' compensation. The plan provides for an annual discretionary contribution by Cato. Cato will make a safe-harbor non-elective contribution each year to each employee's account equal to 3 percent of the participant's compensation. Total match and discretionary contributions amounted to \$713,157 and \$640,789, respectively, for the years ended March 31, 2017 and 2016, respectively.

Cato maintains a self-insurance program for its employees' health care costs. Cato is liable for losses on claims up to \$40,000 per claim for 2017 and 2016. Cato has third-party insurance coverage for any losses in excess of such amounts. Self-insurance costs are accrued based on claims reported as of March 31, 2017 and 2016, as well as an estimated liability for claims incurred but not reported. The total accrued liability for self-insurance costs was \$(104,501) and \$(46,379) at March 31, 2017 and 2016, respectively, and is reported as accounts payable and accrued expenses in the statements of financial position.

Note 12 - Commitments

Cato has contracts through 2019 for hotels for future conferences. In the event of cancellation, Cato may be required to pay various costs as stipulated in the contracts, the amounts of which are dependent upon the respective dates of cancellation. Due to the numerous variables involved, Cato's ultimate liability under these contracts cannot be determined; however, the estimated costs

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Notes to Financial Statements March 31, 2017 and 2016

as of March 31, 2017 range from approximately \$0 to \$180,000 depending on the nature, timing, and number of conference cancellations. As of August 25, 2017, Cato had not canceled and had no intentions to cancel any future conferences.

Cato is obligated under an agreement to provide payments to its former president each year through December 2016 at the dates specified in the agreements provided the terms of the specific agreements are met. Cato has recognized an expense and liability at March 31, 2017 and 2016 for the proportionate share of the total obligation that will be accrued and paid over the term of the agreement. Another agreement to provide services over a five-year period ending in December 2017 is being expensed and paid as incurred and no liability is recorded at March 31, 2017 or 2016.

Note 13 - Joint activities

Cato has incurred and allocated joint costs of fundraising in disseminating information to the general public and supporters in three direct mailings during the year ended March 31, 2017 and four direct mailings during the year ended March 31, 2016. Total costs allocated were \$674,264 in 2017 and \$786,569 in 2016. Of the total costs allocated, \$519,935 in 2017 and \$627,540 in 2016 were recorded in program services, and \$154,329 in 2017 and \$159,029 in 2016 were recorded in fundraising expenses in the statements of activities and change in net assets.

Note 14 - Concentration of credit risk

Cato maintained balances at banks in excess of Federal Deposit Insurance Corporation ("FDIC") coverage. The amount of uninsured deposits at March 31, 2017 amounted to approximately \$8,456,000.

Note 15 - Donated services

For the years ended March 31, 2017 and 2016, Cato received benefit from donated advertising services of approximately \$483,000 and \$481,000, respectively. Additionally, for the years ended March 31, 2017 and 2016, Cato received other in-kind donations of approximately \$573,000 and \$237,000, respectively. The value of these in-kind donations has been reflected on the accompanying statements of activities and change in net assets as contributions revenue and program expenses.

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**Notes to Financial Statements
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Note 16 - Fair value measurements

Cato has determined the fair value of certain assets through application of FASB ASC Topic 820, *Fair Value Measurement*. Fair values of assets measured on a recurring basis at March 31, 2017 and 2016 are as follows:

	Fair value	Fair value measurements at reporting date using		
		Quoted prices in active markets for identical assets/liabilities (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
<u>March 31, 2017</u>				
Assets				
Money Market Funds	\$ 5,031,437	\$ 5,031,437	\$ -	\$ -
Exchange-Traded Funds - equity	383,258	383,258	-	-
Exchange-Traded Funds - fixed income	90,744	90,744	-	-
Mutual Funds - equity	25,460,489	25,460,489	-	-
Mutual Funds - fixed income	297,028	297,028	-	-
Total investments	<u>\$ 31,262,956</u>	<u>\$ 31,262,956</u>	<u>\$ -</u>	<u>\$ -</u>
<u>March 31, 2016</u>				
Assets				
Money Market Funds	\$ 5,029,882	\$ 5,029,882	\$ -	\$ -
Exchange-Traded Funds - equity	302,234	302,234	-	-
Exchange-Traded Funds - fixed income	131,964	131,964	-	-
Mutual Funds - equity	464,447	464,447	-	-
Mutual Funds - fixed income	14,982,388	14,982,388	-	-
Total investments	<u>\$ 20,910,915</u>	<u>\$ 20,910,915</u>	<u>\$ -</u>	<u>\$ -</u>

This FASB ASC topic establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. This hierarchy consists of three broad levels: Level 1 inputs consist of unadjusted quoted prices in active markets for identical assets and provide highest quality inputs. Level 2 inputs are based primarily on quoted prices for identical assets in inactive markets or similar assets in active or inactive markets or other significant observable inputs. Level 3 inputs provide the lowest quality inputs because there are no significant observable inputs. Cato uses appropriate valuation techniques based on the available inputs to measure the fair value of its investments. When available, Cato measures fair value using Level 1 inputs because they generally provide the most reliable evidence of fair value. There have been no changes in the valuation methodologies during the current year. Money market funds reported as Level 1 inputs have been valued at the closing price reported by the fund sponsor from an actively traded exchange. Exchange-traded funds have been valued at the closing price reported on the active market in which the individual securities are traded. Mutual funds have been valued at the reported net asset value of the fund, which is the price at which additional shares can be obtained.

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