

Slover Library Foundation
Consolidated Financial Statements
June 30, 2016

CAVANAUGH NELSON PLC

CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

Independent Auditor's Report

Members of the Board of Directors
Slover Library Foundation
Norfolk, Virginia

We have audited the accompanying consolidated statement of net assets – modified cash basis of the Slover Library Foundation (the Foundation) and its subsidiary as of June 30, 2016 and 2015, and the related consolidated statements of activities and changes in net assets – modified cash basis, and of cash flows - modified cash basis for each of the three years in the period ended June 30, 2016, 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 consolidated financial statements in accordance with the modified cash basis of accounting as described in Note 1; this includes determining that the modified cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Slover Library Foundation and its subsidiary as of June 30, 2016 and 2015 and their activities and changes in net assets and cash flows for each of the three years in the period ended June 30, 2016 in conformity with the modified cash basis of accounting described below.

Basis of Accounting

As discussed in Note 1 of the consolidated financial statements, which describes the basis of accounting, the consolidated financial statements are prepared on the modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

A handwritten signature in black ink that reads "Carmay Nelson PLC". The signature is written in a cursive, flowing style.

January 10, 2017

SLOVER LIBRARY FOUNDATION
CONSOLIDATED STATEMENT OF NET ASSETS
MODIFIED CASH BASIS

	As of June 30,	
	2016	2015
Assets		
Investments, at fair value:		
Cash and cash equivalents	\$ 747,871	\$ 923,085
Equity and equity type funds	4,465,697	4,607,806
Bonds and bond type funds	1,910,430	1,245,611
Accrued income	6,307	1,727
Other investment, at cost	42,671	28,614
Total investments	7,172,976	6,806,843
Cash	188,738	320,154
Pledges receivable	716,374	989,959
Total assets	\$ 8,078,088	\$ 8,116,956
 Liabilities and net assets		
Deferred pledge revenue	\$ 716,374	\$ 989,959
 Net assets:		
Slover Library Foundation	7,328,268	7,093,551
Non-controlling interest in consolidated subsidiary	33,446	33,446
Total net assets	7,361,714	7,126,997
Total liabilities and net assets	\$ 8,078,088	\$ 8,116,956

The notes to the financial statements are an
integral part of this statement.

SLOVER LIBRARY FOUNDATION
CONSOLIDATED STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS
MODIFIED CASH BASIS

	Years ended June 30,		
	2016	2015	2014
Revenue and support:			
Contributions received from donors	\$ 808,473	\$ 1,457,287	\$ 1,278,432
Rent revenue	52,000	-	-
Contribution related to tax credits	-	3,378,461	-
Investment income (loss), net	(45,407)	(136,318)	31,086
Total revenue and support	<u>815,066</u>	<u>4,699,430</u>	<u>1,309,518</u>
Expenses:			
Program services:			
Support for the Slover Memorial Library	<u>319,363</u>	<u>613,078</u>	<u>18,167,861</u>
Supporting services:			
Fundraising:			
Consultant fees	3,300	74,372	77,500
Campaign materials	-	-	3,784
Payroll expenses	199,927	192,721	-
Accounting and consulting fees	42,544	83,328	43,244
Insurance	6,722	6,954	-
Stationery and office supplies	1,568	2,732	5,478
Other expenses	6,925	3,551	1,730
Total supporting services	<u>260,986</u>	<u>363,658</u>	<u>131,736</u>
Total expenses	<u>580,349</u>	<u>976,736</u>	<u>18,299,597</u>
Change in net assets	234,717	3,722,694	(16,990,079)
Net assets at beginning of year	7,126,997	3,404,303	20,369,382
Capital contribution	<u>-</u>	<u>-</u>	<u>25,000</u>
Net assets at end of year	<u><u>\$ 7,361,714</u></u>	<u><u>\$ 7,126,997</u></u>	<u><u>\$ 3,404,303</u></u>

The notes to the financial statements are an
integral part of this statement.

SLOVER LIBRARY FOUNDATION
CONSOLIDATED STATEMENT OF CASH FLOWS
MODIFIED CASH BASIS

	Years ended June 30,		
	2016	2015	2014
Cash flows from operating activities			
Change in net assets	\$ 234,717	\$ 3,722,694	\$ (16,990,079)
Adjustments to reconcile change in net assets to net cash provided by (used for) operating activities:			
Net losses on investments	205,422	156,320	89,529
Change in accrued income	(4,580)	13,309	101,931
Net cash provided by (used for) operating activities	<u>435,559</u>	<u>3,892,323</u>	<u>(16,798,619)</u>
Cash flows from investing activities			
Sales of investments	133,890	1,062,105	16,391,552
Purchases of investments	(876,079)	(6,001,899)	(1,256,596)
Net cash provided by (used for) investing activities	<u>(742,189)</u>	<u>(4,939,794)</u>	<u>15,134,956</u>
Cash flows from financing activities			
Proceeds from capital contribution to consolidated subsidiary	-	-	25,000
Net cash provided by financing activities	<u>-</u>	<u>-</u>	<u>25,000</u>
Net increase (decrease) in cash	(306,630)	(1,047,471)	(1,638,663)
Cash and cash equivalents, beginning of year	<u>1,243,239</u>	<u>2,290,710</u>	<u>3,929,373</u>
Cash and cash equivalents, end of year	<u><u>\$ 936,609</u></u>	<u><u>\$ 1,243,239</u></u>	<u><u>\$ 2,290,710</u></u>
 Cash and cash equivalents are classified as follows:			
Investments - cash and cash equivalents	\$ 747,871	\$ 923,085	\$ 1,301,944
Cash	<u>188,738</u>	<u>320,154</u>	<u>988,766</u>
	<u><u>\$ 936,609</u></u>	<u><u>\$ 1,243,239</u></u>	<u><u>\$ 2,290,710</u></u>

The notes to the financial statements are an integral part of this statement.

SLOVER LIBRARY FOUNDATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
MODIFIED CASH BASIS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Organization

The Slover Library Foundation (the Foundation) was incorporated on November 3, 2008 to administer the funds raised for the construction of the Colonel Samuel L. Slover Library (the Library) by the City of Norfolk, Virginia (the City) and post construction to administer a technical support fund for the Library. The Foundation is a not-for-profit, charitable organization as defined under Section 501(c)(3) of the Internal Revenue Code (IRC) and has been granted exemption from federal income taxes by the Internal Revenue Service (IRS).

Presentation

The consolidated financial statements include the accounts of Slover Tenant, LLC (Slover Tenant), the Foundation's 99.75% owned subsidiary (together, referred to as the Foundation). Slover Tenant was established to support and further the charitable, educational and literary purpose of the Foundation. All intercompany transactions between the Foundation and Slover Tenant have been eliminated during consolidation.

The Foundation's accounts are maintained, and the financial statements are presented, on the modified cash basis of accounting, modified from the cash basis of accounting to record investments in accordance with accounting principles generally accepted in the United States (GAAP). Consequently, the financial statements are not intended to present financial position and results of operations in conformity with GAAP. The major differences between the modified cash basis of accounting used by the Foundation and U.S. generally accepted accounting principles are that contribution income is recognized when received rather than upon receipt of the related pledge, capital expenditures are expensed when paid and operating expenses and contributions are recognized when paid rather than when the related obligations are incurred.

With the exception of the above, the Foundation prepares its financial statements using not for profit guidelines established by GAAP. GAAP affects the manner by which the Foundation accounts for certain contributions and requires the Foundation to present in its financial statements certain basic information that focuses on the entity as a whole rather than on individual funds. GAAP also requires a financial statement presentation based on net assets classified by the existence or absence of externally imposed restrictions. None of the net assets of the Foundation are considered restricted net assets.

Cash and Cash Equivalents

The Foundation considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents.

Investments

The Foundation presents investments in cash equivalents, equity instruments and bonds at fair value based upon quoted market prices, when available. Realized and unrealized gains and losses on investments are included net in the statement of activities.

Use of Estimates

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

Risks and Uncertainties

The Foundation's investments are exposed to various risks, such as interest, market and credit risks. Due to the level of risk associated with certain investments, it is reasonably possible that changes in the values of investments will occur in the near term and that such changes could materially affect the amounts reported in the accompanying statements of financial position.

Subsequent Events

The Foundation evaluated subsequent events through January 10, 2017 the date the financial statements were available to be issued, for purposes of determining whether such events required recordation or disclosure in the accompanying financial statements.

Income Taxes

While the Foundation is exempt from federal and state income taxes, the Foundation's subsidiary is a taxable entity whose activities, if deemed unrelated to the Foundation's exempt purpose, could subject the Foundation to taxes on unrelated business income.

The Foundation's tax returns are generally subject to examination by authorities for a period of three years from the date they are filed and, consequently, the Foundation's tax return filed for the year ended June 30, 2013 remains subject to examination. In September 2015 the IRS approved the Foundation's request to be classified as a public charity, retroactive to its year ended June 30, 2014 and deemed the Foundation a supporting organization of the City. Accordingly, the Foundation is not required to file annual tax returns for the years ended June 30, 2014, 2015 and 2016. Due to an amendment of its bylaws effective June 30, 2016 the Foundation is no longer considered a supporting organization of the City and will be required to file an annual tax return beginning with its year ending June 30, 2017.

Reclassification

Certain prior year footnote balances have been reclassified to conform to the current year's presentation. Such reclassifications had no impact on previously reported net assets or change in net assets.

NOTE 2 - INVESTMENTS AND CASH EQUIVALENTS

Investment income

Investment income for the years ended June 30, consists of the following:

	Years ended June 30,		
	2016	2015	2014
Interest and dividends	\$ 177,759	\$ 25,360	\$ 141,868
Net losses on investments	(205,422)	(156,320)	(89,529)
Management fees	<u>(17,744)</u>	<u>(5,358)</u>	<u>(21,253)</u>
Total investment income (loss)	<u>\$ (45,407)</u>	<u>\$ (136,318)</u>	<u>\$ 31,086</u>

Investments

Investments consist of the following at June 30:

	2016	2015
Investments carried at fair value:		
Cash and cash equivalents:		
Schwab Municipal Money Fund	\$ 745,294	\$ 920,954
Cash	<u>2,577</u>	<u>2,131</u>
Total cash and cash equivalents	<u>747,871</u>	<u>923,085</u>
Equity funds:		
Kayne Anderson MLP Investment Co.	231,525	233,244
Morgan Stanley Institutional Fund, Inc. Global Franchise Portfolio Class I	539,177	521,056
Schwab Total Stock Market Index Fund	979,052	986,122
Vanguard Dividend Growth Fund Investor Shares	538,480	514,558
Vanguard Total World Stock Index Investor Shares	611,728	647,955
Vanguard Emerging Markets Stock Index Fund	<u>321,650</u>	<u>373,234</u>
Total equity mutual and index funds	3,221,612	3,276,169
Alternative investments - SFM Global Strategies, L.P.	<u>1,244,085</u>	<u>1,331,637</u>
Total equity and equity type funds	<u>4,465,697</u>	<u>4,607,806</u>
Bond and bond type funds:		
Doubleline Total Return Bond Fund Class I	397,766	395,583
Metropolitan West Total Return Bond Fund Class I	<u>472,530</u>	<u>464,791</u>
Total bond funds	870,296	860,374
Corporate bonds – Anheuser-Busch InBev Finance	80,156	-
Municipal bonds – other	<u>959,978</u>	<u>385,237</u>
Total bonds and bond type funds	<u>1,910,430</u>	<u>1,245,611</u>
Accrued interest on bonds	<u>6,307</u>	<u>1,727</u>
Total investments at fair value	7,130,305	6,778,229
Other investment, at cost	<u>42,671</u>	<u>28,614</u>
Total investments	<u>\$ 7,172,976</u>	<u>\$ 6,806,843</u>

Individual investment positions that exceed 5% of total investments have been identified above.

Fair values

GAAP defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. GAAP also establishes a three level fair value hierarchy and describes the inputs that are used to measure assets and liabilities as follows:

Level I: The asset and liability fair values are based on quoted prices in active markets for identical assets or liabilities.

Level II: The asset and liability fair values are based on observable inputs that include quoted market prices for similar assets or liabilities; quoted market prices that are not in an active market; or other inputs that are observable and can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level II assets include debt securities with quoted prices that are traded less frequently than exchange traded instruments.

Level III: The asset and liability fair values are based on unobservable inputs that are supported by little or no market activity. Level III assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation.

The following table presents the Foundation's assets that are measured at fair value on a recurring basis for each hierarchy level at June 30:

Investments at fair value:	Level I	Level II	Level III	Total
June 30, 2016				
Cash and cash equivalents	\$ 747,871	\$ -	\$ -	\$ 747,871
Equity funds	3,221,612	-	-	3,221,612
Alternative investments	-	-	1,244,085	1,244,085
Municipal and corporate bonds	-	1,040,134	-	1,040,134
Bond funds	870,296	-	-	870,296
Accrued income	-	6,307	-	6,307
	<u>\$ 4,839,779</u>	<u>\$ 1,046,441</u>	<u>\$ 1,244,085</u>	<u>\$ 7,130,305</u>
June 30, 2015				
Cash and cash equivalents	\$ 923,085	\$ -	\$ -	\$ 923,085
Equity funds	3,276,169	-	-	3,276,169
Alternative investments	-	-	1,331,637	1,331,637
Municipal and corporate bonds	-	385,237	-	385,237
Bond funds	860,374	-	-	860,374
Accrued income	-	1,727	-	1,727
	<u>\$ 5,059,628</u>	<u>\$ 386,964</u>	<u>\$ 1,331,637</u>	<u>\$ 6,778,229</u>

The following table presents a reconciliation of investment securities in which significant unobservable inputs (Level III) were used to determine fair value for the year ended June 30:

	2016	2015
Balance, beginning of year	\$ 1,331,637	\$ -
Purchases	-	1,340,000
Realized gains, net	<u>(87,552)</u>	<u>(8,363)</u>
Balance, end of year	<u>\$ 1,224,085</u>	<u>\$ 1,331,637</u>

During the year, the Foundation purchased an investment consisting of limited partnership investments that employ hedging and other non-traditional investment techniques, classified as Level 3 investments.

NOTE 3 – PLEDGES RECEIVABLE

Pledges receivable and the related deferred pledge revenues consist of the outstanding balances on pledges received through June 30 related to the Batten Challenge. Under the modified cash basis of accounting followed by the Foundation the related contributions are only recognized as income when received. Accordingly, the pledges receivable have no impact on the Foundation's net assets or changes in net assets.

NOTE 4 – REHABILITATION TAX CREDITS AND COMMITMENTS

During the year ended June 30, 2015, Slover Tenant was awarded Virginia Historic Rehabilitation Tax Credits which were subsequently allocated to its non-controlling interest for \$3,378,461 in contributions. Preceding the award of the tax credits, certain operating arrangements were made between the Foundation, the City and Slover Tenant, including lease and sublease agreements under which the Foundation leased and subsequently subleased the City's Seaboard Historic Building (formerly known as Old Norfolk City Hall) (the Building), as defined in the lease, for a period of six years. The lease and sublease agreements primarily limit the use of the Building to house and operate a central library facility for the City. The lease and sublease transactions do not have a material impact on the Foundation's operations.

In addition to the above, the Foundation and its subsidiary entered into a guaranty agreement with Slover Tenant's non-controlling member whereby the Foundation guaranteed certain operational aspects and Building commitments specified in the Foundation's aforementioned lease with the City, and in Slover Tenant's Operating Agreement as amended. The remaining aspects of the guaranty agreement will not have a material impact on the Foundation or its operations.