

**Baylor Alumni Association  
and Subsidiary**  
Consolidated Financial Statements  
May 31, 2014 and 2013  
(With Independent Auditor's Report Thereon)



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## INDEPENDENT AUDITOR'S REPORT

The Board of Directors  
Baylor Alumni Association and Subsidiary:

We have audited the accompanying consolidated financial statements of Baylor Alumni Association and Subsidiary (the Association), which comprise the consolidated statements of financial position as of May 31, 2014 and 2013, and the related consolidated statements of activities, functional expenses, 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 consolidated 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 consolidated 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 audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 Baylor Alumni Association and Subsidiary as of May 31, 2014 and 2013, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

***Uncertainties Regarding the Future Outcome of Litigation***

As discussed in Note 11 to the consolidated financial statements, on September 7, 2013 the Association membership voted to not adopt a Transition Agreement with Baylor University, which would have significantly impacted the operation of the Association and ultimately result in the dissolution of the Association. As a result of not approving the Transition Agreement, Baylor University has unilaterally terminated certain contract and license agreements, as well as prohibited the Association from referencing the Baylor name. These actions have resulted in lawsuits being filed by both parties against each other, with the outcome and ultimate impact on the operations of the Association uncertain at this time. The Association continues to work with Baylor University to determine the ultimate role the Association will serve in supporting Baylor University. Our opinion is not modified with respect to that matter.

November 30, 2014

**Baylor Alumni Association  
and Subsidiary**

Consolidated Statements of Financial Position

May 31, 2014 and 2013

	2014	2013
<b>Assets</b>		
Cash	\$ 91,245	287,821
Accounts receivable	2,031	18,616
Due from Baylor University	27,425	698
Contribution receivable	290,000	290,000
Prepaid expenses	5,852	11,325
Cash restricted/designated for endowments	181,198	464,228
Investment	5,466,497	4,894,475
Restricted agency funds received for the benefit of others	42,135	41,786
Beneficial interest in trust	855,000	720,000
Land	9,296	9,296
Equipment	343,871	343,322
Works of art and other historical treasures	160,273	160,273
Less accumulated depreciation	<u>(326,496)</u>	<u>(314,704)</u>
Total assets	<u>\$ 7,148,327</u>	<u>6,927,136</u>
<b>Liabilities and Net Assets</b>		
Liabilities:		
Accounts payable	\$ 48,959	29,957
Accrued expenses	8,957	52,391
Agency funds received for benefit of others	42,135	41,786
Total liabilities	<u>100,051</u>	<u>124,134</u>
Net assets:		
Unrestricted:		
Designated for endowment	3,563,236	3,252,996
Undesignated	828,111	832,125
	<u>4,391,347</u>	<u>4,085,121</u>
Temporarily restricted	-	60,952
Permanently restricted	<u>2,656,929</u>	<u>2,656,929</u>
Total net assets	<u>7,048,276</u>	<u>6,803,002</u>
Total liabilities and net assets	<u>\$ 7,148,327</u>	<u>6,927,136</u>

See accompanying notes to consolidated financial statements.

**Baylor Alumni Association  
and Subsidiary**

Consolidated Statement of Activities

Year Ended May 31, 2014

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
<b>Revenues:</b>				
Annual membership dues	\$ 23,591	-	-	23,591
Life membership dues	19,756	-	-	19,756
Sustaining membership gifts	29,425	-	-	29,425
Other contributions	36,433	25	-	36,458
Endowment earnings used in operations	416,588	-	-	416,588
Commissions on ring sales	27,525	-	-	27,525
Baylor Line advertising and underwriting	50,100	-	-	50,100
Royalties	99,820	-	-	99,820
Lifelong learning	64,288	-	-	64,288
Other events	1,254	-	-	1,254
Miscellaneous revenues	33,921	-	-	33,921
Net assets released from restriction	<u>60,977</u>	<u>(60,977)</u>	<u>-</u>	<u>-</u>
Total revenues	<u>863,678</u>	<u>(60,952)</u>	<u>-</u>	<u>802,726</u>
<b>Expenses:</b>				
Program:				
Membership services	556,461	-	-	556,461
Management and general	329,839	-	-	329,839
Fund-raising	<u>121,304</u>	<u>-</u>	<u>-</u>	<u>121,304</u>
Total expenses	<u>1,007,604</u>	<u>-</u>	<u>-</u>	<u>1,007,604</u>
Change in net assets before other changes	<u>(143,926)</u>	<u>(60,952)</u>	<u>-</u>	<u>(204,878)</u>
<b>Other changes:</b>				
Gains and earnings on investments, net of transfers for operations	290,484	-	-	290,484
Contribution of beneficial interest in trust	159,829	-	-	159,829
Loss on disposal of property	<u>(161)</u>	<u>-</u>	<u>-</u>	<u>(161)</u>
Total other changes	<u>450,152</u>	<u>-</u>	<u>-</u>	<u>450,152</u>
Change in net assets	306,226	(60,952)	-	245,274
Net assets at beginning of year	<u>4,085,121</u>	<u>60,952</u>	<u>2,656,929</u>	<u>6,803,002</u>
Net assets at end of year	<u>\$ 4,391,347</u>	<u>-</u>	<u>2,656,929</u>	<u>7,048,276</u>

See accompanying notes to consolidated financial statements.

**Baylor Alumni Association  
and Subsidiary**

Consolidated Statement of Activities

Year Ended May 31, 2013

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Revenues:</b>				
Annual membership dues	\$ 275,049	-	-	275,049
Life membership dues	117,177	-	-	117,177
Sustaining membership gifts	212,067	-	-	212,067
Other contributions	592,528	850	98,303	691,681
Endowment earnings used in operations	265,522	-	-	265,522
Commissions on ring sales	62,325	-	-	62,325
Baylor Line advertising and underwriting	23,559	-	-	23,559
Royalties	87,362	-	-	87,362
Lifelong learning	66,884	-	-	66,884
Other events	103,338	60,102	-	163,440
Miscellaneous revenues	7,712	-	-	7,712
Net assets released from restriction	54,664	(54,664)	-	-
Total revenues	<u>1,868,187</u>	<u>6,288</u>	<u>98,303</u>	<u>1,972,778</u>
<b>Expenses:</b>				
Program:				
Membership services	1,048,770	-	-	1,048,770
Management and general	383,997	-	-	383,997
Fund-raising	310,058	-	-	310,058
Total expenses	<u>1,742,825</u>	<u>-</u>	<u>-</u>	<u>1,742,825</u>
Change in net assets before other changes	<u>125,362</u>	<u>6,288</u>	<u>98,303</u>	<u>229,953</u>
<b>Other changes:</b>				
Gains and earnings on investments, net of transfers for operations	547,954	-	-	547,954
Contribution of beneficial interest in trust	120,000	-	-	120,000
Loss on disposal of property	(3,650)	-	-	(3,650)
Total other changes	<u>664,304</u>	<u>-</u>	<u>-</u>	<u>664,304</u>
Change in net assets	789,666	6,288	98,303	894,257
Net assets at beginning of year	<u>3,295,455</u>	<u>54,664</u>	<u>2,558,626</u>	<u>5,908,745</u>
Net assets at end of year	<u>\$ 4,085,121</u>	<u>60,952</u>	<u>2,656,929</u>	<u>6,803,002</u>

See accompanying notes to consolidated financial statements.

**Baylor Alumni Association  
and Subsidiary**

Consolidated Statement of Functional Expenses

Year Ended May 31, 2014

	<u>Program</u>			
	<u>Membership</u>	<u>Management</u>	<u>Fund-raising</u>	<u>Total</u>
	<u>Services</u>	<u>and General</u>		
Computer charges	\$ 1,529	14,507	-	16,036
Telephone	-	11,561	-	11,561
Insurance	-	10,393	-	10,393
Travel and meals	79	896	1,914	2,889
Guest services	1,439	-	285	1,724
Processing charges	-	7,698	-	7,698
Advertising and promotion	60	-	-	60
Catering for special events	5,826	2,711	-	8,537
Printing	55,174	3,094	-	58,268
Postage	22,251	627	-	22,878
Supplies	737	5,016	32	5,785
Professional fees:				
Baylor Line	42,182	-	-	42,182
Other	123,633	115,079	-	238,712
Event supplies	446	-	-	446
Rent/lease	1,400	15,225	-	16,625
Personnel costs	233,089	123,680	118,923	475,692
Depreciation	-	12,633	-	12,633
Scholarships	66,250	-	-	66,250
Miscellaneous	2,366	6,719	150	9,235
	<u>\$ 556,461</u>	<u>329,839</u>	<u>121,304</u>	<u>1,007,604</u>

See accompanying notes to consolidated financial statements.

**Baylor Alumni Association  
and Subsidiary**

Consolidated Statement of Functional Expenses

Year Ended May 31, 2013

	<u>Program</u>			
	<u>Membership</u>	<u>Management</u>	<u>Fund-raising</u>	<u>Total</u>
	<u>Services</u>	<u>and General</u>		
Computer charges	\$ -	19,869	-	19,869
Telephone	-	17,414	-	17,414
Insurance	-	9,957	-	9,957
Travel and meals	3,486	4,947	21,424	29,857
Guest services	3,547	-	13,629	17,176
Processing charges	-	15,405	-	15,405
Advertising and promotion	6,826	-	12,932	19,758
Catering for special events	83,823	-	13,845	97,668
Printing	100,200	1,430	220	101,850
Postage	37,698	1,137	-	38,835
Supplies	14,465	8,198	-	22,663
Professional fees:				
Baylor Line	109,062	-	-	109,062
Other	49,617	37,173	-	86,790
Contributions	8,932	-	-	8,932
Event supplies	24,314	-	320	24,634
Rent/lease	52,305	7,004	-	59,309
Personnel costs	496,058	238,697	247,538	982,293
Depreciation	-	12,924	-	12,924
Contract labor	2,600	775	-	3,375
Scholarships	55,357	-	-	55,357
Miscellaneous	480	9,067	150	9,697
	<u>\$ 1,048,770</u>	<u>383,997</u>	<u>310,058</u>	<u>1,742,825</u>

See accompanying notes to consolidated financial statements.



**Baylor Alumni Association  
and Subsidiary**

Consolidated Statements of Cash Flows

Years Ended May 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Cash flows from operating activities:		
Change in net assets	\$ 245,274	894,257
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Contributions to permanent endowments	-	(98,303)
Depreciation expense	12,633	12,924
Net realized and unrealized gain on investments	(572,022)	(801,139)
Beneficial interest in trust contributions	(135,000)	(120,000)
Loss on disposal of property	161	3,650
Decrease (increase) in accounts receivable	16,585	(2,506)
Decrease (increase) in due from Baylor University	(26,727)	5,135
Decrease in contribution receivable	-	10,000
Decrease in prepaid expenses	5,473	2,013
Increase in accounts payable	19,002	11,762
Increase (decrease) in accrued expenses	(43,434)	12,448
Net cash provided by (used in) operating activities	<u>(478,055)</u>	<u>(69,759)</u>
Cash flows from investing activities:		
Net change in cash restricted /designated for endowments	283,030	2,031
Capital expenditures	(1,551)	(14,124)
Net cash provided by (used in) investing activities	<u>281,479</u>	<u>(12,093)</u>
Cash flows from financing activities:		
Proceeds from contributions to permanent endowments	-	98,303
Net cash provided by financing activities	<u>-</u>	<u>98,303</u>
Net increase (decrease) in cash	(196,576)	16,451
Cash at beginning of year	<u>287,821</u>	<u>271,370</u>
Cash at end of year	<u>\$ 91,245</u>	<u>287,821</u>

See accompanying notes to consolidated financial statements.

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements

May 31, 2014 and 2013

(1) Summary of Significant Accounting Policies

(a) Organization

Baylor Alumni Association and Subsidiary (collectively, the Association) was organized to provide support for benevolent, charitable, and educational undertakings by extending financial and other aid to Baylor University and to students thereof, by generally encouraging sentiments favorable to education and by promoting union of and good fellowship among former students. The Association was organized to serve as the general alumni organization of Baylor University, and to coordinate all alumni activities and maintain the administrative agency and executive personnel needed to provide for continuity of alumni activity and interest. As described in Note 11, the Association is currently in litigation and discussions with Baylor University to determine what role the Association will serve in supporting Baylor University. Revenues are derived mainly from annual and life membership dues, royalties, charitable contributions and investment income.

Baylor Alumni Association is a non-profit Texas corporation without capital stock. Baylor Alumni Association's wholly-owned subsidiary, Baylor Alumni Service Enterprises, Inc. (the Corporation), was incorporated by Baylor Alumni Association with an initial capital contribution on September 12, 1980 under the Texas Nonprofit Corporation Act. The officers and directors of the Corporation serve in the same capacity as officers and directors of the Baylor Alumni Association.

(b) Principals of Consolidation

The consolidated financial statements include the accounts of Baylor Alumni Association and its wholly-owned subsidiary, Baylor Alumni Service Enterprises, Inc. All significant intercompany transactions and accounts have been eliminated in consolidation.

(c) Cash Equivalents

For purposes of the consolidated statements of cash flows, the Association considers all highly liquid assets with original maturities of three months or less to be cash equivalents. Cash and cash equivalents designated for long-term purposes or received with donor-imposed restrictions limiting their use to long-term purposes are not considered cash and cash equivalents for purposes of the statement of cash flows. There were no cash equivalents at May 31, 2014 and 2013.

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(1) Summary of Significant Accounting Policies (continued)

(d) Investments

Investments are measured at fair value in the consolidated statements of financial position. Investment income (including gains and losses on investments, interest, and dividends) is included in the consolidated statements of activities as increases or decreases in unrestricted net assets unless the income or loss is restricted by donor or law.

(e) Equipment, Works of Art and other Historical Treasures

Purchased equipment, works of art and other historical treasures are stated at cost as of the date of acquisition. Assets which are received from donations are recorded at fair value at the date of the gift. Equipment is depreciated on the straight-line method over the estimated useful lives of the assets. Depreciation on works of art and other historical treasures is not recorded. The Association capitalizes all acquisitions with a value greater than \$1,000. Costs of maintenance and repairs are charged to operations as incurred.

(f) Temporarily Restricted Net Assets

At May 31, 2013, temporarily restricted net assets of \$60,952 were donor restricted for scholarships. These funds were used to fund scholarships during the year ended May 31, 2014.

(g) Permanently Restricted Net Assets

Permanently restricted net assets are restricted to investment in perpetuity. The endowment funds are maintained with other investments administered by an independent trustee.

The Association has established a permanently restricted endowment fund in conjunction with its Sesquicentennial fund-raising campaign. The purpose of the campaign is to raise enough contributions to “endow” various employment positions as well as programs sponsored by the Association so that they will be self-sustaining in future years through income earned on the restricted net assets. The Abner V. McCall endowment fund was established so that investment income of the permanently restricted net assets would be available for general operations of the Association. Various other donors have made contributions to establish

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(1) Summary of Significant Accounting Policies (continued)

(g) Permanently Restricted Net Assets (continued)

endowed scholarship funds so that the investment income earned from the permanently restricted net assets would be available for scholarships provided by the Association.

(h) Designated Net Assets

Certain assets received by the Association, which are unrestricted in nature, have been designated by the Board of Directors for a particular purpose. These commitments are presented separately in the net assets of the Association as being designated.

The Board has designated \$1 per membership from the annual membership dues for the scholarship fund of Baylor University. The scholarship amounts for 2014 and 2013 of \$270 and \$2,932, respectively, were paid and/or accrued to Baylor University as of May 31, 2014 and 2013. In addition, all of the life membership dues and investment income not used for current year operations are designated for the unrestricted endowment fund of the Association.

(i) Fair Value Hierarchy

Generally accepted accounting principles establish a fair value hierarchy that prioritizes the inputs to valuation techniques used for fair value measurements of nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the consolidated financial statements. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Association has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable inputs for the asset or liability.

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(1) Summary of Significant Accounting Policies (continued)

(j) Support and Expenses

Contributions received and unconditional promises to give are measured at their fair values and are reported as an increase in net assets. The Association reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets, or if they are designated as support for future periods. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions. Donor restricted contributions whose restrictions are met in the same reporting period are reported as unrestricted support.

The Association reports gifts of land and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Association reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

(k) Advertising

Advertising costs, except for costs associated with direct-response advertising, are charged to operations when incurred. Advertising costs charged to operations were \$60 and \$19,758 for the years ended May 31, 2014 and 2013, respectively.

(l) Income Taxes

Baylor Alumni Association qualifies as a non-profit organization under Section 501(c)(3) of the Internal Revenue Code. Therefore, the Association is generally exempt from federal and state income taxes.

The Association recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(1) Summary of Significant Accounting Policies (continued)

(l) Income Taxes (continued)

which the change in judgment occurs. The Association is no longer subject to U.S. federal and state income tax examinations by tax authorities for years including and subsequent to 2011.

The Association records interest related to unrecognized tax benefits and penalties in management and general expenses. There were no interest and penalties for 2014 and 2013.

(m) Fund-Raising Expenses

Fund-raising expenses consist primarily of membership development and solicitation activities through direct mail and telephone initiatives, as well as personnel costs and direct expenses of the Sesquicentennial campaign and Hall of Fame scholarship fundraiser.

(n) Functional Allocation of Expenses

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

(o) Agency Transactions

The Association recognizes an asset and corresponding liability for funds received in connection with agency transactions. The financial effects of transactions related to agency funds are recorded as changes in the funds held for agency liability and are not included in the consolidated statements of activities.

(p) Use of Estimates

Management has made estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities in the preparation of these consolidated financial statements. Significant items subject to such estimates and assumptions include the useful lives of equipment, allowance for contribution receivables, and valuation of investments and beneficial interest in trust. Actual results could differ from those estimates and assumptions.

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(2) Investment

At May 31, 2014 and 2013, the Association's investment consisted entirely of the Group Investment Fund II of the Baptist Foundation of Texas (the Fund). The Fund is measured at fair value using a Level 2 input (as defined in Note 1(i)). This input consists of the net asset value per share of the Fund. The Fund is designed specifically to meet the unique needs of endowment funds. This is done by maintaining a highly diversified and balanced portfolio to seek maximum total return within reasonable risk levels, consistent with the long-term nature of endowment accounts. The Funds are socially screened to eliminate companies whose business activities are inconsistent with Baptist faith and beliefs. The fund's long-term asset allocation is well diversified, investing in global equities, energy, marketable alternatives, fixed income, real estate and private equity.

The Fund is valued daily and contributions and withdrawals may be made twice a month at the current net asset value. Income distributions can be made monthly, quarterly or annually.

Following is a summary of the Fund's investments at May 31, 2014 and 2013:

	2014	2013
Equity securities - domestic	\$ 1,801,757	1,481,068
Equity securities - international	1,773,878	1,528,544
Debt securities	1,128,285	900,094
Real estate	280,978	306,884
Private equity	280,979	223,188
Money market	200,620	454,697
	\$ 5,466,497	4,894,475

Investment income is comprised of realized and unrealized gains of \$588,441 and \$697,169, and interest and dividends of \$118,631 and \$116,307 as May 31, 2014 and 2013, respectively.

(3) Beneficial Interest in Trust

During 2009, a perpetual charitable trust (the Trust) was established by an outside grantor, whereby, the Association, along with four other organizations, was named a beneficiary. Each year 50% of the Trust income will be distributed to the beneficiaries based on their stated proration and the remaining 50% will be reinvested into the corpus of the Trust. The Association's pro-rata share is 20%. The Trust term is 50 years and at the end of the term all mineral and royalty assets of the Trust will be distributed to Baylor

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(3) Beneficial Interest in Trust(continued)

University and the remainder of all assets will be distributed to all the beneficiaries based on the same proportionate share as the income distributions.

Funding of the Trust came from the estate of the grantor upon death, which occurred in December 2010 and the estate was settled during 2013. The fair value of the Trust was determined to be \$4,276,066 and \$3,624,560 at May 31, 2014 and 2013, respectively. Accordingly, management recognized 20% of the fair value of the trust at May 31, 2013 and 2014 of \$855,000 and \$720,000, respectively.

Because there is no market in which the beneficial interest in the Trust can trade, there are no observable inputs available to establish the fair value. Therefore, the inputs used are considered Level 3 inputs (as defined in Note 1(i)). The following table presents a roll-forward of the fair value of Level 3 assets and liabilities for the years ended May 31, 2013 and 2014.

	<u>2014</u>	<u>2013</u>
Balance, beginning of year	\$ 720,000	600,000
Total gains and losses	156,759	135,909
Distributions to beneficiaries	<u>(21,759)</u>	<u>(15,909)</u>
Balance, end of year	<u>\$ 855,000</u>	<u>720,000</u>

During 2014, certain distributions from the Trust made payable to the Association were instead delivered to Baylor University by the Trustee. The Association has requested payment from Baylor University and recorded an account receivable of \$24,829. Subsequent to yearend the Trustee filed a Petition with the Courts to seek instructions regarding the administration of the Trust and modification of the Trust instrument. The Association, as a beneficiary, has continued to record their share of the Trust's assets in accordance with the Trust document.

(4) Endowment

The Association's endowment consists of approximately 22 individual funds established for a variety of purposes. As required by generally accepted accounting principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions. As a result, the Association classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations (decrements) to the permanent endowment made in accordance with the direction of the applicable donor gift instrument.



**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(4) Endowment (continued)

The Association has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowments while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Association must hold in perpetuity as well as board-designated funds. Under this policy the endowment assets are invested in a manner that is intended to produce a real rate of return of at least 5% net of expenses, on an annualized basis. Actual returns in any given year may vary from this amount. Investment income from permanent endowments for non-scholarship funds, which includes interest and dividends as well as realized and unrealized gains and losses, are included in unrestricted net assets. Investment losses from permanent endowments for scholarship funds are charged to permanently restricted net assets, while investment income in excess of accumulated investment losses is included in temporarily restricted net assets for the use of scholarships.

Investment income from the designated endowment available to be spent for operations in 2014 and 2013 was \$416,588 and \$265,522, respectively, and was based on the Association's spending policy discussed above.

The following is the composition of endowment net assets by type of fund as of May 31, 2014 and 2013:

	<u>Unrestricted, Designated</u>	<u>Permanently Restricted</u>	<u>Total</u>
At May 31, 2014:			
Donor-restricted endowments	\$ -	2,656,929	2,656,929
Board designated endowment	<u>3,563,236</u>	<u>-</u>	<u>3,563,236</u>
	<u>\$ 3,563,236</u>	<u>2,656,929</u>	<u>6,220,165</u>
At May 31, 2013:			
Donor-restricted endowments	\$ -	2,656,929	2,656,929
Board designated endowment	<u>3,252,996</u>	<u>-</u>	<u>3,252,996</u>
	<u>\$ 3,252,996</u>	<u>2,656,929</u>	<u>5,909,925</u>

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(4) Endowment (continued)

	<u>Unrestricted, Designated</u>	<u>Permanently Restricted</u>	<u>Total</u>
For the year ended May 31, 2014:			
Endowment net assets, beginning of year	\$ 3,252,996	2,656,929	5,909,925
Contributions and additions	19,756	-	19,756
Investment gains	707,072	-	707,072
Distributed earnings	<u>(416,588)</u>	<u>-</u>	<u>(416,588)</u>
Endowment net assets, end of year	<u>\$ 3,563,236</u>	<u>2,656,929</u>	<u>6,220,165</u>
For the year ended May 31, 2013:			
Endowment net assets, beginning of year	\$ 2,587,865	2,558,626	5,146,491
Contributions and additions	117,177	98,303	215,480
Investment losses	813,476	-	813,476
Distributed earnings	<u>(265,522)</u>	<u>-</u>	<u>(265,522)</u>
Endowment net assets, end of year	<u>\$ 3,252,996</u>	<u>2,656,929</u>	<u>5,909,925</u>

(5) Related Party Transactions

Baylor University provides various services to the Association for which the costs are reimbursed by the Association. During the year ended May 31, 2013, expenses reflected in the accompanying consolidated financial statements that relate to these services were \$22,619.

The Association receives investment income on certain endowment funds administered by Baylor University. Investment income received by the Association from these endowments for the years ended May 31, 2014 and 2013 totaled \$31,092 and \$30,953, respectively.

In 1994, the Association and Baylor University entered into an agreement which allowed the Association the exclusive use of the Hughes-Dillard Alumni Center building for an indefinite term. As discussed in Note 11, during 2014 Baylor University terminated the Association's right to use the office building and, under mutual agreement, the Association vacated the building.

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(6) Intentions to Give

During 2014 and 2013, the Association received contributions from various donors totaling \$-0- and \$37,803, respectively, for the Sesquicentennial Campaign, as more fully described in Note 1(g). In addition, various donors have made pledges (intentions to give) for future contributions to the campaign. These intentions to give will not be reflected as contributions in the accompanying consolidated statements of activities until the pledges are collected.

(7) Contribution Receivable

A contribution receivable is recognized at fair value when the donor makes a promise to give to the Association that is, in substance, unconditional. A receivable of \$290,000 at May 31, 2014 and 2013 represent amounts that are pledged to establish funds for scholarships. The \$290,000 contribution receivable as of May 31, 2014 is due as follows: 2015, \$186,666; 2016, \$93,334; and 2017, \$10,000.

(8) Leases

The Association has a noncancelable operating lease for postage equipment that expires in one year and a noncancelable operating lease for a copier that expires in 4 years. The Association has a “rolling 90-day basis” lease agreement for office space beginning in January 2014. The Association also leased other equipment, storage space, and facilities for special events throughout the year. Rental expenses for 2014 and 2013 were \$16,625 and \$59,309, respectively. Future minimum lease payments under the noncancelable operating leases are as follows: 2015, \$4,392; 2016, \$4,392; 2017, \$2,159; and 2018, \$978.

(9) Employee Benefit Plan

The Association sponsors a 403(b)(9) defined contribution plan. All employees who have attained the age of 21, are not a student, are full-time employees, and have one year of service are eligible for the plan. The plan allows employees to make voluntary pre-tax salary contributions up to an annually defined maximum as allowed by the Internal Revenue Code. Employer contributions to the plan were suspended in 2012.

(10) Business and Credit Concentrations

At May 31, 2014 and 2013, and periodically throughout the years then ended, the Association maintained balances in deposit accounts at a financial institution in excess of federally insured limits.

**Baylor Alumni Association  
and Subsidiary**

Notes to Consolidated Financial Statements  
(Continued)

(11) Transition Agreement and Relationship with Baylor University

On May 31, 2013, the Association's executive committee and Baylor University (Baylor) representatives, after approximately a year of discussions and deliberation, entered into a certain agreement (the Transition Agreement) that would transfer all operations not related to the communication programs (including the Baylor Line magazine and Between the Lines email) of the Association to Baylor. If approved by the Association's membership, the agreement would result in the termination of all other agreements between the Association and Baylor, and the ultimate legal dissolution of the Association. Additionally, a new 501(c)(3) organization, Baylor Line Corporation, would be created that would publish the Baylor Line magazine and the Between the Lines email newsletter. This organization would be independent from Baylor, and maintain the editorial independence of the publications. A vote of the Association members took place on September 7, 2013. Two-thirds of the members voting on September 7 did not approve the Transition Agreement.

In conjunction with the Transition Agreement, the University issued the Association a notice of unilateral termination of several legal agreements, including the 1993 license agreement (which allows the Association the exclusive use of the names Baylor University Alumni Association, Baylor Alumni Association and The Baylor Line) and the 1994 agreement concerning the Hughes-Dillard Alumni Center, which the Association agreed to vacate to support Baylor's stadium project

On June 6, 2014 Baylor filed a suit against the Association, alleging that Baylor has terminated its trademark and recognition agreements with the Association, and that the Association is infringing on Baylor's marks by conducting business under various "Baylor" designations.

The Association has denied Baylor's allegations, and has filed counterclaims against Baylor. The Association claims that Baylor has prevented the Association from performing certain functions afforded them in their contracts with Baylor and, therefore, Baylor is estopped from asserting that the Association has breached its contractual obligations. The ultimate outcome of these lawsuits raises an uncertainty as to the future role that the Association will play with Baylor. The uncertain environment in which the Association now operates, and lack of access to Baylor students for alumni contributions and fundraising activities, continues to place stress on the operations of the Association. The Association has reduced certain expenses as revenues have decreased. Management represents that the Association will remain in existence for a reasonable period of time.

(12) Subsequent Events

Subsequent events have been evaluated through November 30, 2014 which is the date the consolidated financial statements were available to be issued.