

**COLLEGE FUTURES FOUNDATION**

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**CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

# COLLEGE FUTURES FOUNDATION

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## C O N T E N T S

	<b>Page</b>
Independent Auditors' Report	1
Consolidated Statements of Financial Position	2
Consolidated Statements of Activities and Changes in Net Assets	3
Consolidated Statements of Cash Flows	4
Notes to Consolidated Financial Statements	5–17



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## INDEPENDENT AUDITORS' REPORT

The Board of Directors  
College Futures Foundation

We have audited the accompanying consolidated financial statements of College Futures Foundation (a nonprofit organization), which comprise the consolidated statements of financial position as of December 31, 2016 and 2015, and the related consolidated statements of activities and changes in net assets, 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 the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### Auditors' 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 auditors' 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 auditors consider 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 College Futures Foundation as of December 31, 2016 and 2015, and the changes in net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

BPM LLP

San Francisco, California  
September 28, 2017

**COLLEGE FUTURES FOUNDATION**  
**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**

December 31, 2016 and 2015

*(in thousands)*

	<u>2016</u>	<u>2015</u>
<b>ASSETS</b>		
Cash and cash equivalents	\$ 4,241	\$ 4,958
Investments, at fair value	468,579	455,828
Net receivables from unsettled trades	13,500	17,500
Student loans receivable, net	1,073	1,586
Other assets	1,098	694
Fixed assets, net	<u>892</u>	<u>1,011</u>
 Total assets	 <u><u>\$ 489,383</u></u>	 <u><u>\$ 481,577</u></u>
<b>LIABILITIES AND NET ASSETS</b>		
Liabilities:		
Accounts payable and accrued liabilities	\$ 788	\$ 811
Grants payable, net	11,495	10,098
Deferred federal excise tax liability	<u>1,429</u>	<u>1,183</u>
 Total liabilities	 13,712	 12,092
 Net assets - unrestricted	 <u>475,671</u>	 <u>469,485</u>
 Total liabilities and net assets	 <u><u>\$ 489,383</u></u>	 <u><u>\$ 481,577</u></u>

The accompanying notes are an integral  
part of these consolidated financial statements.

**COLLEGE FUTURES FOUNDATION**  
**CONSOLIDATED STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS**

For the years ended December 31, 2016 and 2015

*(in thousands)*

	<u>2016</u>	<u>2015</u>
Revenue:		
Investment income, net	\$ 28,085	\$ 12,742
Student loan related revenue, net	<u>102</u>	<u>145</u>
Net revenue before excise and income tax expense	28,187	12,887
Excise and income tax expense	<u>(576)</u>	<u>(200)</u>
Net revenue after excise and income tax expense	<u>27,611</u>	<u>12,687</u>
Expenses:		
Program expenses:		
Grants awarded and direct charitable activities	16,948	18,038
Program-related expenses	<u>2,494</u>	<u>2,465</u>
Total program expenses	19,442	20,503
Management and general expenses	<u>1,983</u>	<u>1,977</u>
Total expenses	<u>21,425</u>	<u>22,480</u>
Change in net assets	6,186	(9,793)
Net assets - unrestricted, beginning of year	<u>469,485</u>	<u>479,278</u>
Net assets - unrestricted, end of year	<u><u>\$ 475,671</u></u>	<u><u>\$ 469,485</u></u>

The accompanying notes are an integral part of these consolidated financial statements.

**COLLEGE FUTURES FOUNDATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

For the years ended December 31, 2016 and 2015

*(in thousands)*

	<u>2016</u>	<u>2015</u>
Cash flows from operating activities:		
Change in net assets	\$ 6,186	\$ (9,793)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation of fixed assets	365	206
Net realized and unrealized gain on investments	(28,379)	(11,273)
Provision for loan losses	16	(30)
Deferred federal excise tax	247	(329)
Changes in operating assets and liabilities:		
Net decrease in student loans receivable	496	743
Net increase in other assets	(401)	(24)
Net decrease in accounts payable and accrued liabilities	(27)	(155)
Net increase in grants payable	<u>1,397</u>	<u>81</u>
Net cash used in operating activities	<u>(20,100)</u>	<u>(20,574)</u>
Cash flows from investing activities:		
Proceeds from sale of investments	33,938	39,902
Purchases of investments	(18,308)	(23,592)
Net receivables from unsettled trades	4,000	3,500
Purchases of property and equipment	<u>(247)</u>	<u>(663)</u>
Net cash provided by investing activities	<u>19,383</u>	<u>19,147</u>
Net decrease in cash and cash equivalents	(717)	(1,427)
Cash and cash equivalents, beginning of year	<u>4,958</u>	<u>6,385</u>
Cash and cash equivalents, end of year	<u>\$ 4,241</u>	<u>\$ 4,958</u>
Supplemental disclosure of cash flow information:		
Cash paid for excise and income taxes	<u>\$ 688</u>	<u>\$ 731</u>

The accompanying notes are an integral part of these consolidated financial statements.

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**1. Organization and Business**

College Futures Foundation (“College Futures”) is a private foundation working with partners throughout California to increase bachelor’s degree attainment among low-income students and others who are under-represented in higher education.

College Futures operates on the belief that every qualified student in California should have the opportunity to succeed in college and it recognizes that creating a vibrant future for our state requires awarding more bachelor’s degrees to broader populations of students.

Each year, College Futures awards grants to dozens of partner organizations throughout California, funding and supporting work in three main areas: improving student transitions toward degree completion; developing and strengthening partnerships across institutions, systems, and regions to drive increases in bachelor’s degree attainment; and reducing gaps between policy and practice to advance student access to and success in college.

Established in 2005, College Futures and its wholly owned subsidiary, CEFI Corporation (“CEFI”), together referred to as the “Foundation,” are the result of a series of corporate restructurings that were completed in 2006. The Foundation was funded with the proceeds from the wind down of the nonprofit Chela Education Financing, Inc.

**2. Summary of Significant Accounting Policies**

***Basis of Consolidation***

The accompanying Consolidated Financial Statements of the Foundation have been prepared on the accrual basis of accounting and are presented on the basis of unrestricted, temporarily restricted, or permanently restricted net assets. At December 31, 2016 and 2015, the Foundation had no temporarily or permanently restricted net assets. The Consolidated Financial Statements include the accounts of College Futures and CEFI. All significant intercompany accounts and transactions have been eliminated.

***Cash and Cash Equivalents***

Cash equivalents consist of demand deposits in banks and money market funds with original maturities of 90 days or less.

***Investments***

Investments are stated at fair value. Net realized and unrealized gains or losses on investments are reflected as increases or decreases in unrestricted net assets. Gains and losses that result from market fluctuations are recognized in the period such fluctuations occur. Realized gains or losses are calculated based on purchase prices. Dividend income is recorded on ex-dividend dates. Interest income from investments is recorded on an accrual basis.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**2. Summary of Significant Accounting Policies, continued**

***Investments***, continued

Debt and equity securities with readily determinable fair values are carried at estimated fair value, based on quoted market prices. The Foundation invests in limited partnerships including diversified inflation hedges, fixed income and bond funds, multi-strategy endowment pools, and private equity funds that may not be immediately liquid nor have readily determinable fair values. These investments are valued at amounts reported to the Foundation by the general partners of such entities, in accordance with their established guidelines. Further, management reviews the annual forms K-1, the audited financial statements for the partnerships, reviews investment managers' valuation policies, monitors news in the public domain in connection with its investment managers, meets periodically with investment managers, and participates in quarterly investor calls. Management believes these methods provide a reasonable basis for the fair value. These values may differ significantly from values that would have been used had a readily available market existed for such investments, and the differences could be material.

***Net Receivables from Unsettled Trades***

Receivables from unsettled trades are amounts due from pending investment redemption requests made before December 31, 2016 and 2015. These trades were settled in January 2017 and January 2016, respectively.

***Fair Value Measurements***

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Foundation uses various valuation approaches. In accordance with Generally Accepted Accounting Principles ("GAAP"), a hierarchy has been established for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the Foundation. Unobservable inputs are inputs that reflect the Foundation's assumptions about what market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The Foundation classifies its financial assets and liabilities according to the following hierarchy, from (1) highest to (3) lowest in the use of observable inputs, and minimizes the use of unobservable inputs when measuring fair value:

*Level 1* – quoted prices in active markets for identical investments. The types of investments in Level 1 include listed equities held in the name of the Foundation.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**2. Summary of Significant Accounting Policies, continued**

***Fair Value Measurements***, continued

*Level 2* – pricing inputs, including broker quotes, are generally those other than exchange quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.

*Level 3* – pricing inputs are unobservable for the investment and include situations where there is little, if any, market activity for the investment.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement. The Foundation's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and consideration of factors specific to the investment.

***Grants***

Unconditional grants are recognized as grant expense and a liability when the Foundation's Board of Directors (the "Board") approves the grants or the President and Chief Executive Officer authorizes grants in accordance with Board-approved authority. Unconditional grants that are expected to be paid in less than one year are measured at net settlement value. Unconditional grants that are expected to be paid in more than one year are measured at the present value of the estimated future cash flows. Grant refunds are recorded as a reduction of grant expense at the time the Foundation becomes aware the grant will be refunded.

***Income Taxes***

College Futures is a nonprofit organization exempt from income tax under Section 501(c)(3) of the Internal Revenue Code (the "Code") and Section 23701(d) of the Revenue and Taxation Code of the State of California. Since the beginning of fiscal year 2010, College Futures has been classified as a private foundation within the meaning of Section 509(a) of the Code. As such, College Futures is still exempt from federal income taxes under Section 501(c)(3) of the Code and is exempt from California franchise and/or income taxes under Section 23701(d) of the Revenue and Taxation Code. However, College Futures is subject to federal excise taxes as well as federal and state unrelated business income tax.

As a for-profit Delaware corporation, CEFI uses the liability method to account for income taxes. Under this method, deferred income tax assets and liabilities are based on the differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**2. Summary of Significant Accounting Policies, continued**

***Income Taxes***, continued

The Foundation recognizes interest and penalties accrued related to unrecognized tax benefits in “Management and general expenses” on the Consolidated Statements of Activities and Changes in Net Assets. No interest or penalties have been accrued as of December 31, 2016 and 2015. The Foundation follows guidance for the recognition of uncertain tax positions. Management has concluded there are no uncertain tax positions at December 31, 2016 and 2015.

***Functional Expenses***

The costs of providing various programs and other activities have been summarized on a functional basis in the Consolidated Statements of Activities and Changes in Net Assets. Student loan related expenses and investment related expenses are included in “Student loan related revenue, net” and “Investment income, net”, respectively, on the Consolidated Statements of Activities and Changes in Net Assets. Directly identifiable expenses, such as grants awarded, certain grant-making expenses, and other costs, are charged to program and management and general expenses. Expenses related to more than one function are charged to programs, management and general expenses, student loan related expenses, direct charitable activities, and investment related expenses on the basis of periodic time studies. Management and general expenses include those expenses that are not directly identifiable with any other specific function but provide for the overall support and direction of the Foundation.

***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. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

***Reclassifications***

For comparative purposes, certain amounts in the prior year’s Consolidated Financial Statements have been reclassified to conform to the current year presentation.

***Recent Accounting Pronouncements***

In May 2015, the Financial Accounting Standards Board (the “FASB”) issued Accounting Standards Update (“ASU”) 2015-07, *Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*, which removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share (or its equivalent) practical expedient. For private entities, the new guidance is effective for interim and annual reporting periods that begin after December 15, 2016, with early adoption permitted. The Foundation elected to early adopt ASU 2015-07 in 2015. As a result of the early adoption of ASU 2015-07, these investments are not categorized within the fair value hierarchy.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**2. Summary of Significant Accounting Policies, continued**

***Recent Accounting Pronouncements, continued***

In February 2016, the FASB issued ASU 2016-02 *Leases*, amending the ASC 842. This update requires lessees to recognize operating and financing lease liabilities and corresponding right-of use assets on the statement of financial position. The new guidance is effective for the Foundation beginning January 1, 2020. The Foundation is currently evaluating the impact that this guidance will have on its financial statements.

In August 2016, the FASB issued ASU 2016-14 *Presentation of Financial Statements of Not-for-Profit Entities*, amending the ASC 958. This update changes the presentation of certain information in the financial statements and footnote disclosures of not-for-profit entities. The update also changes the way that not-for-profit entities classify net assets. The new guidance is effective for the Foundation for the year beginning January 1, 2018. The Foundation is currently evaluating the impact that this guidance will have on its financial statements.

***Significant Accounting Policies Associated with Student Loans***

As outlined in Note 1, between 2004 and 2006, there was a corporate restructuring, sale of assets, and a wind-down of operations associated with student loans. Listed below are the significant accounting policies associated with the remaining student loan portfolio.

**Student loans receivable** held are carried at the principal amount outstanding, net of unamortized premiums or discounts, deferred loan fees and costs, and acquisition fair value adjustments, if any. Write-downs of the loans' carrying values attributable to credit quality are charged to the allowance for loan losses. Additionally, from time to time, certain student loans receivables that have previously been written off and deemed uncollectible are recovered.

**The allowance for loan losses** is maintained at a level to provide for probable losses inherent in the consumer education loan ("CEL") portfolio as of the reporting date and is established through a provision charged to student loan expenses. Management considers historical portfolio data, student loan default rates published in market reports and general economic conditions to estimate the allowance for loan losses. Loans are charged off when the collection of principal and interest is 180 days past due.

**Student loan related revenue, net** includes collections on previously written off loans and interest income, offset by internal and external costs directly attributable to the management and oversight of the student loan portfolio.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

**3. Fair Value Measurements and Investments**

The following table presents investment income for the years ended December 31, 2016 and 2015 (in thousands):

	2016	2015
Interest, dividends, and other	\$ 7,476	\$ 10,033
Realized gains, net	15,342	27,769
Unrealized gains (losses), net	13,037	(16,496)
Investment related fees and expenses	(7,770)	(8,564)
Total investment income, net	\$ 28,085	\$ 12,742

The following tables summarize the valuation of the Foundation's assets and liabilities measured on a recurring basis as of December 31, 2016 and 2015 (in thousands):

	2016	2015
Fair value measurements:		
Cash equivalents—money market (Level 1)	\$ 505	\$ 1,578
Investments:		
Balanced global mutual fund (Level 1)	3,340	3,110
Investments measured using NAV:		
Fixed income and bond funds	12,975	10,359
Multi-strategy endowment pool	422,477	409,989
Diversified inflation hedges	8,328	9,566
Private equity funds	21,459	22,804
Total investments, at fair value	468,579	455,828
Net receivables from unsettled trades (Level 2)	13,500	17,500
Total	\$ 482,584	\$ 474,906

There were no significant transfers between Level 1, Level 2, and Level 3 of the fair value hierarchy during 2016 and 2015. The Foundation recognizes transfers into and out of levels on their respective transaction dates.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
December 31, 2016 and 2015

**3. Fair Value of Measurements and Investments, continued**

The Foundation uses NAV to estimate the fair value of underlying investments which a) do not have readily determinable fair values and b) prepare their financial statements consistent with the measurement principles of an investment company or have attributes of an investment company. The following table lists investments in other investment companies (in partnership or trust format) by major class as of December 31, 2016 (in thousands):

	Strategy	NAV in Funds	Number of Funds	Remaining Life	Unfunded Commitments	Redemption Notice Period	Redemption Restrictions
Assets:							
Fixed income and bond funds	Short-term fixed income	\$ 12,975	1	NA	\$ -	10 days	Redemptions only on last business day of any month.
Multi-strategy endowment pool	Multi-strategy <sup>(a)</sup>	422,477	1	NA	-	120 days	Full fund redemptions permitted annually, subject to a 10% holdback and side pockets for illiquid assets. College Futures can redeem up to 7% annually during the specified redemption period, which is not subject to any additional restrictions.
Diversified inflation hedges	Natural resources and real estate	8,328	4	0–8 years	708	NA	NA*
Private equity funds	Venture and buyout U.S. and international	21,459	6	3–9 years	2,578	NA	NA*
Total		<u>\$ 465,239</u>			<u>\$ 3,286</u>		

\* Private equity fund structures with no ability to redeem.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**3. Fair Value Measurements and Investments**, continued

(a) The Multi-strategy endowment pool is one fund that includes investments in equities, real assets, commodities, natural resources, credit, fixed income, hedge funds, and direct hedges. Equity investments strategies include long-only and long-biased, public and private equities in both domestic and international markets. Real asset investment strategies include investments in real estate, power, infrastructure, and non-resource real assets. Commodities and natural resources investment strategies are focused on liquid commodities such as metals and agricultural products and private natural resources such as timber and mining interests. Credit investment strategies are primarily non-investment grade and distressed credit. Fixed income investment strategies are United States Treasuries and Treasury Inflation Protected securities, other sovereign debt, and investment grade credit. Hedge fund strategies include those that are event-driven, such as corporate merger activity and the use of long and offsetting short positions. Finally, the strategies for direct hedges include investments in currencies, gold, and options such as puts and calls.

The liquidity profile for the multi-strategy endowment pool is actively managed to maintain sufficient liquidity for limited partners. At December 31, 2016, 59% and 66% of the pool was convertible to cash within one year and three years, respectively, and at December 31, 2015, 57% and 66% of the pool was convertible to cash within one year and three years, respectively.

**4. Items Associated with Student Loans**

The Consolidated Financial Statements of the Foundation reflect the following items associated with the student loan operations.

**A. Student Loans Receivable**

The Foundation classifies the CEL portfolio as a portfolio segment, as defined in the ASC, and evaluates the adequacy of the allowance for loan losses for the CEL portfolio as a whole. Accordingly, the portfolio segment basis disclosures required by the ASC are presented in this note for the CEL portfolio. In addition, as of December 31, 2016 and 2015, the Foundation does not have any impaired loans as defined in the accounting standards.

The following is a schedule of student loans receivable at December 31, 2016 and 2015 (in thousands):

	2016	2015
CEL loans receivable	\$ 1,117	\$ 1,663
Allowance for loan losses	(44)	(77)
Student loans receivable, net	\$ 1,073	\$ 1,586

The CEL loans had an average time to maturity weighted by dollar value of approximately four and five years as of December 31, 2016 and 2015, respectively.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

**4. Items Associated with Student Loans, continued**

**B. Allowance for Loan Losses**

The table below summarizes the changes in the allowance for loan loss reserve for the years ended December 31, 2016 and 2015 (in thousands):

	2016	2015
Balance at beginning of the year	\$ 77	\$ 96
Provision for possible losses	(17)	(1)
Charges to allowance	(16)	(18)
Balance at end of the year	\$ 44	\$ 77

Total recoveries were approximately \$30,000 and \$44,000 for the years ended December 31, 2016 and 2015, respectively.

**C. Aging of Student Loan Receivables**

The majority of student loan receivables are current, with approximately \$1,045,000 and \$1,594,000 of the balance being current as of December 31, 2016 and 2015, respectively. The remaining balances of \$73,000 and \$69,000 as of December 31, 2016 and 2015, respectively, were 30 or more days past due.

**5. Grants Payable**

Future minimum unconditional grants payable as of December 31, 2016 are scheduled as follows (in thousands):

2017	\$ 8,476
2018	2,782
2019	385
Total unconditional grants payable	11,643
Less discounts to net present value	(148)
Net unconditional grants payable	\$ 11,495

**6. Employee Benefits**

College Futures sponsors a 403(b) plan to which eligible employees may voluntarily contribute a percentage of their compensation. College Futures also contributes matching amounts. College Futures' 403(b) plan expense was \$195,000 and \$167,000, respectively, for the years ended December 31, 2016 and 2015. Beginning in 2014, College Futures also provides a contributory money purchase 401(a) plan for all eligible employees. The 401(a) plan is funded by College Futures only. College Futures' 401(a) plan expense was \$197,000 and \$174,000, respectively, for the years ended December 31, 2016 and 2015. Both plans are maintained by an independent trustee.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**6. Employee Benefits, continued**

College Futures also has an unfunded deferred compensation plan for a select group of highly compensated or management level employees under Section 457(b) of the Code. Eligible employees may voluntarily contribute a percentage of their compensation to the plan. In addition, College Futures contributes to the plan on behalf of eligible employees that did not receive their full contributions through the 403(b) or 401(a) plans due to Internal Revenue Service (“IRS”) limits covering those plans. At December 31, 2016 and 2015, respectively, College Futures held \$384,000 and \$290,000 in “Other assets” which are designated to pay an offsetting deferred compensation liability that is included in “Accounts payable and accrued liabilities” on the Consolidated Statements of Financial Position.

**7. Excise and Income Taxes**

***Excise Taxes***

In accordance with the applicable provisions of the Code, College Futures is required to distribute 5% of the average fair market value of its investment assets annually. Excess distributions may be carried forward up to 5 years to offset years with distributions below 5%. College Futures met this minimum pay out requirement in each of the years presented in these financial statements.

Private foundations are liable for an excise tax of 2% (1% if minimum payout requirements prescribed by the Code are met) on investment income, excluding unrealized gains. College Futures paid 2% in 2016 and 2015. Deferred federal excise taxes arise primarily from unrealized gains on investments and have been accrued based on a 2% rate. If taxes are due, current federal excise taxes payable are included in “Accounts payable and accrued liabilities” on the Consolidated Statements of Financial Position. Conversely, if a refund is due, these accounts are included in “Other assets” on the Consolidated Statements of Financial Position. For the years ended December 31, 2016 and 2015, current federal excise taxes payable were included in “Accounts payable and accrued liabilities.”

The provision for federal excise taxes and unrelated business income taxes at December 31, 2016 and 2015 (in thousands) are:

	2016	2015
Current	\$ 329	\$ 529
Deferred	247	(329)
Total	\$ 576	\$ 200

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**7. Excise and Income Taxes, continued**

***Unrelated Business Income Taxes***

Unrelated business income taxes arise primarily from income generated from certain types of investments, such as particular kinds of real estate investments. If taxes are due, federal and state unrelated business income taxes payable are included in "Accounts payable and accrued liabilities" on the Consolidated Statements of Financial Position. Conversely, if a refund is due, these accounts are included in "Other assets" on the Consolidated Statements of Financial Position. For the years ended December 31, 2016 and 2015, unrelated business income tax refunds were included in "Other assets."

College Futures realized pre-tax unrelated business income of \$1,012,000 and a pre-tax loss of (\$1,013,000) in 2016 and 2015, respectively. Although College Futures realized pre-tax income, no income tax was recognized as of December 31, 2016 and 2015, as College Futures utilized operating loss carryforwards to offset income.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. College Futures' deferred tax asset balances associated with unrelated business income at December 31, 2016 and 2015, respectively, were \$643,000 and \$978,000 and are comprised entirely of net operating loss carryforwards. Based on the available objective evidence at December 31, 2016 and 2015, College Futures does not believe it is more likely than not that the net deferred tax assets will be fully realizable. Accordingly, College Futures has provided a full valuation allowance against its net deferred tax assets at December 31, 2016 and 2015. The valuation allowance decreased by \$335,000 and increased \$335,000 for the years ended December 31, 2016 and 2015, respectively.

As of December 31, 2016, College Futures had federal and state net operating loss carryforwards associated with unrelated business income of approximately \$1,892,000 and \$1,725,000, respectively. There is no limitation on the use of these net operating losses and, if not utilized, the net operating loss carryforwards begin expiring in 2032. College Futures' ability to utilize the net operating losses or realize any benefit is uncertain; therefore, a full valuation allowance has been applied against the associated deferred tax asset.

***Income Taxes***

CEFI realized a pre-tax loss of (\$22,000) and (\$15,000) in 2016 and 2015, respectively. CEFI recognized \$800 as income tax expense in 2016 and 2015 based on California regulatory minimum payment requirements.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**7. Excise and Income Taxes, continued**

***Income Taxes, continued***

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. CEFI's deferred tax asset balances at December 31, 2016 and 2015, respectively, were \$6,673,000 and \$7,377,000 and are comprised entirely of net operating loss carryforwards. Based on the available objective evidence at December 31, 2016 and 2015, CEFI does not believe it is more likely than not that the net deferred tax assets will be fully realizable. Accordingly, CEFI has provided a full valuation allowance against its net deferred tax assets at December 31, 2016 and 2015. The valuation allowance decreased by \$704,000 and increased \$6,000 for the years ended December 31, 2016 and 2015, respectively.

As of December 31, 2016, CEFI had federal and state net operating loss carryforwards of approximately \$18,662,000 and \$5,628,000, respectively. If not utilized, the federal net operating loss carryforwards begin expiring in 2025. State net operating loss carryforwards began expiring in 2015; approximately \$9,400,000 and \$2,800,000 in state net operating loss carryforwards expired in the 2016 and 2015, respectively.

Utilization of net operating losses may be subject to a substantial annual limitation due to the "change of ownership" provisions of the Code Section 382. The annual limitation may result in the expiration of net operating losses before utilization.

**8. Commitments, Contingencies, and Concentrations of Risk**

***Premises and Equipment Lease Commitments***

The Foundation has a lease agreement for office space expiring in February 2019. Total rental expense for the years ended December 31, 2016 and 2015 was \$212,000 and \$212,000, respectively. Future minimum lease commitments under the noncancelable operating lease are (in thousands):

2017	\$ 246
2018	253
2019	<u>42</u>
Total	<u>\$ 541</u>

***Contingencies***

From time to time, the Foundation may be involved as a party to certain legal proceedings and other claims arising in the normal course of its business. While litigation and claims resolution are subject to many uncertainties and cannot be predicted with assurance, it is management's opinion that any resulting losses would not have a material effect on the Foundation's Consolidated Financial Statements.

Continued

**COLLEGE FUTURES FOUNDATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2016 and 2015

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**8. Commitments, Contingencies, and Concentrations of Risk, continued**

***Concentrations of Risk***

Financial instruments that potentially subject the Foundation to credit risk consist primarily of cash, cash equivalents, net receivables from unsettled trades, investments, and student loan receivables. The Foundation maintains cash and cash equivalents with two major financial institutions. At times, such amounts may exceed Federal Deposit Insurance Corporation (“FDIC”) limits.

The Foundation’s credit risk is inherent principally in its investments. Adverse economic conditions either nationwide or internationally may result in a reduction of the investments carrying amount. The maximum loss on the investments would be the carrying amount in the Consolidated Financial Statements.

As of December 31, 2016 and 2015, the Foundation held investments in excess of the Securities Investor Protection Corporation (“SIPC”) insurance limits. To address the risk of investments, the Foundation maintains a formal investment policy that sets out performance criteria, investment guidelines, and asset allocation guidelines, and requires review of the investment manager’s performance. Investments are managed by investment managers who have responsibility for investing the funds in various investment classes. An investment advisor is also utilized. This entire process is actively overseen by the Investment Committee of the Board.

The Foundation’s credit risk is also inherent in its student loans receivable. Adverse economic conditions either regionally or nationwide may result in an increase in student loan borrower defaults.

**9. Subsequent Events**

The Foundation evaluated subsequent events for recognition and disclosure through September 28, 2017, the date which these financial statements were issued. Management concluded that no material subsequent events have occurred since December 31, 2016 that required recognition or disclosure in the Consolidated Financial Statements.