

**Audited Consolidated Financial Statements**

**NATIONAL ASSOCIATION FOR MUSIC  
EDUCATION AND SUBSIDIARY**

*June 30, 2016*

# National Association for Music Education and Subsidiary

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## Independent Auditor's Report

To the Board of Directors  
National Association for Music Education and Subsidiary

We have audited the accompanying consolidated financial statements of the National Association for Music Education (NAfME) and Subsidiary (together referred as "the Association"), which comprise the consolidated statements of financial position as of June 30, 2016, the related consolidated statement of activities, functional expenses, and cash flows for the year then ended, and the related notes to the consolidated financial statements. The prior year summarized comparative information has been derived from NAfME's June 30, 2015 consolidated financial statements, which were audited by other auditors whose report thereon, dated September 29, 2015, expressed an unmodified opinion on those statements. We also audited the changes described in Note J that were applied to restate the 2015 financial statements. In our opinion, such changes are appropriate and have been properly applied.

### Management's Responsibility for the Consolidated 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.

### Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit 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 of 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 2016 consolidated financial statements referred to above present fairly, in all material respects, the financial position of the National Association for Music Education and Subsidiary as of June 30, 2016, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Washington, DC  
November 28, 2016

# National Association for Music Education and Subsidiary

## Consolidated Statements of Financial Position

<i>June 30,</i>	2016	(as restated) 2015
<b>Assets</b>		
Cash and cash equivalents	\$ 666,689	\$ 477,943
Investments	3,747,636	4,212,437
Accounts receivable - net	292,382	217,341
Inventory	136,454	168,838
Prepaid expenses	207,267	172,428
Investment, carried at lower of cost or market	339,178	339,178
Property and equipment, net	2,300,544	2,496,044
<b>Total assets</b>	<b>\$ 7,690,150</b>	<b>\$ 8,084,209</b>
<b>Liabilities and Net Assets</b>		
Liabilities		
Accounts payable and accrued expenses	\$ 919,035	\$ 900,143
Deferred revenue	2,051,790	2,156,835
Total liabilities	2,970,825	3,056,978
Net assets		
Unrestricted		
Undesignated	330,476	355,807
Board designated	4,297,155	4,556,122
Total unrestricted net assets	4,627,631	4,911,929
Temporarily restricted	16,559	40,167
Permanently restricted	75,135	75,135
Total net assets	4,719,325	5,027,231
Commitments and contingencies	-	-
<b>Total liabilities and net assets</b>	<b>\$ 7,690,150</b>	<b>\$ 8,084,209</b>

See notes to the consolidated financial statements.

# National Association for Music Education and Subsidiary

## Consolidated Statement of Activities

*Year Ended June 30, 2016 with Comparative Totals for 2015*

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	
				2016	(as restated) 2015
<b>Operating Activities</b>					
Revenue and support					
Membership dues and contributions	\$ 5,524,228	\$ -	\$ -	\$ 5,524,228	\$ 5,226,448
Meetings and conventions	1,070,138	-	-	1,070,138	805,052
Sale of inventories	571,220	-	-	571,220	516,958
Miscellaneous income	286,311	-	-	286,311	202,245
Advertising	250,536	-	-	250,536	321,326
Royalty income	212,176	-	-	212,176	167,788
Publication revenue	211,101	-	-	211,101	191,156
Contributions/donations	145,248	1,500	-	146,748	174,014
Sponsorships	52,550	-	-	52,550	72,846
Rent revenue	38,211	-	-	38,211	120,045
Grants and contracts	10,880	-	-	10,880	23,371
Investment income (loss)	(75,264)	2,106	-	(73,158)	161,037
Net assets released from restrictions	27,214	(27,214)	-	-	-
Total revenue and support	8,324,549	(23,608)	-	8,300,941	7,982,286
<b>Expenses</b>					
Program services					
Member and student experiences	1,781,583	-	-	1,781,583	1,657,334
Capacity building	1,004,533	-	-	1,004,533	917,587
Publications	904,414	-	-	904,414	1,024,041
Governance	498,184	-	-	498,184	440,812
Brand management	479,383	-	-	479,383	352,381
Give a Note Foundation	429,192	-	-	429,192	229,627
Business process	391,542	-	-	391,542	465,965
Strategic relationship development	279,912	-	-	279,912	306,698
Membership growth and development	244,615	-	-	244,615	243,170
Consultancy	131,999	-	-	131,999	200,552
Public policy	121,750	-	-	121,750	171,212
Professional development	50,730	-	-	50,730	43,569
Organizing	25,830	-	-	25,830	19,375
Total program services	6,343,667	-	-	6,343,667	6,072,323
Supporting services					
Administration	1,819,844	-	-	1,819,844	1,569,602
Technology and research	334,479	-	-	334,479	360,515
Fundraising and development	110,857	-	-	110,857	11,227
Total supporting services	2,265,180	-	-	2,265,180	1,941,344
Total expenses	8,608,847	-	-	8,608,847	8,013,667
<b>Change in net assets</b>	(284,298)	(23,608)	-	(307,906)	(31,381)
Net assets, beginning	4,911,929	40,167	75,135	5,027,231	5,058,612
<b>Net assets, end of year</b>	\$ 4,627,631	\$ 16,559	\$ 75,135	\$ 4,719,325	\$ 5,027,231

See notes to the consolidated financial statements.

# National Association for Music Education and Subsidiary

## Consolidated Statement of Functional Expenses Year Ended June 30, 2016 with Comparative Totals for 2015

	Program Services												Supporting Services					Total		
	Strategic		Member and			Membership			Business			Give a Note	Consultancy	Total	Fundraising and	Technology and	Total Supporting	(as restated)		
	Relationship	Capacity	Professional	Student	Public	Brand	Growth and	Organizing	Process	Publications	Governance	Foundation	(SMG)	Program	Administration	Development	Research	Services	2016	2015
Salaries	\$ 144,582	\$ 411,650	\$ 28,862	\$ 263,285	\$ 65,883	\$ 165,034	\$ 78,827	\$ 19,411	\$ 119,639	\$ 123,462	\$ 119,724	\$ 87,782	\$ 14,987	\$ 1,643,128	\$ 1,043,556	\$ 11,806	\$ -	\$ 1,055,362	\$ 2,698,490	\$ 2,464,645
Employee benefits	31,594	89,952	6,415	57,533	14,397	36,063	17,225	4,242	26,143	26,980	26,162	19,182	3,275	359,163	185,103	2,580		187,683	546,846	627,758
Travel	37,406	172,646	824	629,587	4,734	2,183	662		39	9,169	302,727	53,251	216	1,213,444	28,929	487		29,416	1,242,860	1,092,883
Annual professional dues	434	525	480	555		746		50		868		50		3,708	109	225		334	4,042	11,936
Membership dues expenses				1,695			6,569		8,382					16,646			45,000	45,000	61,646	59,921
Meetings, conventions and conferences	4,325	88,676	608	312,148	2,975					1,068	5,109	27,400		442,309	568	8,955		9,523	451,832	289,916
Cost of goods sold	33	2,708		80,013		60				20,869				103,683		50,998		50,998	154,681	176,405
Professional services/consultants	20,996	2,222		17,998		49,896				26,389	1,845	3,621	66,451	189,418	137,020	850	140,756	278,626	468,044	533,100
Outside support		2,000		3,000	2,000		2,280		28,026					37,306	486			486	37,792	5,533
Production and printing	3,081	27,523		125,970	8,184	8,599	27,666		11,848	562,649	570	12,504	2,413	791,007	8,463	3,136		11,599	802,606	900,619
Membership promotion and retention							62,148							62,148				-	62,148	61,895
Promotion, printing and publicity	1,150	8,314		17,480	30		11,674					248		38,896	4,637	10		4,647	43,543	27,948
Postage and mailing	109	9,894	9	46,616	1,700	301	7,688		67,839	86,817	2,193	3,342	85	226,593	6,543	7,343		13,886	240,479	232,811
Telephone				23		250					15			288				-	288	1,542
State sales tax				143			250							393				-	393	-
Bad debts		13,632		349		2,130						102		16,213		61		61	16,274	19,386
Management fees	300	44,792	1,447	95,941	5,000	146,131	6,892		63,376		15,762	10,506	41,054	431,201	129,305	10,074	42,501	181,880	613,081	374,793
Awards, scholaeships, and grants	740	369		6,262							960	1,047		9,378	141	8,000	2,000	10,141	19,519	16,151
Overhead	35,162	129,630	12,085	122,985	16,847	67,990	22,734	2,127	66,250	46,143	23,117	28,299	3,518	576,887	274,984	6,332	104,222	385,538	962,425	985,337
Other												181,858		181,858				-	181,858	131,088
<b>Total expenses</b>	<b>\$ 279,912</b>	<b>\$ 1,004,533</b>	<b>\$ 50,730</b>	<b>\$ 1,781,583</b>	<b>\$ 121,750</b>	<b>\$ 479,383</b>	<b>\$ 244,615</b>	<b>\$ 25,830</b>	<b>\$ 391,542</b>	<b>\$ 904,414</b>	<b>\$ 498,184</b>	<b>\$ 429,192</b>	<b>\$ 131,999</b>	<b>\$ 6,343,667</b>	<b>\$ 1,819,844</b>	<b>\$ 110,857</b>	<b>\$ 334,479</b>	<b>\$ 2,265,180</b>	<b>\$ 8,608,847</b>	<b>\$ 8,013,667</b>

# National Association for Music Education and Subsidiary

## Consolidated Statements of Cash Flows

<i>Year Ended June 30,</i>	2016	(as restated) 2015
<b>Cash flows from operating activities</b>		
Change in net assets	\$ (307,906)	\$ (31,381)
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Bad debt expense	16,274	19,386
Depreciation	232,728	248,727
Loss on disposition of fixed assets	-	8,221
Net loss (gain) on investments	143,144	(52,200)
Changes in assets and liabilities		
Accounts receivable	(91,315)	(54,482)
Inventory	32,384	(23,102)
Prepaid expenses	(34,839)	(66,528)
Accounts payable and accrued expenses	18,892	(87,537)
Deferred revenue	(105,045)	150,073
Total adjustments	212,223	142,558
Net cash (used in) provided by operating activities	(95,683)	111,177
<b>Cash flows from investing activities</b>		
Purchases of property and equipment	(37,228)	(20,421)
Proceeds from sales of investments	1,109,634	957,532
Purchases of investments	(787,977)	(805,946)
Proceeds from payment of loan advances	-	1,682
Net cash provided by investing activities	284,429	132,847
<b>Net increase in cash and cash equivalents</b>	<b>188,746</b>	<b>244,024</b>
Cash and cash equivalents, beginning of year	477,943	233,919
<b>Cash and cash equivalents, end of year</b>	<b>\$ 666,689</b>	<b>\$ 477,943</b>
<b>Significant non-cash investing and financing activities</b>		
Disposal of fully depreciated property and equipment	\$ -	\$ 220,463

See notes to the consolidated financial statements.

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

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### A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization: The National Association for Music Education ("NAfME"), a non-profit corporation located in Reston, Virginia, was organized April 12, 1907 under the laws of the state of Iowa for the specific purpose of the advancement of music education. NAfME serves as leader and spokesperson for music education in the United States. Its members are engaged in music teaching or other music education work at institutional levels from preschool through college and university. The goals of NAfME include comprehensive music programs in all schools, involvement of people of all ages in learning music, high-quality preparation of teachers, and the use of the most effective techniques and resources in music instruction.

On January 16, 2014, Solutions Music Group, LLC ("SMG"), an entity wholly owned by NAfME was formed as a limited liability company under the laws of the State of Virginia. SMG was formed to engage in the business of providing consulting services to individual schools, school districts, or organizations to develop music curricula or provide other related arts education services in the form of consulting. SMG had \$118,150 of revenue and \$146,360 of expense for the year ended June 30, 2016.

NAfME's significant programmatic areas include:

Governance: Governance covers the activities of the National Executive Board, its subdivisions, including but not limited to Councils, Societies, Committees, and Task Forces as well as the National Officers' work in fulfilling their responsibilities for the management, oversight, policies, and actions of NAfME. Most work is normally carried out through meetings, conferences, events, and other deliberations. This also includes the operation of the National Assembly, the Division Executive Boards, the relationship with federated state affiliates, and individual members.

Public policy: NAfME serves as the national voice for music education by providing, and seeking support for music programs at the federal, state, and local levels by advocating on Capitol Hill to protect sequential, standards-based school music for our nation's students. NAfME works in a variety of coalitions strengthening music education's public policy profile and increasing capacity for achieving the advocacy goals of our members. Most notably through the Music Education Policy Roundtable, a 30-member group coalition of music education advocacy organizations, NAfME pushes its federal legislative agenda and promotes the cause to influential elected officials. Most importantly, NAfME provides assistance to music educators on the ground by supplementing their grassroots advocacy efforts with resources and support.

Membership growth and development: The NAfME membership program is involved in producing and mailing membership promotion materials, mailing membership notices to NAfME's 135,000 plus members (including active, retired, pre-service music teachers and honor students), collection and tracking of national, state, and student chapter dues, and maintaining all membership records and data. Other important functions include the distribution of membership information and management of services designed to be of benefit to members.

Music Educators Journal/Teaching Music – periodicals: Magazines are published alternately each month, for a total of 10 times per year, dealing with all aspects of music and music education for the classroom, elementary through the university level. *Music Educators Journal* is a peer-reviewed publication and is published through Sage Publications. *Teaching Music* focuses on practical teaching information and news about the field and is published through In Tune publications.



# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

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### A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Member and student experiences: NAFME meetings and conventions are conducted to furnish in-service and pre-service professional development for music educators, to allow for the exchange of ideas among members and other teachers, and to facilitate the growth of knowledge of central issues in music education among professionals. The two principal association conventions are the NAFME National In-Service Conference and the Biennial Music Educators National Conference:

- NAFME National In-Service Conference is an annual event designed to provide members with opportunities for music education advocacy, intensive professional development, and performances.
- The Biennial Music Educators National Conference is designed with a special focus on research in music education and music teacher education. This meeting is held in the spring of each even-numbered year.

NAFME also sponsors or cosponsors other meetings designed to meet particular needs among the profession or to facilitate the business of NAFME. These meetings, which may be held in one geographic location or may be mediated through online "webinars", include:

- Meetings of the NAFME National Assembly (officers from the Federated State Associations, the geographic divisions of NAFME, and NAFME Societies and Councils).
- Meetings of the National Executive Board.
- Meetings and conventions held independently by the Federated State Associations, but to which NAFME sends Board Officers.
- Meetings and conventions held by the geographic divisions of NAFME, hosted by a Federated State Association, and cosponsored by NAFME.
- Informational seminars on a variety of special topics (e.g., nonprofit tax requirements and budgeting, copyright issues, curriculum) for specific subgroups of NAFME or specific groups served by NAFME.

Scholarship and grant programs: NAFME administers scholarship programs that support and advance the mission to encourage the study and making of music by all; these include the Shannon Kelly Kane Fund and the Harley Scholarship Fund. The Shannon Kelly Kane Fund provides two \$1,000 scholarships annually and Harley Scholarship Fund provides one scholarship. Four grants are awarded annually as part of the NAFME Tri-M Music Honor Society Chapter of the Year program. Grants are to be used for musically enriching experience that benefits the school/chapter. Two \$1,000 grants are awarded to the Chapter of the Year in the Senior and Junior Division; Runner-Ups are awarded \$800 for Senior Division and \$400 for Junior Division. Criteria for selection are on the Tri-M website. NAFME also, from time to time, provides small grants for music education related research. These grants are distributed and monitored by the Society for Research in Music Education.

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

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### A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Miscellaneous programs: NAFME's other programs include: book publications, contests and competitions, resource development, cultural and community partnerships, electronic communications, information resources, Music in Our Schools Month ("MIOSM"), production and promotion, research publications and other periodicals and resource shops.

Tri-M: Tri-M is an international music honor society for middle school and high school students. Its focus is to encourage music educators to recognize and motivate musical and personal achievement in their students.

Principles of consolidation: The consolidated financial statements include the accounts of NAFME and the Solutions Music Group, LLC (together referred as "the Association"). Significant intra-entity accounts and transactions have been eliminated in consolidation.

Income tax status: NAFME is exempt from federal income taxes under the provision of Section 501(c)(3) of the Internal Revenue Code ("IRC"). NAFME is subject to income taxes on unrelated business income, as defined by the Internal Revenue Service ("IRS"). SMG is a single member limited liability company and since it is a disregarded entity for income tax purposes, SMG's activities are reported on the tax return of its sole member, NAFME.

Basis of accounting: The consolidated financial statements have been prepared on the accrual basis of accounting. Revenues, other than contributions, are recognized when earned; expenses are recorded when the obligation is incurred. Contributions are recorded as unrestricted or temporarily restricted support depending upon the existence and the nature of any donor restrictions. When a 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 restriction.

Use of estimates: The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Cash and cash equivalents: For purposes of reporting cash flows, NAFME considers all highly liquid investments purchased with an original maturity of three months or less that are not included in the investment portfolio to be cash equivalents.

Investments: Investments are stated at fair value. Gains and losses, including changes in fair value, are reported in the consolidated statement of activities as increases or decreases in net assets.

Investments carried at the lower of cost or market: NAFME has holdings in preferred shares of a private company. These investments are considered alternative investments, as the stocks are not traded in an established market with published values. NAFME accounts for these investments at the lower of cost or market. If an investment is determined to be permanently impaired, it is written down to its net realizable value. The net realizable value then becomes the investment's new basis.

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

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### A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Accounts receivable: Accounts receivable are reported net of an allowance for doubtful accounts. Management's estimate of the allowance is based on historical collection experience and a review of the current status of accounts receivable. Receivables are charged to allowance when deemed uncollectible. It is reasonably possible that management's estimate of the allowance will change. Allowance for doubtful accounts at June 30, 2016 and 2015 was \$52,764 and \$39,220, respectively.

Inventory: Inventory consists of specialty items and publications and are valued at the lower of cost or market. Cost is determined on a first-in, first-out basis net of obsolescence. Allowance for obsolete inventory at June 30, 2016 and 2015 was \$29,244 and \$26,963, respectively.

Property and equipment and depreciation: Property and equipment are recorded at cost. Depreciation is computed on a straight-line basis over the estimated useful lives of each asset. The Association capitalizes all property and equipment purchased with a cost of \$500 or more. Depreciation expense for the years ended June 30, 2016 and 2015 was \$232,728 and \$248,727, respectively.

Deferred revenue: Deferred revenue primarily consists of subscription fees and membership dues revenue received in advance of the period in which they are earned.

Net assets: These consolidated financial statements present net assets, revenue, expenses, gains and losses based on the existence of donor-imposed restrictions. Accordingly, net assets and the changes therein are classified as follows:

Unrestricted: Net assets that are not subject to donor-imposed stipulations. Revenues from sources other than contributions and investment income are reported as increases in unrestricted net assets. Designated net assets consist of unrestricted funds set aside for specific purposes by action of NAFME. NAFME's policies set as a goal that NAFME maintain a reserve account equaling or exceeding 100% of the annual operating budget, and is to be used as designated by the board.

Temporarily Restricted: Temporarily restricted net assets are subject to donor-imposed stipulations that may or will be met by the actions of NAFME and/or passage of time.

Permanently Restricted: Permanently restricted net assets are subject to donor-imposed stipulations that they be maintained permanently by NAFME. Generally, the investment income is temporarily restricted until appropriated for expenditure.

Revenue recognition: Revenues are reported as increases in unrestricted net assets unless the use of the related assets is limited by donor-imposed restrictions. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulations that are not met in the same reporting period or by operation of law.

Membership revenue: Membership dues and subscription fees are recognized as revenue over the period of membership. Membership revenue related to future periods is recorded as deferred revenue in the accompanying consolidated statement of financial position.

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

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### A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Contributions: Contributions received are recorded as permanently restricted, temporarily restricted, or unrestricted revenue, depending on the existence and/or nature of any donor restrictions. All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods or restricted for specific purposes are reported as temporarily restricted support that increases those net asset classes. Non-cash and in-kind contributions are recorded as revenue at fair value of the items contributed.

Functional allocation of expenses: The costs of providing various programs and other activities have been summarized on a functional basis in the consolidated statement of activities. Direct costs associated with identifiable expenses are charged to program and supporting services. Accordingly, certain costs have been allocated among the departments, programs, and supporting services benefited. Administration expenses include those expenses that are not directly identifiable with any other specific function but that provide for the overall support and direction of NAFME.

Advertising: Advertising costs are charged to activities when incurred. Advertising expense during the years ended June 30, 2016 and 2015 was \$34,447 and \$18,540, respectively, and is included in promotion, printing, and publicity on the consolidated statement of functional expenses.

Reclassification: Certain reclassifications have been made to the 2015 balances to conform to the 2016 presentation. Specifically, a gross up between in-house advertising revenue and expense of \$73,520 was removed.

Subsequent events: Subsequent events have been evaluated through November 28, 2016, which is the date the consolidated financial statements were available to be issued.

### B. CONCENTRATIONS

Credit risk: NAFME maintains demand deposits with commercial banks and money market funds with financial institutions. At times, certain balances held within these accounts may not be fully guaranteed or insured by the U.S. federal government. The uninsured portions of cash and money market accounts are backed solely by the assets of the underlying institution. Therefore, the failure of an underlying institution could result in financial loss to NAFME.

Market risk: NAFME also invests funds in a professionally managed portfolio of marketable securities. Such investments are exposed to market and credit risks. Therefore, NAFME's investments may be subject to significant fluctuations in fair value. As a result, the investment balances reported in the accompanying consolidated financial statements may not be reflective of the portfolio's value during subsequent periods.

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

### C. INVESTMENTS

In accordance with U.S. generally accepted accounting principles, NAFME uses the following prioritized input levels to measure fair value of financial instruments. The input levels used for valuing financial instruments are not necessarily an indication of risk.

Level 1 – Observable inputs that reflect quoted prices for identical assets or liabilities in active markets such as stock quotes;

Level 2 – Includes inputs other than level 1 that are directly or indirectly observable in the marketplace such as yield curves or other market data;

Level 3 – Unobservable inputs which reflect the reporting entity's assessment of the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk such as bid/ask spreads and liquidity discounts.

The following is a summary of input levels used to determine fair values, measured on a recurring basis, at June 30,:

<b>2016</b>	<b>Total</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>
Investments, at fair value				
Closed end mutual funds	\$ 3,543,495	\$ 3,543,495	\$ -	\$ -
Corporate bonds	114,141	114,141		
	<u>3,657,636</u>	<u>\$ 3,657,636</u>	<u>\$ -</u>	<u>\$ -</u>
Investments, at cost				
Certificates of deposit	<u>90,000</u>			
	<u><b>\$ 3,747,636</b></u>			

<b>2015</b>	<b>Total</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>
Investments, at fair value				
Closed end mutual funds	\$ 4,016,468	\$ 4,016,468	\$ -	\$ -
Corporate bonds	111,969	111,969		
	<u>4,128,437</u>	<u>\$ 4,128,437</u>	<u>\$ -</u>	<u>\$ -</u>
Investments, at cost				
Certificates of deposit	<u>84,000</u>			
	<u><b>\$ 4,212,437</b></u>			

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

### C. INVESTMENTS - CONTINUED

The following summarizes the investment return and its classification in the consolidated statement of activities for the year ended June 30,:

	<b>2016</b>	<b>2015</b>
Interest and dividends	\$ 69,986	\$ 108,837
Net (loss) gain on investments	<u>(143,144)</u>	<u>52,200</u>
	<b><u>\$ (73,158)</u></b>	<b><u>\$ 161,037</u></b>

### D. PROPERTY AND EQUIPMENT

Acquisitions of property and equipment equal to or greater than \$500 are capitalized at cost. Furniture and equipment are depreciated using the straight-line method over an estimated useful life of the assets, ranging from three to seven years, while building and improvements are depreciated or amortized over estimated useful lives of ten to forty years.

Property and equipment consisted of the following at June 30,:

	<b>2016</b>	<b>2015</b>
Building and improvements	\$ 2,323,736	\$ 2,323,736
Furniture and equipment	1,954,604	1,917,375
Land	<u>1,069,089</u>	<u>1,069,089</u>
	5,347,429	5,310,200
Less accumulated depreciation	<u>(3,046,885)</u>	<u>(2,814,156)</u>
	<b><u>\$ 2,300,544</u></b>	<b><u>\$ 2,496,044</u></b>

### E. TEMPORARILY RESTRICTED NET ASSETS

Net assets were released from restriction by satisfying the program restrictions. Temporarily restricted net asset activity consisted of the following at June 30,:

	<b>2015</b>	<b>Additions</b>	<b>Investment Gain</b>	<b>Released from Restrictions</b>	<b>2016</b>
Harley scholarship fund	\$ 9,692	\$ -	\$ 451	\$ -	\$ 10,143
Kane scholarship fund	5,261	1,500	1,655	(2,000)	6,416
SMG all in program	25,214	-	-	(25,214)	-
	<b><u>\$ 40,167</u></b>	<b><u>\$ 1,500</u></b>	<b><u>\$ 2,106</u></b>	<b><u>\$ (27,214)</u></b>	<b><u>\$ 16,559</u></b>

  

	<b>2014</b>	<b>Additions</b>	<b>Investment Gain</b>	<b>Released from Restrictions</b>	<b>2015</b>
Harley scholarship fund	\$ 9,242	\$ -	\$ 450	\$ -	\$ 9,692
Kane scholarship fund	2,079	3,532	1,650	(2,000)	5,261
SMG all in program	-	108,860	-	(83,646)	25,214
	<b><u>\$ 11,321</u></b>	<b><u>\$ 112,392</u></b>	<b><u>\$ 2,100</u></b>	<b><u>\$ (85,646)</u></b>	<b><u>\$ 40,167</u></b>

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

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### F. PERMANENTLY RESTRICTED NET ASSETS

Permanently restricted net assets consisted of the “Kane Scholarship Fund” and the “Harley Scholarship Fund”, both of which are endowment funds. Investment income from these endowment funds is restricted for donor specified purposes. As required by accounting principles generally accepted in the United States of America, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions

Interpretation of relevant law: The Virginia General Assembly issued the Virginia Uniform Prudent Management of Institutional Funds Act ("UPMIFA"). Unless there are explicit donor instructions, this law gives the Boards of non-profit organizations the flexibility to determine appropriate use of endowment principal and related investment income. In accordance with UPMIFA, NAFME Board should consider the following factors in determining a prudent use of investment income and endowment principal:

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

The Board of NAFME continually reviews its policy regarding the use of endowment funds, and makes necessary modifications to the Investment Policy.

Return objectives and risk parameters: NAFME has adopted investment and spending policies for donor-restricted endowment assets that attempt to generate a series of cash withdrawals that grow with inflation for use in programs supported by its endowment while seeking to maintain the purchasing power of the donor restricted endowment assets. Donor-restricted endowment assets include those assets of donor restricted funds that NAFME must hold in perpetuity or for donor-specified period(s). Under this policy, as approved by the Board, the endowment assets are invested in accordance with sound investment practices emphasizing long-term investment fundamentals. It is recognized that short-term market fluctuations may cause variations in account performance. NAFME accepts a low level of risk in investment return.

Strategies employed for achieving objectives: To satisfy its long-term rate of return objectives, NAFME relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized/unrealized) and current yield (interest/dividends). NAFME targets a diversified asset allocation in order to satisfy its cash withdrawal and long-term rate-of-return objectives.

Funds with deficiencies: From time to time, the fair value of assets associated with donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires NAFME to retain as a fund of perpetual duration. In accordance with accounting principles generally accepted in the United States of America, deficiencies of this nature are reported in unrestricted net assets. There were no such deficiencies as of June 30, 2016 and 2015.

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

### F. PERMANENTLY RESTRICTED NET ASSETS - CONTINUED

Spending policies: In order to support the operating activities of NAFME, the investment policy approves appropriation of the endowment funds income for the donor designated purpose in the year(s) when sufficient accumulated investment income is realized to make a meaningful scholarship or grant. In establishing this policy, NAFME considered the long-term expected return on its endowment. Accordingly, over the long-term, NAFME expects the current spending policy to allow its endowment to grow, consistent with its objective to maintain the purchasing power of the endowment assets held in perpetuity as well as to provide additional real growth through new gifts and investment return.

Endowment net assets: Endowment net assets consisted of the following as of June 30, 2016:

	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Kane Scholarship Fund	\$ 6,416	\$ 65,395	\$ 71,811
Harley Scholarship Fund	10,143	9,740	19,883
	<b>\$ 16,559</b>	<b>\$ 75,135</b>	<b>\$ 91,694</b>

Endowment net assets: Endowment net assets consisted of the following as of June 30, 2015:

	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Kane Scholarship Fund	\$ 5,261	\$ 65,395	\$ 70,656
Harley Scholarship Fund	9,692	9,740	19,432
	<b>\$ 14,953</b>	<b>\$ 75,135</b>	<b>\$ 90,088</b>

Endowment activity: Changes in endowment net assets consisted of the following for the years ended June 30, 2016 and 2015:

	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Endowment net assets, June 30, 2014	\$ 11,321	\$ 75,135	\$ 86,456
Net investment return	2,100		2,100
Contributions	3,532		3,532
Appropriations	(2,000)		(2,000)
<b>Endowment net assets, June 30, 2015</b>	<b>14,953</b>	<b>75,135</b>	<b>90,088</b>
Net investment return	2,106		2,106
Contributions	1,500		1,500
Appropriations	(2,000)		(2,000)
<b>Endowment net assets, June 30, 2016</b>	<b>\$ 16,559</b>	<b>\$ 75,135</b>	<b>\$ 91,694</b>



# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

### G. PENSION PLANS AND RETIREMENT BENEFITS

NAfME has a defined contribution retirement plan covering all employees who work over one thousand hours in the plan year following one month of service. On an annual basis, NAfME contributes 7% of participants' eligible compensation to the defined contribution retirement plan. For the years ended June 30, 2016 and 2015, net amounts contributed after forfeitures were \$139,187 and \$166,062, respectively.

NAfME sponsors a 403(b) plan for eligible employees. Employees are eligible to participate in the plan upon their date of hire. Participants may contribute a portion of their eligible compensation to the plan, subject to limits approved by the Internal Revenue Service. Participants are immediately vested in their own contributions. NAfME does not make matching contributions to the 403(b) plan.

Accrued vacation and sick leave: Depending on length of service and other factors, NAfME's employees are entitled to paid vacation time. At June 30, 2016 and 2015, the accrual for vacation leave was \$213,285 and \$293,584, respectively, and is included in accounts payable and accrued expenses in the consolidated statement of financial position at June 30, 2016 and 2015.

Effective July 1, 2009, employees in good standing are entitled to be paid sick leave upon employment termination, depending on meeting certain age and years of service requirements. At June 30, 2016 and 2015, accrued sick leave was \$171,991 and \$119,053, respectively, and is included in accounts payable and accrued expenses in the consolidated statement of financial position at June 30, 2016 and 2015.

### H. COMMITMENTS AND CONTINGENCIES

NAfME has various leases for automobiles and equipment which are classified as operating leases with lease terms expiring through February 15, 2019. The leases require monthly payments ranging from \$329 to \$3,712 over the term of the lease. Total rent expense for all operating leases for the years ended June 30, 2016 and 2015 was \$99,633 and \$115,210, respectively, and is included in overhead expenses on the consolidated statement of functional expenses.

Future minimum lease payments under the non-cancelable operating leases as follows:

Year Ending June 30,	
2017	\$ 73,890
2018	29,782
2019	3,156
	<hr/>
	\$ 106,828

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

### H. COMMITMENTS AND CONTINGENCIES - CONTINUED

NAfME leases office and storage space to National Art Education Association and Metronome Software LLC under operating agreements with lease terms expiring through July 31, 2020. The leases require monthly payments ranging from \$350 to \$5,649 over the lease term. No security deposits were received for these leases. Additionally, NAfME rents parking spaces to Access Bank on a month-to-month basis which can be terminated by either party at any time. For the years ended June 30, 2016 and 2015, total rent revenue was \$38,211 and \$120,045, respectively.

Future minimum rentals pursuant to the lease agreements and rental arrangements are as follows:

Year Ending June 30,	
2017	\$ 8,100
2018	8,100
2019	8,100
2020	8,100
	<hr/>
	<b>\$ 32,400</b>

### I. RELATED PARTIES

The Give a Note Foundation (the "Foundation") is a related party of NAfME. The Foundation was formed by the leadership of NAfME as a separate corporation, and obtained a separate 501(c)(3) exemption status with the Internal Revenue Service. Although economic interest exists between the Foundation and NAfME, the Foundation maintains a board that is independent from that of NAfME, and therefore, does not consolidate its assets, liabilities, net assets, or activities with those of NAfME.

On April 23, 2012 and on June 30, 2015, NAfME entered into cost sharing agreements with the Foundation, whereby the Foundation may share use of certain office equipment, facilities and staff service. According to the terms of the agreements, the Foundation shall reimburse NAfME, for such costs, on a monthly basis, except for the first two years of each respective agreement, in which NAfME has agreed to forgive all related costs incurred by the Foundation. For the years ended June 30, 2016 and 2015, total donated costs were \$181,850 and \$131,088, respectively.

# National Association for Music Education and Subsidiary

## Notes to the Consolidated Financial Statements

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### J. RESTATEMENT OF PRIOR YEAR FINANCIAL STATEMENTS

The June 30, 2015 financial statements have been restated from amounts originally reported to reflect the correction of two separate errors that resulted in the overstatement of revenue and the overstatement in unrestricted net assets. NAFME's net assets and change in net assets were restated as follows:

Net assets as of July 1, 2015, as previously reported	\$ 5,125,047
Effect upon net assets due to restatement	<u>(97,816)</u>
Net assets as of July 1, 2015, as restated	<u>\$ 5,027,231</u>
Change in net assets as previously reported for the year ended June 30, 2015	\$ 66,435
Effect upon change in net assets due to restatement	<u>(97,816)</u>
Change in net assets for the year ended June 30, 2015, as restated	<u>\$ (31,381)</u>