

Audited Consolidated Financial Statements

**NATIONAL ASSOCIATION FOR MUSIC
EDUCATION AND SUBSIDIARY**

June 30, 2017

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 statement of financial position as of June 30, 2017, and the related consolidated statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the National Association for Music Education and Subsidiary as of June 30, 2017, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited the National Association for Music Education and Subsidiary's 2016 consolidated financial statements, and our report dated November 28, 2016, expressed an unmodified opinion on those audited consolidated financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2016 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

Tate & Tryon

Washington, DC
November 17, 2017

National Association for Music Education and Subsidiary

Consolidated Statements of Financial Position

June 30,	2017	2016
Assets		
Cash and cash equivalents	\$ 545,356	\$ 666,689
Investments	4,085,991	3,747,636
Accounts receivable - net	152,625	292,382
Inventory	106,437	136,454
Prepaid expenses	339,739	207,267
Investment, carried at lower of cost or market	339,178	339,178
Property and equipment, net	2,109,634	2,300,544
Total assets	\$ 7,678,960	\$ 7,690,150
Liabilities and Net Assets		
Liabilities		
Accounts payable and accrued expenses	\$ 1,067,953	\$ 919,035
Deferred revenue	2,028,941	2,051,790
Total liabilities	3,096,894	2,970,825
Net assets		
Unrestricted		
Undesignated	(254,585)	330,476
Board designated	4,745,067	4,297,155
Total unrestricted net assets	4,490,482	4,627,631
Temporarily restricted	16,449	16,559
Permanently restricted	75,135	75,135
Total net assets	4,582,066	4,719,325
Commitments and contingencies	-	-
Total liabilities and net assets	\$ 7,678,960	\$ 7,690,150

See notes to the consolidated financial statements.

National Association for Music Education and Subsidiary

Consolidated Statement of Activities Year Ended June 30, 2017 with Comparative Totals for 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	
				2017	2016
Operating Activities					
Revenue and support					
Membership dues and contributions	\$ 5,398,673	\$ -	\$ -	\$ 5,398,673	\$ 5,524,228
Meetings and conventions	828,675	-	-	828,675	1,070,138
Sale of inventories	546,985	-	-	546,985	571,220
Investment income (loss)	413,365	1,890	-	415,255	(73,158)
Publication revenue	258,715	-	-	258,715	211,101
Royalty income	245,270	-	-	245,270	212,176
Advertising	194,060	-	-	194,060	250,536
Sponsorships	115,118	-	-	115,118	52,550
Grants and contracts	73,862	-	-	73,862	10,880
Miscellaneous income	260,343	-	-	260,343	286,311
Contributions/donations	23,957	-	-	23,957	146,748
Rent revenue	19,940	-	-	19,940	38,211
Net assets released from restrictions	2,000	(2,000)	-	-	-
Total revenue and support	8,380,963	(110)	-	8,380,853	8,300,941
Expenses					
Program services					
Member and student experiences	1,830,354	-	-	1,830,354	1,781,583
Brand management	858,580	-	-	858,580	479,383
Capacity building	811,898	-	-	811,898	1,004,533
Publications	757,984	-	-	757,984	904,414
Governance	409,169	-	-	409,169	498,184
Business process	402,708	-	-	402,708	391,542
Strategic relationship development	255,904	-	-	255,904	279,912
Give a Note Foundation	447,359	-	-	447,359	429,192
Membership growth and developmer	146,786	-	-	146,786	244,615
Public policy	116,795	-	-	116,795	121,750
Professional development	106,966	-	-	106,966	50,730
Consultancy	36,838	-	-	36,838	131,999
Organizing	26,490	-	-	26,490	25,830
Total program services	6,207,831	-	-	6,207,831	6,343,667
Supporting services					
Administration	1,976,139	-	-	1,976,139	1,819,844
Technology and research	211,362	-	-	211,362	334,479
Fundraising and development	122,780	-	-	122,780	110,857
Total supporting services	2,310,281	-	-	2,310,281	2,265,180
Total expenses	8,518,112	-	-	8,518,112	8,608,847
Change in net assets	(137,149)	(110)	-	(137,259)	(307,906)
Net assets, beginning	4,627,631	16,559	75,135	4,719,325	5,027,231
Net assets, end of year	\$ 4,490,482	\$ 16,449	\$ 75,135	\$ 4,582,066	\$ 4,719,325

See notes to the consolidated financial statements.

National Association for Music Education and Subsidiary

Consolidated Statement of Functional Expenses Year Ended June 30, 2017 with Comparative Totals for 2016

	Program Services											Supporting Services				Total				
	Member and Student Experiences	Brand Management	Capacity Building	Publications	Governance	Business Process	Strategic Relationship Development	Give a Note Foundation	Membership Growth and Development	Public Policy	Professional Development	Consultancy (SMG)	Organizing	Total Program	Administration	Technology and Research	Fundraising and Development	Total Supporting Services	2017	2016
Salaries	\$ 200,874	\$ 193,840	\$ 332,102	\$ 128,560	\$ 85,620	\$ 142,818	\$ 125,648	\$ 99,446	\$ 47,844	\$ 57,035	\$ 47,021	\$ 7,839	\$ 17,087	\$ 1,485,734	\$ 657,046	\$ -	\$ 30,889	\$ 687,935	\$ 2,173,669	\$ 2,698,490
Employee benefits	45,982	44,375	76,026	29,431	19,601	32,694	28,764	22,766	10,953	13,057	10,764	1,795	3,911	340,119	150,367	113	7,071	157,551	497,670	546,846
Travel	744,514	2,038	167,790	20	258,143	3	34,658	48,316	4,919	3,888	1,651	802	1,025	1,267,767	12,389		15,527	27,916	1,295,683	1,242,860
Annual professional dues	747	2,338	775	375	2,352	112	1,243	1,842	595	500	180	50		11,109	5,727			5,727	16,836	4,042
Membership dues expenses	4,768	895				8,386			9,200		62			23,311		45,000		45,000	68,311	61,646
Meetings, conventions and conferences	356,950	395	68,457		15,483		3,426	2,330	1,950	3,500	316			452,807	12,259		202	12,461	465,268	451,832
Cost of goods sold	124,899			919			250							126,068			10,108	10,108	136,176	154,681
Professional services/consultants	2,020	170,061	3,150	17,535	4,658		26,427	290		22,000				271,141	664,770		29,386	694,156	965,297	468,044
Outside support	16,000		0			68		765	5,000					21,833	144			144	21,977	37,792
Production and printing	64,549	118	4,212	445,289	1,085	20,658	222	12,776	5,424	963	1,465	75		556,836	2,507			2,507	559,343	802,606
Membership promotion and retention									33,583					33,583				-	33,583	62,148
Promotion, printing and publicity	6,359	3,714	25,042	295	1,324		1,015	476	12,826		308			51,359	17,631			17,631	68,990	43,543
Postage and mailing	61,066	335	1,433	91,246	1,313	74,379	1,287	7,562	638	424	2,437			242,120	7,799		4,484	12,283	254,403	240,479
Telephone														-				-	-	288
State sales tax				3,164										3,164				-	3,164	393
Bad debts														-		3,975		3,975	3,975	16,274
Management fees	80,620	360,425	20,488		1,553	42,848	263	4,897			19,429			530,523	250,601	46,577	12,971	310,149	840,672	613,081
Awards, scholaeships, and grants	33,026		307				995	7,822	300					42,450		2,000		2,000	44,450	19,519
Overhead	87,980	80,046	112,116	41,150	18,037	80,742	31,706	40,470	13,554	15,428	23,333	1,277	4,467	550,306	194,899	113,697	12,142	320,738	871,044	962,425
Other								197,601						197,601				-	197,601	181,858
Total expenses	\$ 1,830,354	\$ 858,580	\$ 811,898	\$ 757,984	\$ 409,169	\$ 402,708	\$ 255,904	\$ 447,359	\$ 146,786	\$ 116,795	\$ 106,966	\$ 36,838	\$ 26,490	\$ 6,207,831	\$ 1,976,139	\$ 211,362	\$ 122,780	\$ 2,310,281	\$ 8,518,112	\$ 8,608,847

National Association for Music Education and Subsidiary

Consolidated Statements of Cash Flows

<i>Year Ended June 30,</i>	2017	2016
Cash flows from operating activities		
Change in net assets	\$ (137,259)	\$ (307,906)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Bad debt expense	3,975	16,274
Depreciation	210,424	232,728
Net (gain) loss on investments	(330,571)	143,144
Changes in assets and liabilities		
Accounts receivable	135,782	(91,315)
Inventory	30,017	32,384
Prepaid expenses	(132,472)	(34,839)
Accounts payable and accrued expenses	148,918	18,892
Deferred revenue	(22,849)	(105,045)
Total adjustments	43,224	212,223
Net cash used in operating activities	(94,035)	(95,683)
Cash flows from investing activities		
Purchases of property and equipment	(19,514)	(37,228)
Proceeds from sales of investments	1,416,122	1,109,634
Purchases of investments	(1,423,906)	(787,977)
Net cash (used in) provided by investing activities	(27,298)	284,429
Net (decrease) increase in cash and cash equivalents	(121,333)	188,746
Cash and cash equivalents, beginning of year	666,689	477,943
Cash and cash equivalents, end of year	\$ 545,356	\$ 666,689

See notes to the consolidated financial statements.

National Association for Music Education and Subsidiary

Notes to the Consolidated Financial Statements

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 \$9,150 and \$118,150 of revenue and \$41,388 and \$146,360 of expense for the years ended June 30, 2017 and 2016, respectively.

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

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

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 Code. 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

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 was \$52,764 for both June 30, 2017 and 2016.

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, 2017 and 2016 was \$23,703 and \$29,244, 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, 2017 and 2016 was \$210,424 and \$232,728, 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, 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, which 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

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, 2017 and 2016 was \$36,760 and \$34,447, respectively, and is included in promotion, printing, and publicity in the consolidated statement of functional expenses.

Subsequent events: Subsequent events have been evaluated through November 17, 2017, 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,:

2017	Total	Level 1	Level 2	Level 3
Investments, at fair value				
Closed end mutual funds	\$ 3,884,655	\$ 3,884,655	\$ -	\$ -
Corporate bonds	111,336	111,336		
	<u>3,995,991</u>	<u>\$ 3,995,991</u>	<u>\$ -</u>	<u>\$ -</u>
Investments, at cost				
Certificates of deposit	<u>90,000</u>			
	<u>\$ 4,085,991</u>			

2016	Total	Level 1	Level 2	Level 3
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>\$ 3,747,636</u>			

National Association for Music Education and Subsidiary

Notes to the Consolidated Financial Statements

C. INVESTMENTS - CONTINUED

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

	2017	2016
Interest and dividends	\$ 84,684	\$ 69,986
Net gain (loss) on investments	330,571	(143,144)
	\$ 415,255	\$ (73,158)

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,:

	2017	2016
Building and improvements	\$ 2,323,736	\$ 2,323,736
Furniture and equipment	1,974,117	1,954,604
Land	1,069,089	1,069,089
	5,366,942	5,347,429
Less accumulated depreciation	(3,257,308)	(3,046,885)
	\$ 2,109,634	\$ 2,300,544

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,:

	2016	Additions	Investment Gain	Released from Restrictions	2017
Harley scholarship fund	\$ 10,143	\$ -	\$ 393	\$ -	\$ 10,536
Kane scholarship fund	6,416	-	1,497	(2,000)	5,913
	\$ 16,559	\$ -	\$ 1,890	\$ (2,000)	\$ 16,449

	2015	Additions	Investment Gain	Released from Restrictions	2016
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)	-
	\$ 40,167	\$ 1,500	\$ 2,106	\$ (27,214)	\$ 16,559

National Association for Music Education and Subsidiary

Notes to the Consolidated Financial Statements

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, 2017 and 2016.

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, 2017:

	Temporarily Restricted	Permanently Restricted	Total
Kane Scholarship Fund	\$ 5,913	\$ 65,395	\$ 71,308
Harley Scholarship Fund	10,536	9,740	20,276
	\$ 16,449	\$ 75,135	\$ 91,584

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

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

Endowment activity: Changes in endowment net assets consisted of the following for the years ended June 30, 2017 and 2016:

	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, June 30, 2015	\$ 14,953	\$ 75,135	\$ 90,088
Net investment return	2,106		2,106
Contributions	1,500		1,500
Appropriations	(2,000)		(2,000)
Endowment net assets, June 30, 2016	16,559	75,135	91,694
Net investment return	1,890		1,890
Appropriations	(2,000)		(2,000)
Endowment net assets, June 30, 2017	\$ 16,449	\$ 75,135	\$ 91,584

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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, 2017 and 2016, net amounts contributed after forfeitures were \$150,834 and \$139,187, 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 Code. 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, 2017 and 2016, the accrual for vacation leave was \$225,489 and \$213,285, respectively, and is included in accounts payable and accrued expenses in the consolidated statement of financial position at June 30, 2017 and 2016. 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, 2017 and 2016, accrued sick leave was \$191,425 and \$171,991, respectively, and is included in accounts payable and accrued expenses in the consolidated statement of financial position at June 30, 2017 and 2016.

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, 2017 and 2016 was 103,824 and \$99,633, respectively, and is included in overhead expenses in the consolidated statement of functional expenses.

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

Year Ending June 30,

2018	\$	29,782
2019		<u>3,156</u>
	\$	<u>32,938</u>

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H. COMMITMENTS AND CONTINGENCIES - CONTINUED

NAfME leased storage space to Access National Bank under an operating agreement which expired March 2017. The lease required monthly payments of \$2,106 over the lease term. Additionally, NAfME rents parking spaces to Access National Bank on a month-to-month basis which can be terminated by either party at any time. For the years ended June 30, 2017 and 2016, total rent revenue was \$19,940 and \$38,211, respectively.

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, 2017 and 2016, total donated costs were \$197,601 and \$181,850, respectively.