

**THE BAPTIST FOUNDATION OF ALABAMA**

Financial Statements

December 31, 2016 and 2015

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**LOCAL FIRM.**  
**NATIONAL KNOWLEDGE.**  
**GLOBAL REACH.**

## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
The Baptist Foundation of Alabama  
Montgomery, Alabama

We have audited the accompanying financial statements of The Baptist Foundation of Alabama, which comprise the statements of financial position as of December 31, 2016 and 2015, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 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 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the 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 financial statements referred to above present fairly, in all material respects, the financial position of The Baptist Foundation of Alabama as of December 31, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Barfield, Murphy, Shank & Smith, LLC*

Birmingham, Alabama  
July 10, 2017

**THE BAPTIST FOUNDATION OF ALABAMA**  
 Statements of Financial Position  
 December 31, 2016 and 2015

	<b>2016</b>	<b>2015</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 316,418	\$ 244,201
Accounts and bequests receivable	593,534	45,438
Investments	51,961,674	50,970,493
Investments held in charitable remainder trusts and gift annuities	145,886	148,400
Investments held for others	189,030,213	175,479,000
Property and equipment, net	1,989,734	2,030,537
	\$ 244,037,459	\$ 228,918,069
 <b>Liabilities and Net Assets</b>		
Accounts payable and accrued expenses	\$ 592,583	\$ 518,006
Liabilities associated with charitable remainder trusts and gift annuities	7,934	39,161
Investments held for others	189,030,213	175,479,000
	189,630,730	176,036,167
 <b>Net assets</b>		
Unrestricted	24,455,972	23,330,167
Temporarily restricted	5,162,556	5,014,646
Permanently restricted	24,788,201	24,537,089
	54,406,729	52,881,902
	\$ 244,037,459	\$ 228,918,069

See notes to financial statements.

**THE BAPTIST FOUNDATION OF ALABAMA**  
 Statements of Activities  
 Years ended December 31, 2016 and 2015

	2016	2015
<b>Change in Unrestricted Net Assets</b>		
Support and revenue		
Contributions	\$ 943,558	\$ 234,447
Cooperative program	129,678	360,832
Investment and administrative fee income	929,889	975,535
Trust and other income	443,463	43,943
Interest and dividend income	421,872	400,495
Realized gain on investments	522,226	197,271
Unrealized gain (loss) on investments	264,513	(897,624)
Net assets released from restriction	986,594	1,033,846
	4,641,793	2,348,745
Functional expenses		
Program services		
Disbursements for beneficiaries and others	1,076,229	1,217,116
Trust administration	804,749	759,433
Eldercare	279,803	231,979
General and administrative	631,570	614,139
Development	723,637	746,578
	3,515,988	3,569,245
Change in unrestricted net assets	1,125,805	(1,220,500)
<b>Change in Temporarily Restricted Net Assets</b>		
Contributions	44,543	15,035
Interest and dividend income	343,455	326,150
Realized gain on investments	720,949	145,237
Unrealized gain (loss) on investments	25,557	(468,708)
Net assets released from restriction	(986,594)	(1,033,846)
	147,910	(1,016,132)
Change in temporarily restricted net assets	147,910	(1,016,132)
<b>Change in Permanently Restricted Net Assets</b>		
Contributions	220,128	78,944
Change in value of assets and liabilities associated with charitable remainder trusts and gift annuities	30,984	5,160
	251,112	84,104
Change in permanently restricted net assets	251,112	84,104
Change in net assets	1,524,827	(2,152,528)
Net assets - beginning of year	52,881,902	55,034,430
Net assets - end of year	\$ 54,406,729	\$ 52,881,902

See notes to financial statements.

**THE BAPTIST FOUNDATION OF ALABAMA**

Statements of Cash Flows

Years ended December 31, 2016 and 2015

	2016	2015
<b>Operating Activities</b>		
Change in net assets	\$ 1,524,827	\$ (2,152,528)
Adjustments to reconcile change in net assets to net cash used in operating activities		
Depreciation	88,109	97,564
Loss on disposal of property and equipment	-	1,284
Investment income	(765,327)	(726,645)
Realized gain on investments	(1,243,175)	(342,508)
Unrealized (gain) loss on investments	(290,070)	1,366,332
Contributions restricted for long-term purposes	(220,128)	(78,944)
Changes in operating assets and liabilities		
Accounts and bequests receivable	(548,096)	1,704
Accounts payable and accrued expenses	74,577	62,935
Value of assets and liabilities associated with charitable remainder trusts and gift annuities	(28,713)	(3,161)
Net cash used in operating activities	(1,407,996)	(1,773,967)
<b>Investing Activities</b>		
Proceeds from sale of investments	3,727,765	3,348,264
Purchases of investments	(2,420,374)	(1,593,303)
Proceeds from disposal of property and equipment	-	10,000
Purchases of property and equipment	(47,306)	(64,331)
Net cash provided by investing activities	1,260,085	1,700,630
<b>Financing Activities</b>		
Proceeds from contributions restricted for investment in permanent endowment	220,128	78,944
Net cash provided by financing activities	220,128	78,944
Net increase in cash and cash equivalents	72,217	5,607
Cash and cash equivalents - beginning of year	244,201	238,594
Cash and cash equivalents - end of year	\$ 316,418	\$ 244,201

See notes to financial statements.

## THE BAPTIST FOUNDATION OF ALABAMA

Notes to Financial Statements

December 31, 2016 and 2015

### NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### **Nature of Activities**

The Baptist Foundation of Alabama (the Foundation) is a not-for-profit corporation, organized pursuant to the requirements of the Alabama Nonprofit Corporation Act. The Foundation was organized for the purposes of encouraging the making of gifts, benefactions, and other donations for the advancement, promotion, endowment, and maintenance of all institutions and agencies, whether religious, educational, eleemosynary, missionary, promotional, literary, or informational, recognized by and under the direction of either the Alabama Baptist State Convention (the Convention) or its affiliated local churches and district associations in carrying out their enterprises and undertakings.

#### **Basis of Accounting**

The financial statements of the Foundation have been prepared in accordance with accounting principles generally accepted in the United States of America. In preparing the financial statements, management evaluated subsequent events through July 10, 2017, the date the financial statements were available to be issued.

#### **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 that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### **Basis of Financial Statement Presentation**

The Foundation reports contributions held for specified beneficiaries for which the Foundation has not been granted variance power as an asset and a liability. In addition, the Foundation reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

*Unrestricted Net Assets* are those currently available at the direction of the Board for use in the Foundation's operations, invested in property and equipment, or designated by the Board of Directors or management to function as endowments.

*Temporarily Restricted Net Assets* are those which are stipulated by donors for specific operating purposes and those that are time restricted.

*Permanently Restricted Net Assets* are those contributed with donor restrictions requiring they be held in perpetuity.

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

**Basis of Financial Statement Presentation - Continued**

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, restricted net assets are reclassified to unrestricted net assets and are reported in the statements of activities as net assets released from restriction.

**Cash and Cash Equivalents**

The Foundation considers all instruments with an original maturity of three months or less to be cash and cash equivalents. Cash equivalents consist of money market securities stated at fair value which approximates cost. Cash and cash equivalents are maintained at financial institutions and, at times, balances may exceed federally insured limits. These amounts represent actual account balances held by financial institutions at the end of the period, and unlike the balances reported in the financial statements, the account balances do not reflect timing delays inherent in reconciling items such as outstanding checks and deposits in transit. The Foundation has never experienced any losses related to these balances.

**Receivables**

The Foundation reports receivables at net realizable value. Management determines the allowance for doubtful accounts based on historical losses and current economic conditions. On a continuing basis, management analyzes delinquent receivables and, once these receivables are determined to be uncollectible, they are written off through a charge against an existing allowance or against earnings. Based on management's review, no allowance for doubtful accounts was considered necessary at December 31, 2016 or 2015.

The Foundation has elected to participate in the Deepwater Horizon Court-Supervised Settlement Program related to the oil spill in the Gulf of Mexico on April 20, 2010, and has filed and received approval of its claim totaling \$472,786 (less legal fees totaling \$70,918). At December 31, 2016, the Foundation recorded a net receivable totaling \$401,868 related to the claim, which was received in January 2017 and is included in other income (under unrestricted support and revenue) in the accompanying statements of activities.

**Property and Equipment**

Property and equipment are carried at cost or, if donated, the approximate fair value at the date of donation, less accumulated depreciation and include expenditures which substantially increase the useful lives of existing property and equipment. Maintenance, repairs and minor renovations are charged to income as incurred. When property and equipment are retired or otherwise disposed of, the related costs and accumulated depreciation are removed from the respective accounts and any gain or loss on the disposition is credited or charged to income. The Foundation provides for depreciation of property and equipment using the straight-line method designed to amortize costs over the following estimated useful lives: buildings and improvements, 7 to 39 years; furniture and fixtures, 3 to 10 years; and automobiles, 5 years.



## THE BAPTIST FOUNDATION OF ALABAMA

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

### NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

#### Investments

Investments in debt and equity securities with readily determinable fair values are recorded at fair market value. Investments without readily determinable fair values are recorded at cost, or if impaired, at estimated realizable value. The Foundation's investments as of December 31, 2016 and 2015 consisted primarily of funds invested in fixed-income and equity securities. Expenses relating to investment income, including custodial fees and investment advisory fees, totaled \$161,827 and \$164,722 during the years ended December 31, 2016 and 2015, respectively, and have been netted against investment income in the accompanying statements of activities.

Many of the Foundation's investments are converted to units of common funds administered by the Foundation. These common funds include the assets of charitable trusts and other specified types of assets authorized by law to be jointly invested, as well as general endowment funds. Investments held for others include obligations consisting of units of these common funds, as well as other specific identified assets. These assets are segregated from general assets of the Foundation. The common funds that are managed by the Foundation are exempt from registration requirements of both state and federal securities law.

The units of common funds included in the Foundation's investments are reported at their net asset value, equal to the Foundation's pro-rata share of the total fair value of the underlying securities comprising the common funds.

The Foundation invests in several hedge funds for further diversification of its common funds. Hedge fund investments are more illiquid than traditional investments, often taking three to twelve months to redeem, pending the completion of the final year-end close of the fund.

The Board of Directors and management of the Foundation have interpreted the State Prudent Management of Institutional Funds Act (SPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the endowment funds and (b) the value of subsequent contributions to the endowment funds and accumulations to the permanent endowment funds made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment funds that are not classified in permanently restricted net assets are classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, the Foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: (1) the duration and preservation of the fund, (2) the purposes of the Foundation and the donor-restricted endowment funds, (3) general economic conditions, (4) the possible effect of inflation and deflation, (5) the expected total return from income and the appreciation of investments, (6) other resources of the Foundation, and (7) the investment policies of the Foundation.

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

**Investments - Continued**

The Investment Committee is charged with the fiduciary responsibility of preserving and augmenting the value of the endowments, included in investments, thereby sustaining the ability to generate financial support to further the mission of the Foundation. The Foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under this policy, as approved by the Board of Directors, the endowment assets are invested in a manner that is intended to produce results that cover the spending policy payout percentage (4.25% or 2.80% at December 31, 2016 and 2015), administrative expenses, plus the rate of inflation while assuming a moderate level of investment risk.

**Irrevocable Trust Agreements**

The Foundation's right to remainder interests under irrevocable trust agreements are recognized as temporarily or permanently restricted contributions upon receipt of assets funding such agreements. The Foundation also recognizes contributions related to certain trusts that do not provide for specific beneficiaries and trust agreements that grant the Foundation variance power as related to the trust assets and/or income.

**Charitable Remainder Trusts and Gift Annuities**

The Foundation has various charitable gift annuity and charitable remainder trust agreements under which the donor makes a charitable donation, the remainder interest of which is irrevocably dedicated to specified beneficiaries. These agreements require periodic payments to the donor, or their designated non-charitable beneficiary (the annuitant), of a specified sum until the death of the annuitant. The objective in investing the assets received from the donor is to provide income and growth to meet the periodic annuity payments required. At the death of the annuitant, the remaining balances are disbursed as designated by the donor in the agreement.

The Foundation also has certain charitable remainder trusts and gift annuities under which the ultimate beneficiary is the Foundation. The assets associated with these agreements are recorded as assets of the Foundation. The present value of the anticipated annuity to be paid is reflected as a liability of the Foundation and the excess amounts are reported as temporarily and permanently restricted net assets. Charitable remainder trust and gift annuity contracts in which the Foundation has a beneficial interest totaled \$145,886 and \$148,400 at December 31, 2016 and 2015, respectively. The liability associated with these charitable remainder trusts and gift annuities is estimated as the present value of expected future cash outflows, over the terms of the agreements, using discount rates of 6.00% to 8.00% and applicable mortality tables and totaled \$7,934 and \$39,161 at December 31, 2016 and 2015, respectively.

## **THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

### **NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

#### **Investments Held for Others**

Investments held for others include resources held and managed by the Foundation in a fiduciary capacity for their respective beneficiaries. The Foundation is authorized to serve as trustee or agent for any institution or agency affiliated directly or indirectly with the Alabama Baptist State Convention. In addition, the Foundation serves as trustee for certain charitable trusts through which, for a period of time, trust income is distributed to the grantor or other non-charitable beneficiaries, and all, or a predetermined percentage, of the trust assets are designated for a qualified charitable purpose. In addition, the Foundation serves as executor for various estates and custodial accounts that provide for a portion, or all, of the estate's assets to be given to an institution or agency affiliated directly or indirectly with the Alabama Baptist State Convention, the Foundation, or any other organization which has a primary purpose that is consistent with the purpose of the Convention or Foundation. Distributions of assets to the Foundation, if any, received through these estates are recorded as contributions at fair value when the estate is declared valid.

Investments held for others also include investments of various charitable gift annuities and charitable remainder trusts. As provided in the governing instruments, the assets and liabilities of these trusts and annuities are restricted for the exclusive benefit of their respective beneficiaries.

#### **Concentration of Credit Risk**

The Foundation maintains various investment accounts with a national investment firm to facilitate the investment, trading, and safekeeping of the various trusts' assets. In management's opinion, the safekeeping of these assets is adequately insured by the Securities Investor Protection Corporation (SIPC) and through supplemental insurance provided by the investment firm.

The Foundation investment allocations are predetermined by the Investment Committee and communicated to its investment brokerage firm. At December 31, 2015, approximately 13% of total investments were invested in one mutual fund.

#### **Income Taxes**

The Foundation is organized as a not-for-profit corporation under the Alabama Nonprofit Corporation Act. Additionally, the Foundation has been granted tax-exempt status by the Internal Revenue Service for income tax purposes. The Foundation is subject to unrelated business income tax (UBIT) only if it engages in activities subject to the UBIT regulations.

Tax positions are initially recognized in the financial statements when it is more likely than not that the position will be sustained upon examination by the tax authorities. The Foundation had no uncertain tax positions that qualify for either recognition or disclosure in the financial statements as of December 31, 2016 or 2015 based on an assessment of many factors including experience and interpretations of applicable tax laws.

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

**Fair Value**

The established framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. Fair value is the price the Foundation would expect to receive to sell an asset or pay to transfer a liability in an orderly transaction with a market participant at the measurement date. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described as follows:

Level 1 - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Foundation has the ability to access.

Level 2 - Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets.
- Quoted prices for identical or similar assets or liabilities in inactive markets.
- Inputs other than quoted prices that are observable for the asset or liability.
- Inputs which are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used maximize the use of observable inputs and minimize the use of unobservable inputs.

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 2 - INVESTMENTS**

Investments consisted of the following at December 31, 2016:

	<u>Fair Value</u>	<u>Cost</u>	<u>Unrealized Appreciation (Depreciation)</u>
Cash and cash equivalents	\$ 24,568,562	\$ 24,568,562	\$ -
Fixed income securities	63,219,722	63,653,760	(434,038)
Limited partnerships	68,171,159	58,326,751	9,844,408
Mutual funds	51,115,385	47,856,387	3,258,998
Marketable equity securities	27,659,241	24,418,919	3,240,322
Mortgages and notes receivable	1,320,648	1,320,648	-
Commercial real estate	284,800	284,800	-
Residential real estate	1,629,665	1,253,361	376,304
Timber and timberland	1,578,000	1,536,309	41,691
Other assets	1,075,033	664	1,074,369
Accrued income	515,558	515,558	-
	<u>\$ 241,137,773</u>	<u>\$ 223,735,719</u>	<u>\$ 17,402,054</u>

Included in the accompanying statements of financial position under the following captions:

Investments	\$ 51,961,674
Investments held in charitable remainder trusts and gift annuities	145,886
Investments held for others	189,030,213
	<u>\$ 241,137,773</u>

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 2 - INVESTMENTS - Continued**

Investments consisted of the following at December 31, 2015:

	<u>Fair Value</u>	<u>Cost</u>	<u>Unrealized Appreciation</u>
Cash and cash equivalents	\$ 17,699,317	\$ 17,699,317	\$ -
Fixed income securities	61,856,513	61,615,085	241,428
Limited partnerships	71,565,832	62,129,277	9,436,555
Mutual funds	57,533,598	53,877,137	3,656,461
Marketable equity securities	10,827,754	10,202,100	625,654
Mortgages and notes receivable	1,589,460	1,589,460	-
Commercial real estate	655,000	655,000	-
Residential real estate	1,712,013	1,302,022	409,991
Timber and timberland	2,215,000	2,123,001	91,999
Other assets	541,951	660	541,291
Accrued income	401,455	401,455	-
	<u>\$ 226,597,893</u>	<u>\$ 211,594,514</u>	<u>\$ 15,003,379</u>

Included in the accompanying statements of financial position under the following captions:

Investments	\$ 50,970,493
Investments held in charitable remainder trusts and gift annuities	148,400
Investments held for others	175,479,000
	<u>\$ 226,597,893</u>

Transactions affecting assets held for others are as follows:

	<u>2016</u>	<u>2015</u>
Balance - beginning of year	\$ 175,479,000	\$ 180,977,524
Deposits and additions	17,270,239	9,581,211
Interest, dividends and amortization	3,198,581	3,092,571
Realized and unrealized gains (losses)	6,067,224	(3,870,116)
Disbursements for beneficiaries and other withdrawals	(12,984,831)	(14,302,190)
Balance - end of year	<u>\$ 189,030,213</u>	<u>\$ 175,479,000</u>

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 3 - ENDOWMENT**

The Foundation's endowment consists of individual funds established for a variety of purposes. The endowment includes donor-restricted endowment funds and funds designated by the Board of Directors to function as endowments. Net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The following provides a description of restrictions placed on the net assets represented in the Foundation's endowment funds at December 31:

	<u>Type</u>	<u>2016</u>	<u>2015</u>
Permanently restricted	A	\$ 24,788,201	\$ 24,537,089
Temporarily restricted	B	4,127,638	4,038,810
Unrestricted (quasi-endowments)	C	11,743,690	12,081,702
		<u>\$ 40,659,529</u>	<u>\$ 40,657,601</u>

Type A restrictions represent the portion of perpetual endowment funds that are required to be retained permanently either by explicit donor stipulation or by SPMIFA. Type B restrictions represent the portion of perpetual endowment funds subject to a time restriction under SPMIFA. Type C restrictions are the portion of the Foundation's endowment funds designated by the Board of Directors or management to function as endowments (quasi-endowments). The principal portion of unrestricted endowments may be expended at any time by the decision of the Board of Directors or management.

The fair value of assets associated with individual donor-restricted endowment funds may fall below the level necessary to maintain the purchasing power of the original gift plus additions. Deficiencies of this nature are reported in unrestricted net assets and totaled \$739,280 and \$878,066 at December 31, 2016 and 2015, respectively. These deficiencies resulted from unfavorable market fluctuations and continued appropriation for certain programs that were deemed prudent by the Foundation's Board of Directors.

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 3 - ENDOWMENT - Continued**

Changes in endowment net assets consisted of the following during the years ended December 31, 2016 and 2015:

	<b>Unrestricted</b>	<b>Temporarily Restricted</b>	<b>Permanently Restricted</b>	<b>Total</b>
Endowment net assets - December 31, 2014	\$ 13,087,667	\$ 5,074,704	\$ 24,452,985	\$ 42,615,356
Contributions	236,420	20,442	78,944	335,806
Interest and dividend income	192,390	433,220	-	625,610
Realized and unrealized losses, net	(182,147)	(316,411)	-	(498,558)
Appropriation of endowment assets for expenditure	(1,252,628)	(1,173,145)	-	(2,425,773)
Change associated with charitable remainder trusts and gift annuities	-	-	5,160	5,160
Endowment net assets - December 31, 2015	12,081,702	4,038,810	24,537,089	40,657,601
Contributions	195,622	23,665	220,128	439,415
Interest and dividend income	188,495	439,436	-	627,931
Realized and unrealized gains, net	392,399	738,091	-	1,130,490
Appropriation of endowment assets for expenditure	(1,114,528)	(1,112,364)	-	(2,226,892)
Change associated with charitable remainder trusts and gift annuities	-	-	30,984	30,984
Endowment net assets - December 31, 2016	<u>\$ 11,743,690</u>	<u>\$ 4,127,638</u>	<u>\$ 24,788,201</u>	<u>\$ 40,659,529</u>

The Foundation expects its endowment funds, over time, to provide an average rate of return of approximately 6.00% to 8.00% annually. Actual returns in any given year may vary from this amount. To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.



**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 3 - ENDOWMENT - Continued**

The Foundation's policy of appropriating for distribution each year is 4.25% of its endowment fund's average fair value over the prior 16 quarters through the calendar year end preceding the calendar year in which the distribution is planned. The percentage is decreased to 2.80% for endowments that have declined and are consequently considered deficient. In establishing this policy, the Foundation considered the long-term expected return on its endowment. Accordingly, over the long term, the Foundation expects the current spending policy to allow its endowment to grow at the rate of inflation, currently an average of 2.00% to 3.00% annually, consistent with the Foundation's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investments.

**NOTE 4 - PROPERTY AND EQUIPMENT**

Property and equipment consisted of the following at December 31:

	<u>2016</u>	<u>2015</u>
Land	\$ 696,687	\$ 696,687
Buildings and improvements	1,658,421	1,658,421
Furniture and fixtures	476,305	453,233
Automobiles	228,504	204,270
	<u>3,059,917</u>	<u>3,012,611</u>
Less accumulated depreciation	1,070,183	982,074
	<u>\$ 1,989,734</u>	<u>\$ 2,030,537</u>

**NOTE 5 - TEMPORARILY AND PERMANENTLY RESTRICTED NET ASSETS**

Temporarily and permanently restricted net assets were available for the following purposes at December 31:

	<u>2016</u>	<u>2015</u>
Temporarily restricted		
Eldercare	\$ 248,082	\$ 210,028
Church loans	786,834	765,808
Scholarships	1,623,147	1,573,760
Other endowments	2,504,493	2,465,050
	<u>\$ 5,162,556</u>	<u>\$ 5,014,646</u>
Permanently restricted		
Endowments	<u>\$ 24,788,201</u>	<u>\$ 24,537,089</u>

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 6 - FAIR VALUE**

The following is a description of the valuation methodologies used for assets measured at fair value. There were no changes in the methodologies used during the years ended December 31, 2016 or 2015.

- *Cash and Cash Equivalents*: Valued at amortized cost which approximates fair value.
- *Investment Securities*: Valued based on quoted market prices, when available, or market prices provided by recognized broker dealers. Securities traded in the over-the-counter market and listed securities for which no sale was reported on that date are stated at the last quoted bid price. Government-sponsored enterprises and commercial paper are stated at cost plus accrued interest, which approximates fair value.
- *Limited Partnerships*: Valued based on the net asset value of the investment (or its equivalent) without further adjustment (unless management determines that the net asset value is deemed to be not reflective of fair value) since the limited partnerships are investment companies that have calculated net asset value per share in accordance with the specialized accounting guidance for investment companies. The fair value of the Foundation's investments in limited partnerships generally represents the amount the Foundation would expect to receive if it were to liquidate its investment in the partnerships excluding any redemption charges that may apply.
- *Mortgages and Notes Receivable*: Valued based upon estimated cash flows adjusted for credit risk which are discounted using an interest rate appropriate for the maturity of the applicable loan.
- *Real Estate*: Valued based upon appraisals, which utilize inputs derived from or corroborated by observable market data.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although management believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 6 - FAIR VALUE - Continued**

The following table sets forth, by level within the fair value hierarchy, the Foundation's investment assets at fair value, as of December 31, 2016 and 2015:

	<b>Fair Value</b>	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
<b>December 31, 2016</b>				
Cash and cash equivalents	\$ 24,568,562	\$ 24,568,562	\$ -	\$ -
Fixed income securities	63,219,722	63,219,722	-	-
Limited partnerships	68,171,159	-	27,506,447	40,664,712
Mutual funds	51,115,385	51,115,385	-	-
Marketable equity securities	27,659,241	27,659,241	-	-
Mortgages and notes receivable	1,320,648	-	1,320,648	-
Commercial real estate	284,800	-	284,800	-
Residential real estate	1,629,665	-	1,629,665	-
Timber and timberland	1,578,000	-	1,578,000	-
Other assets	1,075,033	465	1,074,568	-
Accrued income	515,558	515,558	-	-
	<u>\$ 241,137,773</u>	<u>\$ 167,078,933</u>	<u>\$ 33,394,128</u>	<u>\$ 40,664,712</u>
<b>December 31, 2015</b>				
Cash and cash equivalents	\$ 17,699,317	\$ 17,699,317	\$ -	\$ -
Fixed income securities	61,856,513	61,856,513	-	-
Limited partnerships	71,565,832	-	37,857,674	33,708,158
Mutual funds	57,533,598	57,533,598	-	-
Marketable equity securities	10,827,754	10,827,754	-	-
Mortgages and notes receivable	1,589,460	-	1,589,460	-
Commercial real estate	655,000	-	655,000	-
Residential real estate	1,712,013	-	1,712,013	-
Timber and timberland	2,215,000	-	2,215,000	-
Other assets	541,951	496	541,455	-
Accrued income	401,455	401,455	-	-
	<u>\$ 226,597,893</u>	<u>\$ 148,319,133</u>	<u>\$ 44,570,602</u>	<u>\$ 33,708,158</u>

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 6 - FAIR VALUE - Continued**

The following table sets forth a summary of changes in the fair value of the Foundation's level-three investment assets for the years ended December 31:

	<u>2016</u>	<u>2015</u>
Balance - beginning of year	\$ 33,708,158	\$ 39,448,559
Purchases	7,074,517	2,991,499
Withdrawals	-	-
Unrealized (losses) gains		
Included in change in net assets	(23,609)	204,286
Included in change in investments held for others	(94,354)	454,701
Transfers out	-	(9,390,887)
Balance - end of year	<u>\$ 40,664,712</u>	<u>\$ 33,708,158</u>

The Foundation invests in limited partnerships and limited liability companies, which are commonly known as alternative investments. These alternative investments make indirect and direct investments in complex financial instruments whose value is derived from an underlying security, commodity, or asset. These investments may contain elements of both credit and market risk. Such risks include, but are not limited to, limited liquidity, need for direct oversight, dependence on key individuals, emphasis on speculative investments, and transparency of portfolio composition. Because alternative investments are not readily marketable, their value is subject to some degree of uncertainty and, therefore, may differ from the value that would have been used if a ready market for such investments existed.

Management determines the classification of alternative investments within the fair value hierarchy based on the Foundation's ability to redeem the investments at net realizable value at the measurement date. If the Foundation has the ability to redeem its investment at net asset value per share (or its equivalent) at the measurement date, the investment asset is included within level two of the fair value hierarchy. Otherwise, the investment asset is included within level three of the fair value hierarchy.

The Foundation's policy is to recognize transfers in and transfers out of the valuation levels as of the beginning of the reporting period. There were no transfers between valuation levels during the year ended December 31, 2016. During the year ended December 31, 2015, the fair value of the Foundation's investment in the Undiscovered Value Fund, Ltd. was transferred out of level three and into level two within the fair value hierarchy as the lock-up provision expired during the year, and thus, the Fund is redeemable at net asset value per share (or its equivalent) at December 31, 2015 and 2016.

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 6 - FAIR VALUE - Continued**

The following table summarizes information related to the redemption rights of alternative investments held by the Foundation at December 31, 2016 and 2015:

<b>Investment</b>	<b>Fair Value</b>	<b>Redemption Frequency</b>	<b>Redemption Notice Period</b>	<b>Lock-up Provision</b>
December 31, 2016				
Courage Special Situations Offshore Fund, Ltd.				
Class A Series	\$ 2,622,017	Quarterly	60 days	Rolling three years
Class C Series	2,041,065	Quarterly	60 days	Rolling three months
Courage Credit Opportunity Offshore Fund III, L.P.	3,775,431	Quarterly	60 days	Rolling three years
Private Advisors Hedged Equity Fund (QP), Ltd.	17,232,002	Quarterly	65 days	n/a
Undiscovered Value Fund, Ltd.	15,508,965	Quarterly	65 days	Initial year of investment
RMS Forest Growth Fund III, LP	10,165,217	n/a	n/a	Life of the partnership (15 years)
U.S. Farming Realty Trust II, LP	8,577,970	n/a	n/a	Life of the partnership (10 years)
Ceres Farms, LLC	8,235,673	Annually	5 months	Rolling one year
PEF II, LLC	12,819	Unknown	Unknown	Unknown
	<u>\$ 68,171,159</u>			
December 31, 2015				
Courage Special Situations Offshore Fund, Ltd.				
Class A Series	\$ 1,903,783	Quarterly	60 days	Rolling three years
Class C Series	2,467,942	Quarterly	60 days	Rolling three months
Courage Credit Opportunity Offshore Fund III, L.P.	1,828,014	Quarterly	60 days	Rolling three years
Private Advisors Hedged Equity Fund (QP), Ltd.	17,176,759	Quarterly	65 days	n/a
Undiscovered Value Fund, Ltd.	9,562,502	Quarterly	65 days	Initial year of investment
RMS Forest Growth Fund III, LP	10,912,459	n/a	n/a	Life of the partnership (15 years)
U.S. Farming Realty Trust II, LP	8,614,923	n/a	n/a	Life of the partnership (10 years)
SSI Convertible Income Fund, LP	11,091,853	Quarterly	30 days	n/a
Ceres Farms, LLC	7,981,037	Annually	5 months	Rolling one year
PEF II, LLC	26,560	Unknown	Unknown	Unknown
	<u>\$ 71,565,832</u>			

## THE BAPTIST FOUNDATION OF ALABAMA

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

### NOTE 6 - FAIR VALUE - Continued

The following is a description of the significant investment strategies of the Foundation's alternative investments:

- *Courage Special Situations Offshore Fund, Ltd.*: Achieve significant capital gains while minimizing risk associated with the broad equity markets, focusing on event driven, special situations and value oriented investment opportunities.
- *Courage Credit Opportunities Offshore Fund III, L.P.*: Achieve investment returns while emphasizing distressed investments in financially troubled companies, including those of companies that may, or have, become involved in reorganization or bankruptcy proceedings.
- *Private Advisors Hedged Equity Fund (QP), Ltd.*: Seek long-term capital appreciation above historical equity returns, over a full market cycle, with volatility that is lower than that of the equity market and returns that demonstrate a low correlation to both the equity and fixed income markets.
- *Undiscovered Value Fund, Ltd.*: Seek long-term capital appreciation above historical equity returns over a full market cycle with volatility that is lower than that of the equity market.
- *RMS Forest Growth Fund III, LP*: Invest in timberland properties and/or long-term timberland leaseholds or project ventures which invest in timberland properties or long-term timberland leaseholds.
- *U.S. Farming Realty Trust II, LP*: Achieve short-term distributable cash income and long-term capital appreciation through investments in a diversified portfolio of farmlands in the United States of America to be leased to farming operators.
- *SSI Convertible Income Fund, LP*: Invest in, hold, sell, trade and otherwise deal in securities consisting principally, but not solely, of stocks, bonds, notes, bills, exchange-traded funds, participating and convertible debt instruments, and other securities and instruments that are traded publicly and privately in the "144A" market. The Fund also seeks to profit from declines in the value of securities and hedge its positions by short selling and through other strategies.
- *Ceres Farms, LLC*: Open-ended investment fund whose objective is to generate an attractive total return through the acquisition and management of farmland in the midwestern United States of America.

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 6 - FAIR VALUE - Continued**

The net asset value of alternative investments is dependent upon the value of the investments held by each limited partnership, which are valued using both observable and unobservable inputs. The following table sets forth the valuation approaches, unobservable inputs, and range of inputs of the Foundation's level-three investment assets as reported in the audited financial statements of the limited partnerships at December 31, 2016:

Investment	Fair Value	Valuation Approaches	Unobservable Input	Range of Inputs (Average)
Courage Special Situations Offshore Fund, Ltd.	\$ 4,663,071	Market, comparable transactions	EBITDA multiple	10.00 to 11.00
Courage Credit Opportunities Offshore Fund III, L.P.	3,775,431	Income, discounted cash flows Market, comparable transactions	n/a n/a	n/a n/a
Undiscovered Value Fund, Ltd.	5,247,350	Market, comparable transactions	n/a	n/a
RMS Forest Growth Fund III, LP	10,165,217	Income, discounted cash flows	Discount rate Percentage change in future timber pricing Cost of management (annual cost per acre)	4.75% to 5.75% (5.30%) -13.00% to 28.20% (2.55%) \$3.93 to \$42.64 (\$19.66)
U.S. Farming Realty Trust II, LP	8,577,970	Market, comparable transactions	Price per acre Comparability adjustments Income, discounted cash flows	\$769 to \$20,000 (\$10,385) -25% to 676% (325.50%) Annualized net operating income per acre Capitalization rate
Ceres Farms, LLC	<u>8,235,673</u> <u>\$ 40,664,712</u>	Real estate appraisals	n/a	n/a

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 6 - FAIR VALUE - Continued**

The following table sets forth the valuation approaches, unobservable inputs, and range of inputs of the Foundation's level-three investment assets as reported in the audited financial statements of the limited partnerships at December 31, 2015:

Investment	Fair Value	Valuation Approaches	Unobservable Input	Range of Inputs (Average)	
Courage Special Situations Offshore Fund, Ltd.	\$ 4,371,725	Income, discounted cash flows	Discount rate	11.50%	
			Growth rate	2.50% to 3.50%	
		Market, comparable companies	Revenue multiple	2.50 to 4.00	
			EBITDA multiple	8.00 to 12.00	
			Market, comparable transactions	Revenue multiple	3.50 to 4.50
EBITDA multiple	13.00 to 14.00				
Courage Credit Opportunities Offshore Fund III, L.P.	1,828,014	Income, discounted cash flows	n/a	n/a	
		Market, comparable companies	n/a	n/a	
		Market, comparable transactions	n/a	n/a	
RMS Forest Growth Fund III, LP	10,912,459	Income, discounted cash flows	Discount rate	5.00% to 5.50% (5.40%)	
			Percentage change in future timber pricing	-14.00% to 24.80% (2.63%)	
		Market, comparable transactions	Cost of management (annual cost per acre)	\$9.97 to \$50.17 (\$20.39)	
			U.S. Farming Realty Trust II, LP	Price per acre	\$1,903 to \$15,200 (\$8,552)
				Comparability adjustments	-76.00% to 35.00% (20.50%)
		Income, discounted cash flows	Annualized net operating income per acre	\$163 to \$494 (\$329)	
			Capitalization rate	2.25% to 3.82% (3.04%)	
			Ceres Farms, LLC	<u>7,981,037</u>	Real estate appraisals
	<u>\$ 33,708,158</u>			n/a	

**NOTE 7 - RELATED PARTY TRANSACTIONS**

The Foundation is affiliated with the Alabama Baptist State Convention, and receives significant administrative support through the Cooperative Program of the State Board of Missions. The State Board of Missions provided \$129,678 and \$360,832 in administrative support to the Foundation during the years ended December 31, 2016 and 2015, respectively. The Foundation also administers certain assets for the State Board of Missions. As of December 31, 2016 and 2015, the Foundation held and managed funds for the State Board of Missions valued at \$10,137,890 and \$9,719,296, respectively. The Board of Directors of the Foundation elected to make contributions of undesignated earnings to the Cooperative Program administered by the State Board of Missions totaling \$166,737 and \$168,391 during each of the years ended December 31, 2016 and 2015.



**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 8 - RETIREMENT PLAN**

The Foundation makes contributions for its employees to a defined contribution retirement plan maintained by GuideStone Financial Resources, an entity affiliated with the Southern Baptist Convention. The Foundation makes non-matching contributions to employee accounts equal to 10% of the employee's salary. The Foundation matches employee contributions, up to 5% of the employee's salary, based on years of service. Employees are eligible for participation in the plan on the first day of employment and are fully vested on their fifth year of service. Contributions to the plan totaled \$163,422 and \$159,171 during the years ended December 31, 2016 and 2015, respectively.

The Foundation also sponsors a deferred compensation plan. Deferred compensation expense totaled \$50,000 during each of the years ended December 31, 2016 and 2015. The deferred compensation liability totaled \$564,877 and \$486,897 at December 31, 2016 and 2015, respectively.

**NOTE 9 - COMMITMENTS AND CONTINGENCIES**

The Foundation leases office equipment under a noncancelable operating lease agreement expiring in September 2018. Rent expense incurred under the operating lease agreement totaled \$14,791 and \$10,123 during the years ended December 31, 2016 and 2015, respectively. At December 31, 2016, future amounts due under the noncancelable operating lease agreement for the next two years are as follows:

2017	\$	6,360
2018		<u>4,770</u>
	\$	<u><u>11,130</u></u>

**THE BAPTIST FOUNDATION OF ALABAMA**

Notes to Financial Statements

December 31, 2016 and 2015

(Continued)

**NOTE 10 - FUNCTIONAL EXPENSES**

The cost of providing various programs and other activities has been presented on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited. The expenses of the Foundation, by function, for the year ended December 31, 2016 consisted of the following:

	<b>Trust</b>		<b>Total</b>	<b>General and</b>		<b>Total</b>
	<b>Administration</b>	<b>Eldercare</b>	<b>Program</b>	<b>Administrative</b>	<b>Development</b>	<b>Expenses</b>
Depreciation	\$ 33,481	\$ 16,741	\$ 50,222	\$ 15,860	\$ 22,027	\$ 88,109
Disbursements for beneficiaries and others	1,076,229	-	1,076,229	-	-	1,076,229
Office expense	96,455	41,905	138,360	80,245	59,909	278,514
Professional	50,851	139	50,990	46,381	19,947	117,318
Promotion and public relations	-	2,428	2,428	2,745	44,071	49,244
Salaries and benefits	618,880	205,945	824,825	478,238	545,685	1,848,748
Travel	5,082	12,645	17,727	8,101	31,998	57,826
	<u>\$ 1,880,978</u>	<u>\$ 279,803</u>	<u>\$ 2,160,781</u>	<u>\$ 631,570</u>	<u>\$ 723,637</u>	<u>\$ 3,515,988</u>

The expenses of the Foundation, by function, for the year ended December 31, 2015 consisted of the following:

	<b>Trust</b>		<b>Total</b>	<b>General and</b>		<b>Total</b>
	<b>Administration</b>	<b>Eldercare</b>	<b>Program</b>	<b>Administrative</b>	<b>Development</b>	<b>Expenses</b>
Depreciation	\$ 37,074	\$ 18,537	\$ 55,611	\$ 17,562	\$ 24,391	\$ 97,564
Disbursements for beneficiaries and others	1,217,116	-	1,217,116	-	-	1,217,116
Office expense	84,092	35,761	119,853	76,340	58,412	254,605
Professional	55,402	30	55,432	38,146	20,993	114,571
Promotion and public relations	-	2,959	2,959	2,091	35,866	40,916
Salaries and benefits	575,636	168,495	744,131	476,762	572,329	1,793,222
Travel	7,229	6,197	13,426	3,238	34,587	51,251
	<u>\$ 1,976,549</u>	<u>\$ 231,979</u>	<u>\$ 2,208,528</u>	<u>\$ 614,139</u>	<u>\$ 746,578</u>	<u>\$ 3,569,245</u>