



CARNEGIE INSTITUTION OF WASHINGTON

Financial Statements and Schedule

June 30, 2013 and 2012

(With Independent Auditors' Report Thereon)



KPMG LLP
Suite 12000
1801 K Street, NW
Washington, DC 20006

Independent Auditors' Report

The Audit Committee
Carnegie Institution of Washington:

We have audited the accompanying financial statements of the Carnegie Institution of Washington (Carnegie), which comprise the statements of financial position as of June 30, 2013 and 2012, 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 U.S. generally accepted accounting principles; 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 of 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 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 Carnegie as of June 30, 2013 and 2012, and the results of its operations and cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.



Other Matters

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information included in the schedules of expenses is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole.

KPMG LLP

November 25, 2013

CARNEGIE INSTITUTION OF WASHINGTON

Statements of Financial Position

June 30, 2013 and 2012

Assets	2013	2012
Cash and cash equivalents	\$ 2,131,428	2,224,055
Accrued investment income	17,496	47,721
Contributions receivable, net (note 2)	14,100,999	18,495,658
Accounts receivable and other assets (note 6 and 7)	23,597,460	21,436,261
Bond proceeds held by trustee (note 7)	15,698	15,694
Investments (notes 3 and 14)	856,597,311	794,835,568
Property and equipment, net (notes 4 and 5)	147,278,352	152,340,983
Total assets	\$ 1,043,738,745	989,395,940
Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses (note 8)	\$ 9,559,263	11,449,485
Deferred revenue (note 5)	28,235,748	29,670,190
Bonds payable (note 7)	65,685,422	65,706,919
Accrued postretirement benefits (note 9)	20,356,659	19,991,999
Total liabilities	123,837,091	126,818,593
Net assets (notes 10 and 11):		
Unrestricted	272,816,713	253,993,414
Temporarily restricted	592,058,025	553,628,669
Permanently restricted	55,026,916	54,955,264
Total net assets	919,901,654	862,577,347
Commitments and contingencies (notes 9, 12, and 13)		
Total liabilities and net assets	\$ 1,043,738,745	989,395,940

See accompanying notes to financial statements.

CARNEGIE INSTITUTION OF WASHINGTON

Statements of Activities

Years ended June 30, 2013 and 2012

	2013				2012			
	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Revenues and support:								
External revenue:								
Grants and contracts	\$ 38,545,813	—	—	38,545,813	40,529,751	—	—	40,529,751
Contributions and gifts (note 14)	\$642,109	9,272,877	1,625	9,916,611	1,323,064	25,477,731	1,000	26,801,795
Other income (loss) (note 8)	\$1,977,861	(1,632,951)	(2,135)	342,775	3,150,074	4,668,329	2,143	7,820,546
External revenue	\$41,165,783	7,639,926	(510.00)	48,805,199	45,002,889	30,146,060	3,143	75,152,092
Investment income, net (note 3)	\$27,452,377	80,256,824	72,162	107,781,363	8,852,590	27,305,764	22,795	36,181,149
Net assets released from restrictions (note 10)	\$49,467,394	(49,467,394)	—	—	55,337,058	(55,337,058)	—	—
Total revenues and other support	<u>\$118,085,554</u>	<u>38,429,356</u>	<u>71,652</u>	<u>156,586,562</u>	<u>109,192,537</u>	<u>2,114,766</u>	<u>25,938</u>	<u>111,333,241</u>
Expenses:								
Program expenses:								
Terrestrial magnetism	\$13,540,172	—	—	13,540,172	14,972,184	—	—	14,972,184
Observatories	\$18,733,368	—	—	18,733,368	20,071,881	—	—	20,071,881
Geophysical laboratory	\$21,003,255	—	—	21,003,255	20,425,062	—	—	20,425,062
Embryology	\$11,643,914	—	—	11,643,914	11,467,512	—	—	11,467,512
Plant biology	\$11,327,868	—	—	11,327,868	10,778,313	—	—	10,778,313
Global ecology	\$8,427,241	—	—	8,427,241	8,241,999	—	—	8,241,999
Other programs	\$757,789	—	—	757,789	852,665	—	—	852,665
Total program expenses	\$85,433,607	—	—	85,433,607	86,809,616	—	—	86,809,616
Administrative and general expenses	\$14,341,283	—	—	14,341,283	11,259,427	—	—	11,259,427
Total expenses	<u>\$99,774,890</u>	<u>—</u>	<u>—</u>	<u>99,774,890</u>	<u>98,069,043</u>	<u>—</u>	<u>—</u>	<u>98,069,043</u>
Change in net assets before pension related changes other than net periodic postretirement benefit cost	\$18,310,664	38,429,356	71,652	56,811,672	11,123,494	2,114,766	25,938	13,264,198
Pension related changes other than net periodic postretirement benefit cost (note 9)	\$512,635	—	—	512,635	(2,079,935)	—	—	(2,079,935)
Change in net assets	\$18,823,299	38,429,356	71,652	57,324,307	9,043,559	2,114,766	25,938	11,184,263
Net assets at beginning of year	<u>\$253,993,414</u>	<u>553,628,669</u>	<u>54,955,264</u>	<u>862,577,347</u>	<u>244,949,855</u>	<u>551,513,903</u>	<u>54,929,326</u>	<u>851,393,084</u>
Net assets at end of year	<u>\$ 272,816,713</u>	<u>592,058,025</u>	<u>55,026,916</u>	<u>919,901,654</u>	<u>253,993,414</u>	<u>553,628,669</u>	<u>54,955,264</u>	<u>862,577,347</u>

See accompanying notes to financial statements.

CARNEGIE INSTITUTION OF WASHINGTON

Statements of Cash Flows

Years ended June 30, 2013 and 2012

	<u>2013</u>	<u>2012</u>
Cash flows from operating activities:		
Change in net assets	\$ 57,324,307	11,184,263
Adjustments to reconcile change in net assets to net cash used in in operating activities:		
Depreciation	10,418,739	9,724,219
Net gains on investments	(102,268,501)	(30,336,573)
Net loss on disposal of property	134,131	25,499
Contributions of stock	(664,933)	(9,511)
Amortization of bond issuance costs, premium, and discount	(21,497)	(21,497)
Contributions and investment income restricted for long-term investment	(1,625)	(273,299)
(Increase) decrease in assets:		
Receivables	2,233,459	(15,354,128)
Accrued investment income	30,225	(47,721)
Increase (decrease) in liabilities:		
Accounts payable and accrued expenses	(1,890,222)	530,640
Deferred revenue	(1,434,442)	(1,637,582)
Accrued postretirement benefits	364,660	2,785,920
Net cash used in operating activities	<u>(35,775,699)</u>	<u>(23,429,770)</u>
Cash flows from investing activities:		
Acquisition of property and equipment	(3,224,877)	(5,961,268)
Construction of facilities and equipment	(2,265,362)	(1,361,296)
Investments purchased	(364,529,139)	(231,962,980)
Proceeds from investments sold or matured	405,700,829	263,146,003
Proceeds from sales of investments by bond trustee	(4)	2,000
Net cash provided by investing activities	<u>35,681,447</u>	<u>23,862,459</u>
Cash flows from financing activities:		
Proceeds from contributions and investment income restricted for:		
Investment in endowment	1,625	1,000
Investment in property and equipment	—	272,299
Net cash provided by financing activities	<u>1,625</u>	<u>273,299</u>
Net decrease in cash and cash equivalents	(92,627)	705,988
Cash and cash equivalents at beginning of year	<u>2,224,055</u>	<u>1,518,067</u>
Cash and cash equivalents at end of year	\$ <u>2,131,428</u>	<u>2,224,055</u>
Supplementary cash flow information:		
Cash paid for interest	\$ 3,071,754	3,071,763
Noncash activity – contributions of stock	664,933	9,510

See accompanying notes to financial statements.

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Notes to Financial Statements

June 30, 2013 and 2012

(1) Organization and Summary of Significant Accounting Policies

(a) *Organization*

The Carnegie Institution of Washington (Carnegie) conducts advanced research and training in the sciences. It carries out its scientific work in six research centers located throughout the United States and at an observatory in Chile. The centers are the Departments of Embryology, Plant Biology, Global Ecology, Terrestrial Magnetism, the Geophysical Laboratory, and the Observatories.

For the years ended June 30, 2013 and 2012, Carnegie had net investment gains of \$108 million and \$36 million. Carnegie's other sources of income are primarily from gifts and federal grants and contracts.

(b) *Basis of Accounting and Presentation*

The financial statements are prepared on the accrual basis of accounting.

(c) *Investments and Cash Equivalents*

Carnegie's common stock and equity investments are reported at fair value based on quoted market prices, or with respect to commingled funds, real estate funds, natural resource funds, absolute return funds, and private equity funds, at estimated values provided by the general partners of limited partnerships or other external investment managers. These estimated values are reviewed and evaluated by Carnegie. Due to the inherent uncertainties of these estimates, these values may differ from the values that would have been reported had a ready market for such investments existed.

Carnegie applies the measurement provisions of Accounting Standards Update No. 2009-12, *Investments in Certain Entities that Calculate Net Asset Value per Share (or Its Equivalent)* to certain investments in funds that do not have readily determinable fair values including commingled funds, private equity, natural resources funds, real estate, and absolute return funds. This guidance permits, as a practical expedient, fair value of investments within its scope to be estimated using net asset value (NAV) or its equivalent.

All investments are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the financial statements. All changes in fair value are recognized in the statements of activities.

Carnegie considers all highly liquid debt instruments purchased with original maturities of 90 days or less to be cash equivalents. Money market and other highly liquid instruments held by investment managers are reported as investments.

(d) *Income Taxes*

Carnegie has been recognized by the Internal Revenue Service as exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code (the Code) except for amounts from unrelated business income. Carnegie is also an educational institution within the meaning of

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Section 170(b)(1)(A)(ii) of the Code. The Internal Revenue Service has classified Carnegie as other than a private foundation, as defined in Section 509(a) of the Code.

Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 740-10, *Income Taxes*, requires that management evaluate tax positions taken by Carnegie and recognize a tax liability (or asset) if Carnegie has taken an uncertain tax position that more likely than not would not be sustained upon examination by the Internal Revenue Service. Carnegie has analyzed the tax positions taken and has concluded that as of June 30, 2013, there are no uncertain tax positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements.

(e) Fair Value of Financial Instruments

Financial instruments of Carnegie include cash equivalents, receivables, investments, bond proceeds held by trustee, accounts payable, and bonds payable. The fair value of investments in common stock and equity securities is based on quoted market prices. The fair value of investments in bond funds, commingled funds, real estate, natural resources, absolute return funds, and private equity is estimated using net asset value or its equivalent as discussed in note 1(c).

The fair value of the California Educational Facilities Authority Refunding Revenue Bonds 2010 Series A and the Maryland Health and Higher Education Facilities Authority Revenue Refunding Bonds Series 2010 is estimated to be the carrying value (see note 7) (level 2 in fair value hierarchy).

Interest rate and commodity swap agreements are entered into by Carnegie to mitigate the risk of changes in interest rates associated with fixed interest rate indebtedness and changes in the price of crude oil and natural gas. Carnegie applies the provisions of ASC 815, *Derivatives and Hedging*. This standard requires certain derivative financial instruments to be recorded at fair value.

ASC 820, *Fair Value Measurements*, establishes, among other things, a hierarchical disclosure framework, which prioritizes and ranks the level of market price observability used in measuring financial instruments at fair value. The hierarchy gives the highest priority to unadjusted quoted market prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3 measurements).

Under ASC 820, financial instruments are categorized in one of the following three categories:

Level 1 – Pricing inputs are unadjusted quoted prices available in active markets for identical assets or liabilities.

Level 2 – Pricing inputs are quoted prices for identical assets or liabilities in markets that are not active, or inputs that are observable either directly or indirectly, for substantially the full term of the asset or liability through corroboration with observable market data.

Level 3 – Pricing inputs are unobservable for the investment and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation.

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June 30, 2013 and 2012

The level of a value determined for a financial instrument within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement in its entirety. Determination of what constitutes “observable” input requires judgment by Carnegie. In general, Carnegie considers observable inputs to be market data that are readily available, regularly distributed or updated, reliable and verifiable, and provided by independent sources that are actively involved in the relevant market.

In general, Carnegie includes funds in which its ownership interests are publicly traded in an active market under Level 1 of the valuation hierarchy. Carnegie classifies investments under Level 2 or 3 if the funds are not publicly traded, but the pricing inputs are directly observable either directly or indirectly and its interests are redeemable. Classification in Level 2 or 3 is based on Carnegie’s ability to redeem its interest at or near the date of the statement of financial position. If the interest can be redeemed in the near term (within 90 days of June 30), the investment is classified in Level 2, alternatively, Level 3

The fair values of cash equivalents, receivables, bond proceeds held by trustee, and accounts payable approximate their carrying values based on their short maturities.

(f) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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. Actual results could differ from those estimates.

(g) Property and Equipment

Carnegie capitalizes expenditures for land, buildings and leasehold improvements, telescopes, scientific and administrative equipment, and projects in progress. Routine replacement, maintenance, and repairs are charged to expense.

Depreciation is computed on a straight-line basis, generally over the following estimated useful lives:

Buildings and telescopes	50 years
Scientific and administrative equipment	2 – 10 years, based on scientific life of equipment

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Notes to Financial Statements

June 30, 2013 and 2012

(h) *Contributions*

Contributions are classified based on the existence or absence of donor-imposed restrictions. Contributions are classified in categories of net assets as follows:

Unrestricted – includes all contributions received without donor-imposed restrictions on use or time.

Temporarily restricted – includes contributions with donor-imposed restrictions as to purpose of gift and/or time period expended.

Permanently restricted – generally includes endowment gifts in which donors stipulated that the corpus be invested in perpetuity. Only the investment income generated from endowments may be spent. Certain endowments require that a portion of the investment income be reinvested in perpetuity.

Contributions include unconditional promises to give. In instances where such promises are to be received after one year or more from the date of the gift, they are recorded at a discounted amount at an appropriate risk-adjusted rate commensurate with the expected collection period (level 3 in the fair value hierarchy). Amortization of the discount is recorded as additional contribution revenue. Satisfaction of donor-imposed restrictions are reported as releases of restrictions in the statements of activities.

Gifts of long-lived assets, such as buildings or equipment, are considered unrestricted when placed in service. Cash gifts restricted for investment in long-lived assets are released from restriction when the asset is acquired or as costs are incurred for asset construction.

(i) *Grants*

Carnegie records revenues on grants from federal agencies only to the extent that reimbursable expenses are incurred. Accordingly, funds received in excess of reimbursable expenses are recorded as deferred revenue, and expenses in excess of reimbursements are recorded as accounts receivable. Reimbursement of indirect costs is based upon provisional rates, which are subject to subsequent audit by Carnegie's federal cognizant agency, the National Science Foundation.

(j) *Allocation of Costs*

The costs of providing programs and supporting services have been summarized in the statements of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited. Fundraising expenses of \$1,364,086 and \$1,540,903 for the years ended June 30, 2013 and 2012, respectively, have been included in administrative and general expenses in the accompanying statements of activities.

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Notes to Financial Statements

June 30, 2013 and 2012

(2) Contributions Receivable

Contributions receivable are summarized as follows as of June 30, 2013 and 2012:

	2013	2012
Unconditional promises expected to be collected in:		
Less than one year	\$ 8,545,277	6,599,745
One to five years	6,538,600	12,635,474
More than five years	—	200,000
	15,083,877	19,435,219
Less:		
Allowance for uncollectible amounts	(727,981)	(405,717)
Discount to present value	(254,897)	(533,844)
	\$ 14,100,999	18,495,658

Contributions receivable as of June 30, 2013 and 2012 were discounted based on the estimated risk-adjusted rate of return on the pledge date at rates ranging from less than 0.26% to 4.36%.

(3) Investments

Investments at fair value consisted of the following as of June 30, 2013 and 2012:

	2013	2012
Time deposits and money market funds	\$ 19,370,398	30,626,930
U.S. Government bond funds	40,020,714	42,213,845
Common stock – domestic	34,265,328	62,613,463
Domestic equity commingled funds	142,277,493	105,778,828
International equity commingled funds	148,075,922	126,736,392
Real estate funds	86,311,971	73,867,059
Natural resources funds	74,810,701	75,805,372
Absolute return funds	242,507,047	208,865,703
Private equity funds	68,957,737	68,327,976
	\$ 856,597,311	794,835,568

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Notes to Financial Statements

June 30, 2013 and 2012

Investment income, net consisted of the following for the years ended June 30, 2013 and 2012:

	2013	2012
Interest and dividends	\$ 6,457,780	6,841,808
Net realized gains	61,564,393	40,956,752
Net unrealized gains (losses)	40,704,108	(10,620,179)
Investment management expenses	(944,918)	(997,232)
	\$ 107,781,363	36,181,149

The following table represents investments that are measured at fair value on a recurring basis as of June 30, 2013:

	2013	Level 1	Level 2	Level 3
Time deposits and money market funds	\$ 19,370,398	19,370,398	—	—
U.S. Government bond funds	40,020,714	1,622,673	38,398,041	—
Common stock – domestic	34,265,328	33,851,632	—	413,696
Domestic equity commingled funds	142,277,493	56,286,970	85,990,523	—
International equity commingled funds	148,075,922	32,139,000	115,936,922	—
Real estate funds	86,311,971	—	—	86,311,971
Natural resources funds	74,810,701	—	—	74,810,701
Absolute return funds	242,507,047	—	167,451,761	75,055,286
Private equity funds	68,957,737	—	—	68,957,737
	\$ 856,597,311	143,270,673	407,777,247	305,549,391

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Notes to Financial Statements

June 30, 2013 and 2012

The following table represents investments that are measured at fair value on a recurring basis as of June 30, 2012:

	<u>2012</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Time deposits and money market funds	\$ 30,626,930	30,626,930	—	—
U.S. Government bond funds	42,213,845	2,544,183	39,669,662	—
Common stock – domestic	62,613,463	62,260,291	—	353,172
Domestic equity commingled funds	105,778,828	32,925,875	72,852,953	—
International equity commingled funds	126,736,392	26,206,886	100,529,506	—
Real estate funds	73,867,059	—	—	73,867,059
Natural resources funds	75,805,372	—	—	75,805,372
Absolute return funds	208,865,703	—	208,219,732	645,971
Private equity funds	68,327,976	—	—	68,327,976
	<u>\$ 794,835,568</u>	<u>154,564,165</u>	<u>421,271,853</u>	<u>218,999,550</u>

The following table presents Carnegie's activity for investments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) as defined in ASC 820 for the years ended June 30, 2013 and 2012.

	<u>Common stock domestic</u>	<u>Real estate funds</u>	<u>Natural resources funds</u>	<u>Absolute return funds</u>	<u>Private equity funds</u>	<u>Total</u>
Balance at June 30, 2011	\$ 353,172	69,925,843	79,357,999	2,550,228	62,235,445	214,422,687
Total realized gains (losses), net	—	8,389,625	562,217	(632,214)	5,758,884	14,078,512
Total unrealized gains (losses), net	—	2,492,547	(5,976,526)	(123,751)	2,483,739	(1,123,991)
Purchases and issuances	—	779,608	4,178,987	—	791,199	5,749,794
Settlements	—	(7,720,564)	(2,317,305)	(1,148,292)	(2,941,291)	(14,127,452)
Balance at June 30, 2012	353,172	73,867,059	75,805,372	645,971	68,327,976	218,999,550
Total realized gains (losses), net	—	8,394,777	7,108,715	9,593,624	672,841	25,769,957
Total unrealized gains (losses), net	60,524	5,500,296	(6,854,151)	(104,691)	839,792	(558,230)
Purchases and issuances	—	6,270,402	1,068,070	114,634,799	3,045,610	125,018,881
Settlements	—	(7,720,563)	(2,317,305)	(49,714,417)	(3,928,482)	(63,680,767)
Balance at June 30, 2013	<u>\$ 413,696</u>	<u>86,311,971</u>	<u>74,810,701</u>	<u>75,055,286</u>	<u>68,957,737</u>	<u>305,549,391</u>

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Notes to Financial Statements

June 30, 2013 and 2012

The following table summarizes the nature and risk of Carnegie's investments in funds, which are valued based on net asset value as a practical expedient for fair value as of June 30, 2013 and 2012:

	<u>Fair value</u>		2013 unfunded commitments	Redemption frequency
	<u>2013</u>	<u>2012</u>		
U.S. Government bond funds	\$ 38,398,041	36,937,564	—	Monthly
Domestic equity commingled funds (b)	85,990,523	72,852,953	27,500,000	Biennial
International equity commingled funds (c)	115,936,922	100,529,506	—	Monthly
Real estate funds (d)	86,311,971	73,867,059	173,752,375	Illiquid
Natural resources funds (e)	74,810,701	75,805,372	67,500,000	Illiquid
				Quarterly to
Absolute return funds (f)	242,507,047	208,643,926	25,000,000	illiquid
Private equity funds (g)	68,957,737	68,327,976	150,000,000	Illiquid
	<u>\$ 712,912,942</u>	<u>636,964,356</u>	<u>443,752,375</u>	

There were no transfers of funds between levels during the years ended June 30, 2013 and 2012.

- (a) This class is comprised of a single fixed income fund. The fixed income fund is a mutual investment fund intended to mirror a U.S. government bond index. In general, this fund seeks to produce returns that mirror or exceed various benchmarks established for comparable portfolios. The notice period is 30 days or less.
- (b) This class is comprised of a single fund which invests in common stocks of biotechnology companies. This fund seeks to produce returns that mirror or exceed various benchmarks established for comparable portfolios.
- (c) This class is comprised of two international partnerships which invest in public equity markets internationally and one institutional mutual fund that mirrors an emerging markets index. Of these, one holds a concentrated portfolio of global companies. In general, these funds seek to produce returns that mirror or exceed various benchmarks established for comparable portfolios. The majority of Carnegie's capital in this category can be redeemed on a monthly basis or more frequently; in one case redemptions can occur within a year. The typical notice period is 30 days or less.
- (d) This class includes several real estate funds which invest primarily in U.S. commercial real estate. One fund targets commercial, residential, and industrial real estate in Europe. The fair values of the investments in this category have been estimated using the net asset value of Carnegie's ownership interest in partners' capital. Investments under this category cannot be redeemed. Instead, distributions are made from operating proceeds on a periodic basis, typically monthly or quarterly. Proceeds from assets sold are generally distributed immediately. It is estimated that the underlying assets of these funds will be liquidated over the next one to ten years.

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- (e) This class includes funds which invest primarily in timber and oil and gas assets. The investment strategy is to acquire, operate, develop, and improve oil and gas and timber producing assets. The fair values of the investments in this category have been estimated using the net asset value of Carnegie's ownership interest in partners' capital. Carnegie employs an established forward pricing curve beyond the first two years of production in establishing its valuation within the oil and gas funds. Investments under this category cannot be redeemed. Instead, distributions are made from operating proceeds on a periodic basis, typically quarterly. Proceeds from assets sold may be distributed immediately. It is estimated that the underlying assets of these funds will be liquidated over the next two to fourteen years.
- (f) This class is comprised of six separate funds, including: three long/short hedge funds which invest in publicly traded equities, a partnership that invests in fixed income securities; a partnership that invests in distressed fixed income securities; a multi-strategy partnership that invests in value investments, credit investments, event-driven situations, real estate, and distressed credit investments; and a partnership that invests in distressed credit securities and event-driven situations. In general, these funds seek to produce positive absolute returns that do not necessarily correlate with the public markets. The fair values of the investments in this category have been estimated using the net asset value of Carnegie's ownership interest in partners' capital. The majority of Carnegie's capital in this category can be redeemed on an annual basis; in some cases redemptions can occur within a year, with a minimum of typically 90 days notice. Less than one percent is invested in a partnership where, under the current terms, funds are in liquidation and cannot be withdrawn. The underlying assets are expected to be distributed over the next year.
- (g) This class is comprised of three separate managers and nine separate private equity funds which invest primarily in leveraged buyouts, venture capital, emerging growth companies, corporate finance, and various niche strategies. Eight of the nine funds are funds of funds, where the manager in turn invests in other private equity funds. Private equity investment transactions may involve acquisitions, leveraged buyouts, reorganizations, privatizations, restructurings, and spin-offs. The fair values of the investments in this category have been estimated using the net asset value of Carnegie's ownership interest in partners' capital. Investments under this category cannot be redeemed. Private capital partnerships span several years that are often divided into commitment and distribution phases. In the first half of the span, capital is drawn down or called as investment opportunities are identified. During the second half of the span, capital is returned to the investment partners in the form of distributions. Such distributions are made on a periodic basis, typically quarterly. It is estimated that the underlying assets of these various funds will be liquidated over the next one to twelve years.

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(4) Property and Equipment

Property and equipment consisted of the following as of June 30, 2013 and 2012:

	2013	2012
Buildings and improvements	\$ 89,534,072	89,099,761
Scientific equipment	63,148,890	60,197,966
Telescopes	93,969,502	93,969,502
Construction in progress	5,394,050	4,170,739
Administrative equipment	4,078,676	3,875,706
Leased equipment	300,558	214,086
Land	817,117	817,117
Art	76,099	76,099
	257,318,964	252,420,976
Accumulated depreciation	(110,040,612)	(100,079,993)
	\$ 147,278,352	152,340,983

Construction in progress consists of scientific equipment as of June 30, 2013 and 2012, respectively.

As of June 30, 2013 and 2012, approximately \$65.6 million and \$67.8 million, respectively, of property and equipment, net of accumulated depreciation, was located in Las Campanas, Chile.

(5) Magellan Consortium

During the year ended June 30, 1998, Carnegie entered into an agreement (Magellan Agreement) with four universities establishing a consortium to build and operate the Magellan telescopes. The two Magellan telescopes are located on Manqui Peak, Las Campanas in Chile. The first telescope, with a cost of approximately \$41.7 million, was placed in service during 2001. The other, with a cost of approximately \$30.1 million, was placed in service in 2003.

The university members of the consortium, by contribution to the construction and operating costs of Magellan, acquire rights of access and oversight as described in the Magellan Agreement. Total contributions by the university members for construction, which amounted to \$36.0 million, covered approximately 50% of the total construction costs. These monies were used by Carnegie to finance part of the Magellan Telescopes' construction costs. The contributions were recorded as deferred revenue and are being recognized ratably as income over the remaining estimated useful lives of the telescopes. As of June 30, 2013 and 2012, the deferred revenue totaled \$26.1 million and \$26.8 million, respectively.

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(6) Long Term Deferred Asset

Carnegie is a Founder and initial contributor to the GMT Project, which is managed by the Giant Magellan Telescope Organization Corporation (GMTO) that includes institutions from the US, Australia and Korea. The GMTO is a nonprofit organization incorporated in 2007 for the purpose of developing and building a state-of-the-art next-generation extremely large telescope. Contributors to the GMTO project acquire rights of access to the telescope upon completion as described in the Founders' Agreement dated March 20, 2009. Beginning in fiscal year 2010, Carnegie began to capitalize cash contributions to the GMTO, primarily received through fundraising efforts, as a deferred long term asset. The asset will be amortized over the expected 50 year life of the telescope beginning at the time it is placed into service. Carnegie's cash contributions to GMTO in fiscal year 2013 and fiscal year 2012 were \$5.0 million and \$3.7 million, respectively. The deferred long term asset value was \$13.2 million and \$8.2 million at June 30, 2013 and 2012, respectively which is reported as part of accounts receivable and other assets on statements of financial position.

(7) Bonds Payable

(a) 2010 Maryland Health and Higher Education Facilities Revenue Bonds

On February 4, 2010, the Maryland Health and Higher Education Facilities Authority (MHHEFA) issued \$30,580,000 of fixed rate, tax-exempt revenue bonds on behalf of Carnegie. Bond proceeds totaling approximately \$30,500,000 were used to refund \$30,000,000 in bonds issued in 2002 by MHHEFA and cover the costs of issuance including related fees.

The structure of the 2010 MHHEFA bonds is two term bonds, maturing in 2037 and 2040. The bond due July 1, 2037, bears interest at a fixed coupon rate of 4.25% with sinking fund redemptions as follows:

Due July 1:	
2036	\$ 6,120,000
2037	<u>6,115,000</u>
	<u>\$ 12,235,000</u>

The bond due July 1, 2040, bears interest at a fixed coupon rate of 4.50% with sinking fund redemptions as follows:

Due July 1:	
2038	\$ 6,115,000
2039	6,115,000
2040	<u>6,115,000</u>
	<u>\$ 18,345,000</u>

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The MHHEFA bonds payable outstanding was \$30,580,000 as of June 30, 2013 and 2012. The interest expense for the MHHEFA issues was \$1,345,508 and \$1,345,512 for the years ended June 30, 2013 and 2012.

The 2010 MHHEFA bonds are secured solely by Carnegie's credit. There are no financial covenants or stand-by credit facilities associated with the bonds.

The bonds are subject to redemption and purchase prior to maturity, beginning on July 1, 2020, at the option of MHHEFA upon the direction of Carnegie.

(b) 2010 California Educational Facilities Authority Revenue Bonds

On March 24, 2010, the California Educational Facilities Authority (CEFA) issued fixed rate, tax-exempt revenue bonds with a par value of \$34,525,000 on behalf of Carnegie. Bond proceeds totaling approximately \$36,400,000 were used to: a) refund \$17,500,000 of 1993 Series B bonds issued by CEFA on behalf of Carnegie for the purpose of financing the Magellan telescope project and the renovation of facilities of the Observatories at Pasadena; b) refund \$18,300,000 of 2006 CEFA Refunding Revenue Bonds that, in turn, were used to finance the Magellan telescope project and the renovation of facilities of the Observatories at Pasadena; and c) cover the costs of issuance including related fees.

The structure of the 2010 CEFA bond is a single fixed-rate bond, maturing in 2040, with a par value of \$34,525,000. The bond bears interest at a fixed coupon rate of 5.00% with sinking fund redemptions as follows:

Due July 1:		
2036	\$	6,905,000
2037		6,905,000
2038		6,905,000
2039		6,905,000
2040		<u>6,905,000</u>
	\$	<u>34,525,000</u>

The CEFA bonds payable outstanding was \$34,525,000 as of June 30, 2013 and 2012. The interest expense for the CEFA issue was \$1,726,245 and \$1,726,250 for the years ended June 30, 2013 and 2012.

The 2010 CEFA bonds are secured solely by Carnegie's credit. There are no financial covenants or stand-by credit facilities associated with the bonds.

The 2010 California bonds are subject to redemption and purchase prior to maturity, beginning on July 1, 2020, at the option of CEFA upon the direction of Carnegie.

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(c) *Line of credit*

On June 1, 2011, Carnegie entered into an unsecured revolving credit facility with a maximum principal amount of \$15 million from a commercial bank. Borrowings under the credit facility bear interest at a floating London Interbank Offered Rate (LIBOR) plus a credit spread of 1.25%. Carnegie did not draw any funds from this line of credit facility in 2012 or 2013. The credit facility expires May 30, 2014.

(8) **Interest Rate and Commodity Swap Agreements**

(a) *2010 Maryland Health and Higher Education Facilities Authority Revenue Bonds*

On February 11, 2010, Carnegie entered into a basis swap with Barclays Capital. A basis swap is an interest rate swap, which involves the exchange of two floating rate financial instruments. Under this agreement, Barclays Capital pays Carnegie 68% of three-month LIBOR and Carnegie pays Barclays Capital the Securities Industry and Financial Markets Association Benchmark (SIFMA) minus 0.08% on a notional amount of \$22,935,000, which matches the amortization structure of the 2010 MHHEFA bonds (see note 7(a)), reducing on the dates and in the amounts as follows:

Due July 1:	
2036	\$ 4,590,000
2037	4,586,250
2038	4,586,250
2039	4,586,250
2040	4,586,250

Carnegie may terminate and cash settle this transaction upon meeting a three business day notice requirement, with both parties obligated to pay any amounts owed on the termination date.

In addition to this basis swap, on February 26, 2010, Carnegie entered into a fixed to floating interest rate swap where Carnegie receives 3.6895% and pays SIFMA on a notional amount of \$7,645,000. This transaction matches the amortization structure of the 2010 bonds (see note 7(a)), reducing on the dates and in the amounts as follows:

Due July 1:	
2036	\$ 1,530,000
2037	1,528,750
2038	1,528,700
2039	1,528,700
2040	1,528,700

Under this agreement, Carnegie may terminate and cash settle the transaction upon meeting a three-day business notice requirement and Barclays Capital owns the right to cancel the swap with Carnegie after ten years and upon meeting a 30-calendar day notice requirement.

The basis and fixed to floating interest rate swap agreements described above are derivative instruments that are recorded at fair value. The estimated fair value as of June 30, 2013 and 2012

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were liabilities of \$2,251,862 and \$1,856,850, respectively. These amounts are included in accounts payable and accrued expenses in 2013 and 2012 on the accompanying statements of financial position. The change in fair value for the years ended June 30, 2013 and 2012 was a loss of \$395,012 and a gain \$685,637, respectively, and is reported as other income.

(b) 2010 California Educational Facilities Authority Refunding Revenue Bonds

On March 17, 2010, Carnegie entered into a basis swap with Barclays Capital. A basis swap is an interest rate swap, which involves the exchange of two floating rate financial instruments. Under this agreement, Barclays Capital pays Carnegie 68% of three-month LIBOR and Carnegie pays Barclays Capital SIFMA minus 0.111% on a notional amount of \$25,893,750, which matches the amortization structure of the 2010 bonds (see note 7(b)), reducing on the dates and in the amounts as follows:

Due July 1:		
2036	\$	5,178,750
2037		5,178,750
2038		5,178,750
2039		5,178,750
2040		5,178,750

Carnegie may terminate and cash settle this transaction upon meeting a three business day notice requirement, with both parties obligated to pay any amounts owed on the termination date.

In addition to this basis swap, on March 17, 2010, Carnegie entered into a fixed to floating interest rate swap where Carnegie receives 3.737% and pays SIFMA on a notional amount of \$8,631,250. This transaction matches the amortization structure of the 2010 bonds (see note 7(b)), reducing on the dates and in the amounts as follows:

Due July 1:		
2036	\$	1,726,250
2037		1,726,250
2038		1,726,250
2039		1,726,250
2040		1,726,250

Under this agreement, Carnegie may terminate and cash settle the transaction upon meeting a three-day business notice requirement and Barclays Capital owns the right to cancel the swap with Carnegie after ten years and upon meeting a 30-calendar day notice requirement.

The basis and fixed to floating interest rate swap agreements described above are derivative instruments that are recorded at fair value. The estimated fair value as of June 30, 2013 and 2012 were liabilities of \$2,349,310 and \$1,884,027, respectively. These amounts are included in accounts payable and accrued expenses in 2013 and 2012 on the accompanying statements of financial position. The change in fair value for the years ended June 30, 2013 and 2012 was a loss of \$465,083 and a gain \$791,514, respectively, and is reported as other income.

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(c) *Commodity Swaps*

Carnegie entered into a series of fixed-floating commodity swap agreements with J. Aron & Company, fixed price payer, for NYMEX West Texas Intermediate Crude Oil (WTI-Oil) and NYMEX Natural Gas.

Under the series of fixed-floating commodity swap agreements, for WTI-Oil, the floating price for each determination period will be the average of the closing settlement price(s) on the NYMEX for the Nearby Light Crude Futures Contract. For natural gas, the floating price for each determination period will be the average of the closing settlement prices for the pricing days of the NYMEX Natural Gas Henry Hub Futures Contract for the reference month.

If, with respect to each determination period, the fixed price exceeds the floating price, the fixed price payer shall pay Carnegie the difference between the two such amounts multiplied by the quantity, and if the floating price exceeds the fixed price, Carnegie will pay the fixed price payer the difference between the two amounts multiplied by the quantity. If the prices are equal, no payment shall be made.

The commodity swap agreements described above are derivative instruments that are recorded at fair value. The estimated fair value as of June 30, 2013 and 2012 was a receivable of \$1,926,077 and \$4,263,968, respectively. These amounts are included in accounts receivable and other assets, in the accompanying statements of financial position. The change in fair value for the years ended June 30, 2013 and 2012 was a loss of \$2,337,896 and a gain of \$1,924,570, respectively, and is reported as other income.

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For the valuation of interest rate and commodity swaps as of June 30, 2013, Carnegie used pricing models based on significant observable inputs as of the valuation date (Level 2) of the fair value hierarchy, including prices of instruments with similar maturities and characteristics, interest rate yield curves, measures of interest rate volatility, and oil and natural gas pricing. The value was determined and adjusted to reflect nonperformance risk of both the counterparty and Carnegie. See note 1(e) for definitions of the fair value hierarchy. The following table represents the interest rate swap liabilities and the commodity swap receivables that are measured at fair value on a recurring basis as of June 30, 2013 and 2012:

Fair value measurements at June 30, 2013				
		Level 1	Level 2	Level 3
Interest rate swaps	\$	—	(4,601,172)	—
Commodity swaps		—	1,926,072	—

Fair value measurements at June 30, 2012				
		Level 1	Level 2	Level 3
Interest rate swaps	\$	—	(3,740,877)	—
Commodity swaps		—	4,263,968	—

(9) Employee Benefit Plans

(a) Retirement Plan

Carnegie has a noncontributory, defined contribution, money-purchase retirement plan in which all U.S. personnel are eligible to participate. After one year of participation, an individual's benefits are fully vested. The Plan has been funded through individually owned annuities issued by Teachers' Insurance and Annuity Association (TIAA) and College Retirement Equities Fund (CREF). Contributions made by Carnegie totaled approximately \$5.0 million and \$4.5 million for the years ended June 30, 2013 and 2012.

(b) Postretirement Benefits Plan

Carnegie provides postretirement medical benefits to all employees who retire after age 55 and have at least 10 years of service. Cash payments made by Carnegie for these benefits totaled \$730,270 and \$658,600 for the years ended June 30, 2013 and 2012, respectively.

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The expense for postretirement benefits for the years ended June 30, 2013 and 2012 consists of the following:

	2013	2012
Service cost – benefits earned during the year	\$ 880,842	706,557
Interest cost on projected benefit obligation	837,318	930,879
Amortization of prior service costs	(18,000)	(18,000)
Amortization of gain	(92,575)	(254,844)
Postretirement benefit expense	\$ 1,607,585	1,364,592

The 2013 postretirement benefits expense was approximately \$877,295 more than the cash payments of \$730,290 and the 2012 postretirement benefits expense was approximately \$705,985 more than the cash payments of \$658,607. The postretirement benefits expense was allocated among program and supporting services expenses in the accompanying statements of activities.

The reconciliation of the Plan's funded status to amounts recognized in the financial statements at June 30, 2013 and 2012 follows:

	2013	2012
Change in benefit obligation:	\$	
Benefit obligation at beginning of year	19,991,999	17,206,079
Service cost	880,842	706,557
Interest cost	837,318	930,879
Actuarial loss	(623,210)	1,807,091
Benefits paid	(730,290)	(658,607)
Benefit obligation at end of year	20,356,659	19,991,999
Change in plan assets:		
Fair value of plan assets at beginning of year	—	—
Contribution to plan	730,290	658,607
Benefits paid	(730,290)	(658,607)
Fair value of plan assets at end of year	—	—
Funded status	\$ (20,356,659)	(19,991,999)

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Pension related changes other than net periodic postretirement benefit cost consisted of the following as of June 30, 2013 and 2012:

	2013	2012
Unrecognized net actuarial gain (loss)	\$ 530,635	(2,061,935)
Unrecognized prior service cost	(18,000)	(18,000)
	\$ 512,635	(2,079,935)

The unrecognized net gain and prior service costs that have not been recognized as a component of net periodic postretirement benefit cost as of June 30, 2013 and 2012:

	2013	2012
Unrecognized net actuarial loss	\$ (3,785,153)	(3,254,518)
Unrecognized prior service cost	(167,000)	(185,000)
	\$ (3,952,153)	(3,439,518)

The net gain and prior service cost that will be amortized into net periodic benefit cost over the next fiscal year:

	2013	2012
Unrecognized net actuarial loss	\$ (131,639)	(92,575)
Unrecognized prior service cost	18,000	18,000
	\$ (113,639)	(74,575)

The present value of the benefit obligation as of June 30, 2013 and 2012 was determined using an assumed discount rate of 4.75% and 4.25%, respectively. The present value of the net periodic postretirement benefit cost as of June 30, 2013 and 2012 was determined using an assumed discount rate of 4.25% and 5.50%, respectively. Carnegie's policy is to fund postretirement benefits as claims and administrative fees are paid.

For measurement purposes, a 10% annual rate of increase in medical claims was assumed for 2013; the rate of increase was assumed to decrease at 1% per year, eventually reaching 5% in 2025. The healthcare cost trend rate assumption has a significant effect on the amounts reported. A one-percentage point change in assumed annual healthcare cost trend rate would have the following effects:

	One- percentage point increase	One- percentage point decrease
Effect on total of service and interest cost components	\$ 397,194	(302,225)
Effect on postretirement benefit obligation	3,623,114	(2,857,965)

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The measurement date used to determine postretirement benefit obligations is June 30.

Carnegie expects to contribute \$630,000 to its postretirement benefit plan during the year ended June 30, 2014.

The following benefit payments (net of retiree contributions), which reflect expected future service, are expected to be paid in future years ending June 30:

2014	\$	630,041
2015		681,209
2016		731,596
2017		794,134
2018 – 2022		5,773,788

The prescription drug benefits offered by Carnegie are determined to not be actuarially equivalent to Medicare Plan D, and the effects of the Medicare Prescription Drug Improvement and Modernization Act, excluding the subsidy, do not have a significant impact on the per capita claims cost.

(10) Net Assets

(a) Unrestricted Net Assets

Unrestricted net assets consisted of the following as of June 30, 2013 and 2012:

		<u>2013</u>	<u>2012</u>
Board-designated quasi-endowments	\$	104,564,745	93,573,064
Undesignated		<u>168,251,968</u>	<u>160,420,350</u>
	\$	<u>272,816,713</u>	<u>253,993,414</u>

(b) Temporarily Restricted Net Assets

Temporarily restricted net assets were available to support the following donor-restricted purposes as of June 30, 2013 and 2012:

		<u>2013</u>	<u>2012</u>
Endowment assets available for future appropriation	\$	547,812,195	509,840,478
Specific research programs		28,477,122	24,091,024
Equipment acquisition and construction		918,830	1,233,133
Passage of time		<u>14,849,878</u>	<u>18,464,034</u>
	\$	<u>592,058,025</u>	<u>553,628,669</u>

(c) Permanently Restricted Net Assets

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Permanently restricted net assets consisted of endowed gifts, the income from which is available to support the following donor-restricted purposes as of June 30, 2013 and 2012:

	2013	2012
Specific research programs	\$ 15,151,405	15,080,878
Operation of maxine singer building	15,000,050	15,000,050
Equipment acquisition and construction	2,764,719	2,764,719
General support (Carnegie endowment)	22,110,742	22,109,617
	\$ 55,026,916	54,955,264

(d) Net Assets Released from Restrictions

During 2013 and 2012, Carnegie met donor-imposed requirements on certain gifts and, therefore, released temporarily restricted net assets as follows:

	2013	2012
Appropriation of endowment assets	\$ 40,934,787	45,516,287
Specific research programs	8,043,309	2,786,282
Equipment acquisition and construction	364,298	268,510
Passage of time	125,000	6,765,979
	\$ 49,467,394	55,337,058

(11) Endowment

Carnegie's endowment consists of a number of individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments to support the purposes of Carnegie. Net assets associated with endowment funds are classified and reported based on the existence or absences of donor-imposed restrictions.

(a) Interpretation of Relevant Law

Effective January 23, 2008, the District of Columbia enacted the Uniform Management of Institutional Funds Act (UPMIFA), the provisions of which apply to endowment funds existing on or established after that date. Based on its interpretation of the provisions of UPMIFA, Carnegie is required to act prudently when making decisions to spend or accumulate donor-restricted endowment funds. As a result of this interpretation, Carnegie classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment and subsequent gifts to the endowment. The remaining portion of the endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by Carnegie in a manner consistent with the standard of prudence prescribed by UPMIFA.

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In accordance with UPMIFA, Carnegie considers the following factors in make a determination to appropriate or accumulate donor-restricted endowment fund:

- 1) The duration and preservation of the fund
- 2) The purposes of the organization and the donor-restricted endowment fund
- 3) General economic conditions, including the possible effects of inflation
- 4) The expected total return from income and the appreciation of investments
- 5) Other resources of the organization
- 6) The investment and spending policies of the organization

(b) *Return Objectives and Risk Parameters*

Carnegie's Board of Trustees has adopted an investment policy, including return objectives, for its endowment. This policy has identified: an appropriate risk posture; stated expectations and objectives; asset allocation guidelines; and criteria to monitor and evaluate the performance results of the Endowment fund's managers. Carnegie expects the Endowment fund to provide an average rate of return of approximately 8-9% annually, while recognizing that performance in any given year may vary from this goal.

(c) *Strategies Employed for Achieving Objectives*

To satisfy its long-term rate of return objectives, Carnegie 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). Carnegie employs a diversified asset allocation strategy that allocates investments among four broad asset classes: common stock, alternative assets, fixed income, and cash. Common stock is subdivided into domestic and international categories. Alternative assets are subdivided into absolute return partnerships, natural resources, and private equity funds.

(d) *Spending Policy and How the Investment Objectives Relate to Spending Policy*

The current Board-approved spending rule requires that the amounts appropriated for spending from the endowment be comprised of: a) 70% of the previous year's budget, adjusted for inflation, and b) 30% of the most recent year-end endowment value, adjusted for debt, and then multiplied by the determined spending rate, currently 5.00%, and adjusted for inflation. The rule functions to smooth annual contributions from the endowment in support of the operating budget. In establishing this policy, Carnegie considered the long-term expected return on its funds. Carnegie expects the current spending and investment policies to grow its endowment at an average of 3-4% annually.

(e) *Appropriation of Endowment Assets for Next Fiscal Year*

For FY14, Carnegie has appropriated \$37,278,000 of its Endowment Funds assets to be distributed for spending. In accordance with the endowment spending policy described above, this amount is

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calculated based upon an endowment spending rate of five percent (5%). Additional amounts required to fulfill debt obligations of Carnegie are also authorized for expenditure.

(f) Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires Carnegie to retain as a fund of perpetual duration. No deficiencies existed as of June 30, 2013 and 2012. These deficiencies resulted from unfavorable market fluctuations that occurred shortly after the investment of new permanently restricted contributions.

Net asset classification by type of endowment as of June 30, 2013:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ —	547,812,195	55,026,915	602,839,110
Board-designated endowment funds	<u>104,564,745</u>	<u>—</u>	<u>—</u>	<u>104,564,745</u>
	<u>\$ 104,564,745</u>	<u>547,812,195</u>	<u>55,026,915</u>	<u>707,403,855</u>

Changes in endowment net assets for the year ended June 30, 2013:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 93,573,064	509,840,478	54,955,263	658,368,805
Investment return:				
Investment income	326,014	1,965,155	1,767	2,292,936
Net appreciation (realized and unrealized gains and losses)	<u>12,594,505</u>	<u>76,941,349</u>	<u>68,260</u>	<u>89,604,114</u>
Total investment return	12,920,519	78,906,504	70,027	91,897,050
Contributions	10,000	—	1,625	11,625
Appropriation of assets for expenditure	<u>(1,938,838)</u>	<u>(40,934,787)</u>	<u>—</u>	<u>(42,873,625)</u>
	<u>\$ 104,564,745</u>	<u>547,812,195</u>	<u>55,026,915</u>	<u>707,403,855</u>

CARNEGIE INSTITUTION OF WASHINGTON

Notes to Financial Statements

June 30, 2013 and 2012

Net asset classification by type of endowment as of June 30, 2012:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Donor-restricted endowment funds	\$ —	509,840,478	54,955,263	564,795,741
Board-designated endowment funds	<u>93,573,064</u>	<u>—</u>	<u>—</u>	<u>93,573,064</u>
	<u>\$ 93,573,064</u>	<u>509,840,478</u>	<u>54,955,263</u>	<u>658,368,805</u>

Changes in endowment net assets for the year ended June 30, 2012:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 90,793,730	521,230,087	54,929,326	666,953,143
Investment return:				
Investment income	1,096,851	6,978,326	5,825	8,081,002
Net appreciation (realized and unrealized gains and losses)	<u>3,598,611</u>	<u>27,148,352</u>	<u>19,112</u>	<u>30,766,075</u>
Total investment return	4,695,462	34,126,678	24,937	38,847,077
Contributions	10,000	—	1,000	11,000
Appropriation of assets for expenditure	<u>(1,926,128)</u>	<u>(45,516,287)</u>	<u>—</u>	<u>(47,442,415)</u>
	<u>\$ 93,573,064</u>	<u>509,840,478</u>	<u>54,955,263</u>	<u>658,368,805</u>

(12) Lease Arrangements

Carnegie leases a portion of the land it owns in Las Campanas, Chile to other organizations. These organizations have built and operate telescopes on the land. Most of the lease arrangements are not specific and some are at no cost to the other organizations. The value of the no-cost leases could not be determined and is not considered significant and, accordingly, contributions have not been recorded in the financial statements.

Carnegie also leases a portion of one of its laboratories to another organization for an indefinite term. Rents to be received under the agreement are approximately \$385,100 annually, adjusted for CPI increases.

Carnegie leases land and buildings for various research departments. The monetary terms of the leases are considerably below fair value; however, these terms were developed considering other nonmonetary transactions between Carnegie and the lessors. The substance of the transactions indicates arm's-length terms between Carnegie and the lessors.

CARNEGIE INSTITUTION OF WASHINGTON

Notes to Financial Statements

June 30, 2013 and 2012

(13) Contingencies

Costs charged to the federal government under cost-reimbursement grants and contracts are subject to government audit. Therefore, all such costs are subject to adjustment. Management believes that adjustments, if any, would not have a significant effect on the financial statements.

(14) Related-Party Transactions

Carnegie recorded contributions from its trustees, officers, and directors of approximately \$1.2 million and \$2.1 million for the years ended June 30, 2013 and 2012, respectively.

A trustee of Carnegie is also the Chairman of an investment entity with which Carnegie has invested \$65.0 million and \$66.6 million in five of its investment funds, as of June 30, 2013 and 2012, respectively. Carnegie paid approximately \$0.9 million and \$1.4 million in fees to these funds for the year ended June 30, 2013 and 2012, respectively.

(15) Subsequent Events

Carnegie has evaluated subsequent events through the date the financial statements were issued, November 25, 2013.

CARNEGIE INSTITUTION OF WASHINGTON

Schedules of Expenses

Years ended June 30, 2013 and 2012

	2013			2012		
	Carnegie funds	Federal and private grants	Total expenses	Carnegie funds	Federal and private grants	Total expenses
Personnel costs:						
Salaries	\$ 21,004,408	10,094,971	31,099,379	18,880,633	11,183,836	30,064,469
Fringe benefits and payroll taxes	12,766,477	4,947,679	17,714,156	11,307,272	6,074,576	17,381,848
Total personnel costs	<u>33,770,885</u>	<u>15,042,650</u>	<u>48,813,535</u>	<u>30,187,905</u>	<u>17,258,412</u>	<u>47,446,317</u>
Fellowship grants and awards	2,845,079	1,966,595	4,811,674	2,469,819	2,141,366	4,611,185
Depreciation	10,418,739	—	10,418,739	9,724,219	—	9,724,219
General expenses:						
Educational and research supplies	2,643,746	2,917,635	5,561,381	2,256,077	2,143,555	4,399,632
Building maintenance and operation	3,268,568	667,617	3,936,185	3,945,616	550,498	4,496,114
Travel and meetings	1,582,124	1,830,098	3,412,222	1,378,970	1,960,450	3,339,420
Professional and contract services	3,043,525	1,614,813	4,658,338	3,259,866	2,067,184	5,327,050
Communications	418,455	118,154	536,609	374,296	163,438	537,734
Administrative and general	3,227,205	316,431	3,543,636	2,706,586	598,446	3,305,032
Interest	2,679,718	—	2,679,718	2,314,189	—	2,314,189
Subcontracts		8,829,721	8,829,721	—	8,737,660	8,737,660
Equipment	3,559,333	2,646,599	6,205,932	5,039,958	4,895,767	9,935,725
Fundraising expense	1,350,430	13,656	1,364,086	1,507,989	32,915	1,540,904
Total general expenses	<u>21,773,104</u>	<u>18,954,724</u>	<u>40,727,828</u>	<u>22,783,547</u>	<u>21,149,913</u>	<u>43,933,460</u>
Total direct costs	<u>68,807,807</u>	<u>35,963,969</u>	<u>104,771,776</u>	<u>65,165,490</u>	<u>40,549,691</u>	<u>105,715,181</u>
Indirect costs:						
Grants and contracts	(11,746,345)	11,746,345	—	(12,908,566)	12,908,566	—
Total costs	<u>57,061,462</u>	<u>47,710,314</u>	<u>104,771,776</u>	<u>52,256,924</u>	<u>53,458,257</u>	<u>105,715,181</u>
Capitalized scientific equipment and facilities	(4,996,886)	—	(4,996,886)	(7,646,138)	—	(7,646,138)
Total expenses	<u>\$ 52,064,576</u>	<u>47,710,314</u>	<u>99,774,890</u>	<u>44,610,786</u>	<u>53,458,257</u>	<u>98,069,043</u>

See accompanying independent auditors' report.