

**UNIVERSITY SCHOOL OF NASHVILLE**

**Financial Statements**

**June 30, 2010 and 2009**

**(With Independent Auditors' Report Thereon)**



**LATTIMORE BLACK MORGAN & CAIN, PC**  
CERTIFIED PUBLIC ACCOUNTANTS AND BUSINESS ADVISORS

# UNIVERSITY SCHOOL OF NASHVILLE

## Table of Contents

	<u>Page</u>
<b>Independent Auditors' Report</b>	<b>1</b>
<b>Financial Statements:</b>	
<b>Statements of Financial Position</b>	<b>2</b>
<b>Statements of Activities</b>	<b>3</b>
<b>Statements of Cash Flows</b>	<b>4</b>
<b>Notes to the Financial Statements</b>	<b>5 - 25</b>



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## **INDEPENDENT AUDITORS' REPORT**

**The Board of Trustees of  
University School of Nashville:**

We have audited the accompanying statement of financial position of the University School of Nashville (the "School") as of June 30, 2010, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the School's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the School as of and for the year ended June 30, 2009, were audited by other auditors whose report dated November 19, 2009 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2010 financial statements referred to above present fairly, in all material respects, the financial position of the University School of Nashville as of June 30, 2010, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Brentwood, Tennessee  
November 11, 2010

*Lattimore Black Morgan & Cain, PC*

# UNIVERSITY SCHOOL OF NASHVILLE

## Statements of Financial Position

June 30, 2010 and 2009

### Assets

	<u>2010</u>	<u>2009</u>
Cash and cash equivalents	\$ 2,523,959	\$ 1,953,794
Investments	3,387,023	2,580,932
Tuition and pledges receivable, net	195,658	223,616
Prepaid expenses	1,737	12,055
Inventories	118,305	110,385
Property, buildings and equipment, net	19,891,484	20,727,211
Permanently restricted investments	6,874,897	6,697,819
Other assets	<u>311,107</u>	<u>294,699</u>
	<u>\$ 33,304,170</u>	<u>\$ 32,600,511</u>

### Liabilities and Net Assets

Accounts payable	\$ 226,387	\$ 212,312
Accrued salaries and related benefits	938,490	860,455
Other accrued liabilities	97,931	136,357
Enrollment deposits	82,460	92,230
Deferred tuition revenue	517,456	456,967
Long-term debt	2,760,000	3,110,000
Obligation under interest rate swap	<u>228,047</u>	<u>195,533</u>
Total liabilities	<u>4,850,771</u>	<u>5,063,854</u>
Net assets:		
Unrestricted	21,187,924	20,721,533
Temporarily restricted	390,578	117,305
Permanently restricted	<u>6,874,897</u>	<u>6,697,819</u>
Total net assets	<u>28,453,399</u>	<u>27,536,657</u>
	<u>\$ 33,304,170</u>	<u>\$ 32,600,511</u>

See accompanying notes to the financial statements.

# UNIVERSITY SCHOOL OF NASHVILLE

## Statements of Activities

Years ended June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
<b>Changes in unrestricted net assets:</b>		
<b>Support and revenues:</b>		
Tuition and fees, net of financial aid, scholarships, and tuition remission totaling \$1,786,649 and \$1,708,771 in 2010 and 2009, respectively	\$ 15,262,992	\$ 14,551,153
Ancillary programs	1,158,255	1,210,737
Contributions	1,002,027	990,334
USN Association fundraising	315,737	314,689
Investment income (loss)	202,459	(476,240)
Loss on hedging activity, net	(32,515)	(96,418)
Other income	13,742	22,135
Net assets released from restrictions	<u>659,566</u>	<u>396,978</u>
<b>Total unrestricted public support and revenue</b>	<u>18,582,263</u>	<u>16,913,368</u>
<b>Operating expenses:</b>		
<b>Program services:</b>		
Instruction and student activities	10,107,073	9,869,027
Ancillary programs	1,106,585	1,129,452
Buildings, grounds and vehicle expense	2,407,791	2,426,989
Depreciation and amortization	1,363,998	1,386,227
Interest	<u>142,653</u>	<u>158,838</u>
<b>Total program services</b>	<u>15,128,100</u>	<u>14,970,533</u>
<b>Supporting services:</b>		
General administration	2,059,346	1,921,407
Development, alumni and communications	664,984	589,367
USN Association activities and fundraising expense	<u>263,442</u>	<u>260,222</u>
<b>Total supporting services</b>	<u>2,987,772</u>	<u>2,770,996</u>
<b>Total expenses</b>	<u>18,115,872</u>	<u>17,741,529</u>
<b>Increase (decrease) in unrestricted net assets</b>	<u>466,391</u>	<u>(828,161)</u>
<b>Changes in temporarily restricted net assets:</b>		
Contributions	199,121	83,379
USN Association fundraising	15,018	17,409
Investment income (loss)	718,700	(857,800)
Net assets released from restrictions	<u>(659,566)</u>	<u>(396,978)</u>
<b>Increase (decrease) in temporarily restricted assets</b>	<u>273,273</u>	<u>(1,153,990)</u>
<b>Changes in permanently restricted net assets:</b>		
Contributions	123,589	37,043
USN Association fundraising	<u>53,489</u>	<u>48,331</u>
<b>Increase in permanently restricted assets</b>	<u>177,078</u>	<u>85,374</u>
<b>Increase (decrease) in net assets</b>	<u>916,742</u>	<u>(1,896,777)</u>
<b>Net assets at beginning of year</b>	<u>27,536,657</u>	<u>29,433,434</u>
<b>Net assets at end of year</b>	<u>\$ 28,453,399</u>	<u>\$ 27,536,657</u>

See accompanying notes to the financial statements.

# UNIVERSITY SCHOOL OF NASHVILLE

## Statements of Cash Flows

Years ended June 30, 2010 and 2009

	<u>2010</u>	<u>2009</u>
<b>Cash flows from operating activities:</b>		
Increase (decrease) in net assets	\$ <u>916,742</u>	\$ <u>(1,896,777)</u>
Adjustments to reconcile increase (decrease) in net assets to cash flows provided by operating activities:		
Depreciation and amortization	1,363,998	1,386,227
Bad debt expense	45,352	78,340
Loss on disposal of equipment	20,513	-
Change in cash value of life insurance policy	(37,165)	-
Net (gain) loss on investments	(921,159)	1,374,976
Loss on hedging activity	32,514	96,418
Contributions permanently restricted for investment in endowment	(177,078)	(85,374)
(Increase) decrease in operating assets:		
Tuition and pledges receivable	(17,394)	(111,025)
Prepaid expenses	10,318	(3,936)
Inventories	(7,920)	2,440
Other assets	(22,134)	9,273
Increase (decrease) in operating liabilities:		
Accounts payable	14,075	(76,671)
Accrued salaries and related benefits	78,036	(451,606)
Other accrued liabilities	(38,426)	869
Enrollment deposits	(9,770)	18,687
Deferred tuition revenue	<u>60,489</u>	<u>4,046</u>
Total adjustments	<u>394,249</u>	<u>2,242,664</u>
Net cash provided by operating activities	<u>1,310,991</u>	<u>345,887</u>
<b>Cash flows from investing activities:</b>		
Purchases of buildings and equipment	(543,058)	(828,664)
Proceeds from sale of investments	422,639	1,904,868
Purchases of investments	<u>(447,485)</u>	<u>(1,996,555)</u>
Net cash used by investing activities	<u>(567,904)</u>	<u>(920,351)</u>
<b>Cash flows from financing activities:</b>		
Proceeds from contributions for investment in endowment	177,078	85,374
Proceeds from contributions for investment in property, buildings and equipment	-	15,263
Payments of long-term debt	<u>(350,000)</u>	<u>(340,000)</u>
Net cash used by financing activities	<u>(172,922)</u>	<u>(239,363)</u>
Increase (decrease) in cash and cash equivalents	570,165	(813,827)
Cash and cash equivalents at beginning of year	<u>1,953,794</u>	<u>2,767,621</u>
Cash and cash equivalents at end of year	<u>\$ 2,523,959</u>	<u>\$ 1,953,794</u>

See accompanying notes to the financial statements.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

(1) Nature of activities

University School of Nashville (the "School"), a Tennessee not-for-profit corporation, is a private coeducational school for kindergarten through twelfth grade.

(2) Summary of significant accounting policies

The financial statements of the School are presented on the accrual basis. The significant accounting policies followed are described below.

(a) Accounting codification

On June 29, 2009, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards No. 168, *The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles* ("SFAS 168"). SFAS 168 is effective for periods ending after September 15, 2009 and makes the FASB *Accounting Standards Codification* ("ASC") the sole source of authoritative accounting technical literature for nongovernmental entities in the United States of America.

(b) Basis of presentation

In accordance with ASC 958, *Not-For-Profit Entities* ("ASC 958"), the School reports information regarding its financial position and activities according to three classes of net assets: unrestricted, temporarily restricted, and permanently restricted, as follows:

Unrestricted:

Undesignated - includes unrestricted resources and represents expendable funds available for support of School operations.

Board Designations:

Quasi-Endowment - unrestricted net assets designated for future purposes. This portion of unrestricted net assets may be expended as authorized by the Board of Trustees Investment and Spending Policy or by Board action.

USN Association - unrestricted net assets resulting from USN Association activities.

Campaign resources - unrestricted net assets designated for future capital and endowment campaign expenses.

Debt repayment - unrestricted net assets in the form of capital campaign receivables and collections to be used to repay outstanding debt.

Deferred compensation - unrestricted net assets deposited in a deferred compensation account, not yet vested by the employee.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

**Plant reserve - unrestricted net assets designated for future facility improvements and maintenance.**

**Invested plant - resources expended for plant, including land and equipment, less related debt.**

**Employee benefits - unrestricted net assets designated for future employee benefit expenses.**

### **Temporarily restricted:**

**These contributions are restricted by the donor for a specific purpose. These restrictions include but are not limited to the Morgan Foundation Lower School Faculty Development and the McMullan Memorial Scholarship funds.**

**Permanently restricted endowment market gains and losses - net market gains resulting from the investment of permanently restricted net assets. This portion of temporary restricted net assets may be expended as authorized by the Board of Trustees Investment and Spending Policy for the purpose stipulated by the donor.**

### **Permanently restricted:**

**Endowment Fund - includes net assets subject to donor-imposed stipulations that they be maintained permanently by the School. Generally, the donors of these assets permit the School to use all or part of the income earned on related investments for general or specific purposes.**

### **(c) Cash equivalents**

**The School considers all highly liquid investments with original maturities of less than three months to be cash equivalents.**

### **(d) Investments and investment income**

**Investments in marketable securities and other equity interests with readily determinable fair values and all investments in debt securities are reported at their fair values in the statement of financial position. Investments in real estate investment funds, hedge funds and private equity funds are reported at their estimated fair values as reported by Diversified Trust Company.**

**Investment income shown in the statement of activities includes interest, dividends, and realized and unrealized gains and losses, net of investment expenses. Investment income is reported in the period earned as an increase in unrestricted net assets unless the use of the assets received is limited by donor-imposed restrictions. Investment income that is restricted by the donor is reported as an increase in unrestricted net assets if the restrictions are met or expire in the year in which the income is recognized. All other donor-restricted investment income is reported as an increase in temporarily restricted net assets depending on the nature of the restrictions.**



# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

(e) Tuition receivables and credit policies

The School reports tuition receivables, net of an allowance for doubtful accounts, at the amount which represents management's estimate of the amount that ultimately will be realized. The School reviews the adequacy of its allowance for uncollectible accounts on an ongoing basis, using historical payment trends, as well as review of specific accounts, and makes adjustments in the allowance as necessary. Late fees and interest are recorded when earned. Delinquent accounts receivable are charged off to the allowance when, in management's opinion, all collection efforts have been exhausted. Provision for uncollectible accounts is classified as a general administration expense and amounted to \$45,352 and \$78,340 in 2010 and 2009, respectively.

(f) Pledges receivable

Unconditional promises to give that are expected to be collected within one year are recorded at their net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of estimated future cash flows. The discounts on those amounts are computed using a risk-adjusted discount rate. Amortization of the discount is included in contribution revenue. Conditional promises to give are not included as support until such time as the conditions are substantially met.

(g) Inventories

Bookstore and other inventories are reported at the lower of cost (first-in, first-out method) or market.

(h) Property, buildings and equipment

Property, buildings and equipment are reported at cost. Depreciation is provided under the straight line method based on estimated service lives of 3 to 10 years for equipment and 10 to 30 years for buildings and improvements. Expenditures for maintenance and repairs are expensed when incurred. Expenditures for renewals or betterments are capitalized. When property is retired or sold, the cost and the related accumulated depreciation are removed from the accounts, and the resulting gain or loss is included in unrestricted net assets. Depreciation expense and costs of maintenance and repairs are classified under program services, since the amounts applicable to supporting services are considered insignificant.

(i) Loan costs

Loan costs are amortized on a straight-line basis over the scheduled repayment period of the related debt and are included in other assets in the statement of financial position. Unamortized loan costs amounted to \$69,189 and \$74,915 at June 30, 2010 and 2009, respectively. Amortization expense amounted to \$5,726 in 2010 and 2009 and is scheduled to be \$5,726 in each of the next 12 years and \$500 thereafter when the loan costs are fully amortized.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

(j) Deferred tuition revenue

Deferred tuition revenue represents advance tuition payments for the upcoming academic year. Such amounts are recognized as revenues in the year to which the payments relate.

(k) Enrollment deposits

New incoming students are required to make an enrollment deposit which is applied to the student's last bill of the first year of enrollment.

(l) Accounting for derivatives

The School utilizes a derivative financial instrument to manage its interest rate exposure by reducing the impact of fluctuating interest rates on its debt service requirements. Derivatives are recognized as either assets or liabilities in the statement of financial position at fair value. Changes in the fair value of derivatives are recognized currently in the statement of activities as a gain or loss on hedging activities.

(m) Tuition and ancillary program revenue recognition

Student tuition and educational fees are recorded as revenues during the year the related academic services are rendered during the school year which generally runs from August to June. Deposits received for tuition for subsequent school years and enrollment deposits made by new incoming students are recorded as deferred revenue until earned.

Ancillary program revenues represents revenue from after school programs, bookstore sales, camps and other related activities and are recognized as revenue when the materials are sold or as the services are rendered.

(n) Financial aid, scholarships and tuition remission

Tuition and fees that reflect the School's normal tuition charges and additional fees for all students are presented net of financial aid, scholarships and tuition remission. Scholarships, given on the basis of financial need and/or academic performance, are netted against tuition and fees. Employees with continuous service prior to the 1994 - 1995 school year receive a tuition remission benefit for dependents.

(o) Contributions and support

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and nature of any donor restrictions.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

Contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are restricted by the donor for future periods or for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset classes. When a restriction is fulfilled (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted and reported in the statement of activities as net assets released from restrictions. However, if a restriction is fulfilled in the same time period in which the contribution is received, the support is reported as unrestricted.

The School reports any gifts of equipment or materials as unrestricted support unless explicit donor restrictions specify how the assets must be used. Gifts of long-lived assets with explicit restrictions as to how the assets are to be used or funds restricted for the acquisition of long-lived assets are reported as restricted support. Expirations of donor restrictions are recognized when the donated or acquired long-lived assets are placed in service.

(p) Income taxes

The School is exempt from federal income taxes under the provisions of Internal Revenue Code Section 501(c)(3), and, accordingly, no provision for income taxes is included in the financial statements.

The School changed its accounting for uncertainty in income taxes as of July 1, 2009 as a result of adopting new principles required by generally accepted accounting principles. Under the new accounting principles, a tax position is recognized as a benefit only if it is “more likely than not” that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the “more likely than not” test, no tax benefit is recorded. The change had no material effect on the School’s financial statements.

As of June 30, 2010, the School has accrued no interest and no penalties related to uncertain tax positions. It is the School’s policy to recognize interest and/or penalties related to income tax matters in income tax expense.

The School files a U.S. Federal information tax return. The School is currently open to audit under the statute of limitations by the Internal Revenue Service for the years ended after June 30, 2006.

(q) Advertising and promotion costs

Advertising and promotion costs are expensed as incurred.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

(r) Long-lived assets

Management evaluates the recoverability of the investment in long-lived assets on an ongoing basis and recognizes any impairment in the year of determination. It is reasonably possible that relevant conditions could change in the near term and necessitate a change in management's estimate of the recoverability of these assets.

(s) Use of estimates

The preparation of financial statements in conformity with 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 and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(t) Events occurring after reporting date

The School has evaluated events and transactions that occurred between June 30, 2010 and November 11, 2010 which is the date that the financial statements were available to be issued, for possible recognition or disclosure in the financial statements. No such events or transactions were noted requiring recognition or disclosure in the financial statements.

(3) Credit risk and other concentrations

Financial instruments that potentially subject the School to concentrations of credit risk consist of cash balances, certificates of deposit, money market accounts and investments.

Cash balances are maintained at two financial institutions that are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000 for each account. The federally insured limits have temporarily been increased from \$100,000 to \$250,000 per depositor through December 31, 2013. The aggregate balances per bank exceeded the FDIC limit by approximately \$2,200,000 and \$1,600,000 at June 30, 2010 and 2009, respectively.

The School also maintains investment balances at various brokerage and investment companies. These investments consist of cash and various stocks, bonds, real estate and hedge funds. Generally, they are not insured by the FDIC or any other government agency and are subject to investment risk, including the risk of loss of principal. Investors are provided limited protection by the Securities Investor Protection Corporation (SIPC). SIPC covers investor losses, in some cases, attributable to bankruptcy or fraudulent practices of brokerage firms.

The School serves students from Nashville and surrounding communities. Accordingly, substantially all pledges and tuition receivables are due from residents of those communities.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

### (4) Fair value measurements

FASB ASC 820, *Fair Value Measurements and Disclosures*, provides the framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. 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 under FASB ASC 820 are described below:

**Level 1 -**Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the School 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 that 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 asset's or liability's 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 need to maximize the use of observable inputs and minimize the use of unobservable inputs.

The following is a description of the valuation methodologies used for asset and liability measurement at fair value. There have been no changes in the methodologies used at June 30, 2010 and 2009.

- (i) *Marketable equity securities, corporate bonds and government securities:* Valued at the closing price reported on the active market on which the individual securities are traded.
- (ii) *Mutual and fixed income funds:* Valued at the net asset value of shares held by the School at year end based on a quoted price in an active market.
- (iii) *Hedge funds:* The School invests in a fund that uses derivative financial instruments to hedge against adverse changes in interest rates and foreign exchange rates. The underlying investments of the derivative fund are valued by the trustee/custodian based on the last prior sales price on the principal board of trade or other contracts market or by quotations from the contra party bank.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

- (iv) *Private equity investment funds:* Valued at fair value based on the beginning of year value of the School's interest plus actual contributions and allocated investment income less actual distributions and allocated administrative expenses.
- (v) *Life insurance policies:* Valued at the cash value of the underlying insurance policies.
- (vi) *Interest rate swaps:* The fair values of interest rate swaps are determined using the market standard methodology of netting the discounted future fixed cash payments (or receipts) and the discounted expected variable cash receipts (or payments). The variable cash receipts (or payments) are based on an expectation of future interest rates (forward curves) derived from observable market interest rate curves.

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

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

The following tables set forth, by level within the fair value hierarchy, the School's financial instruments at fair value as of June 30, 2010 and 2009:

	<u>Fair Value Measurements as of June 30, 2010 using the following inputs</u>			
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
<b>Investments:</b>				
<b>Equity securities:</b>				
Growth	\$ 2,799,173	\$ -	\$ -	\$ 2,799,173
International	<u>1,745,337</u>	<u>-</u>	<u>-</u>	<u>1,745,337</u>
Total equity securities	4,544,510	-	-	4,544,510
<b>Bonds and fixed income funds:</b>				
Cash	92,531	-	-	92,531
Asset-backed	789,533	-	-	789,533
Corporate-backed	1,407,764	-	-	1,407,764
Mortgage-backed	183,273	-	-	183,273
International government	793,160	-	-	793,160
U.S. government	<u>400,621</u>	<u>-</u>	<u>-</u>	<u>400,621</u>
Total fixed income funds	3,666,882	-	-	3,666,882
Money market funds	1,564,335	-	-	1,564,335
Real estate investment funds	267,324	-	-	267,324
Private equity investment funds	-	-	148,995	148,995
Hedge fund residual	-	-	16,335	16,335
Cash value of life insurance	<u>-</u>	<u>53,539</u>	<u>-</u>	<u>53,539</u>
Total investments	\$ <u>10,043,051</u>	\$ <u>53,539</u>	\$ <u>165,330</u>	\$ <u>10,261,920</u>
<b>Obligation under interest rate swap</b>	\$ <u>-</u>	\$ <u>(228,047)</u>	\$ <u>-</u>	\$ <u>(228,047)</u>

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

### Fair Value Measurements as of June 30, 2009 using the following inputs

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
<b>Investments:</b>				
Equity securities	\$ 4,255,646	\$ -	\$ -	\$ 4,255,646
<b>Fixed income funds:</b>				
Cash	56,316	-	-	56,316
Asset-backed	470,253	-	-	470,253
Corporate-backed	1,392,881	-	-	1,392,881
Mortgage-backed	45,086	-	-	45,086
International government	783,135	-	-	783,135
U.S. government	<u>515,512</u>	<u>-</u>	<u>-</u>	<u>515,512</u>
Total fixed income funds	3,263,183	-	-	3,263,183
Money market funds	1,364,550	-	-	1,364,550
Real estate investment funds	194,377	-	-	194,377
Private equity funds	-	-	97,500	97,500
Hedge fund residual	-	-	85,551	85,551
Cash value of life insurance	<u>-</u>	<u>17,944</u>	<u>-</u>	<u>17,944</u>
Total investments	<u>\$ 9,077,756</u>	<u>\$ 17,944</u>	<u>\$ 183,051</u>	<u>\$ 9,278,751</u>
<b>Obligation under interest rate swap</b>	<u>\$ -</u>	<u>\$ (195,533)</u>	<u>\$ -</u>	<u>\$ (195,533)</u>

Investments above are included in the statement of financial position at June 30, 2010 and 2009 as follows:

	<u>2010</u>	<u>2009</u>
Investments	\$ 3,387,023	\$ 2,580,932
Permanently restricted investments	<u>6,874,897</u>	<u>6,697,819</u>
Total investments	<u>\$ 10,261,920</u>	<u>\$ 9,278,751</u>



# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

The following table provides a summary of changes in fair value of the Plan's Level 3 assets for the years ended June 30, 2010 and 2009:

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)		
	Hedge Fund <u>Residual</u>	Private Equity <u>Investment</u>	<u>Total</u>
Balance at June 30, 2008	\$ 852,139	\$ 95,000	\$ 947,139
Realized gains (losses)	-	-	-
Unrealized gains (losses) relating to instruments still held at the reporting date	(35,000)	2,500	(32,500)
Purchases, sales, issuances and settlements, net	<u>(731,588)</u>	<u>-</u>	<u>(731,588)</u>
Balance at June 30, 2009	85,551	97,500	183,051
Realized gains (losses)	-	-	-
Unrealized gains (losses) relating to instruments still held at the reporting date	-	23,995	23,995
Purchases, sales, issuances and settlements, net	<u>(69,216)</u>	<u>27,500</u>	<u>(41,716)</u>
Balance at June 30, 2010	<u>\$ 16,335</u>	<u>\$ 148,995</u>	<u>\$ 165,330</u>

### (5) Investments and investment income

A summary of investments as of June 30, 2010 and 2009 is as follows:

	<u>2010</u>	<u>2009</u>
US and international equities	\$ 4,544,510	\$ 4,255,646
Bonds and fixed income funds	3,666,882	3,263,183
Money market funds	1,564,335	1,364,550
Real estate funds	267,324	194,377
Private equity funds	148,995	97,500
Hedge funds	16,335	85,551
Cash value of life insurance	<u>53,539</u>	<u>17,944</u>
	<u>\$ 10,261,920</u>	<u>\$ 9,278,751</u>

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

Investments are components of the following net asset groups at June 30:

	<u>2010</u>	<u>2009</u>
Unrestricted:		
Designated for quasi-endowment	\$ 857,034	\$ 476,604
Other	<u>2,262,156</u>	<u>2,104,328</u>
Total unrestricted	3,119,190	2,580,932
Temporarily restricted	267,833	-
Permanently restricted	<u>6,874,897</u>	<u>6,697,819</u>
	<u>\$ 10,261,920</u>	<u>\$ 9,278,751</u>

The following schedule summarizes the investment income (loss) included in the statements of activities and changes in net assets for 2010 and 2009:

	<u>2010</u>	<u>2009</u>
Interest and dividend income	\$ 230,828	\$ 40,936
Net gain (loss) on investments	<u>690,331</u>	<u>(1,374,976)</u>
	<u>\$ 921,159</u>	<u>\$ (1,334,040)</u>

The majority of the investment holdings can be liquidated within 30 days or less. At June 30, 2010 and 2009, liquidity restrictions for 0.2% and 0.9% of the total investment holdings, respectively, permit exit on the last day of each quarter with advance notification of at least 60 days prior to the beginning of the quarter, based on the market value of the School's interest at the date redeemed. In addition, 1.5% and 1.1% of the investment holdings as of June 30, 2010 and 2009, respectively, represent capital committed to a private equity fund and cannot be liquidated at the School's discretion.

At June 30, 2010, the general partner of Oakwood Ltd (Oakwood), a hedge fund in which the School, through its outside investment manager, invested funds prior to July 1, 2007, has withheld the final distribution due from the redemption of the School's investment. The funds withheld, in the amount of \$16,335, are a portion of the approximately \$852,000 redemption requested by the School in 2008. Oakwood is holding the funds because it had invested in a fund that had some exposure to the Madoff fraud and bankruptcy case and believes it may be required to remit a portion of the funds to the bankruptcy trustee. The exposure, according to Oakwood, is less than five percent of the redemption. In management's opinion, any potential recovery by the bankruptcy court would not be material to the School's financial statements at June 30, 2010, and no loss provision has been recorded.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

**(6) Tuition and pledges receivable**

A summary of tuition and pledges receivable at June 30, 2010 and 2009 is as follows:

Tuition and other	\$ 316,281	\$ 300,830
Pledges - Capital campaign due in less than one year	-	7,377
Less: allowance for uncollectible accounts	<u>(120,623)</u>	<u>(84,591)</u>
Net tuition and pledges receivable	<u>\$ 195,658</u>	<u>\$ 223,616</u>

**(7) Buildings and equipment**

Buildings and equipment at June 30, 2010 and 2009, consisted of the following:

	<u>2010</u>	<u>2009</u>
Land	\$ 2,814,767	\$ 2,814,767
Buildings and improvements	26,636,511	26,576,736
Equipment	4,379,000	4,247,239
Construction in progress	<u>219,276</u>	<u>-</u>
	34,049,554	33,638,742
Accumulated depreciation	<u>(14,158,070)</u>	<u>(12,911,531)</u>
Property and equipment, net	<u>\$ 19,891,484</u>	<u>\$ 20,727,211</u>

At June 30, 2010, the School had construction contracts related to the facilities mentioned above. These contracts, totaling approximately \$600,000, are to be paid at various stages of completion through fiscal year 2011.

The School has retainage related to construction projects of approximately \$10,000 at June 30, 2010 which is included in accounts payable.

**(8) Long term debt**

On August 19, 2002, the Industrial Development Board of the Metropolitan Government of Nashville and Davidson County (the "IDB") issued \$8,000,000 of twenty-year Educational Facilities Revenue Refunding and Improvement Bonds (the "Bonds"). Net proceeds of the bond issue were loaned to the School to refinance outstanding debt and to finance the acquisition, construction and equipping of improvements to the campus. The note is secured by an irrevocable direct-pay Letter of Credit. Payments of interest only are due monthly, with scheduled principal payments due through August 2022. The Bonds may be prepaid without penalty. During 2010 and 2009, the School prepaid \$350,00 and \$340,000, respectively, of the Bonds which, in accordance with the applicable loan agreement, eliminated the scheduled principal maturities through 2019.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

A summary of future maturities of long-term debt as of June 30, 2010 is as follows:

<u>Year</u>	<u>Amount</u>
2019	\$ 90,000
2020	845,000
2021	890,000
2022	<u>935,000</u>
	<u>\$ 2,760,000</u>

The refunding bonds are also subject to the provisions of a remarketing agreement. Should the School be unable to renew the letter of credit, comply with the terms of the remarketing agreement, or comply with other provisions of the bond indenture, the principal payments under the refunding bonds could be accelerated or penalties could be assessed to the School.

The School has entered into an interest rate swap agreement with a bank for the purpose of hedging its interest rate risk on its outstanding bond issue and fixing the interest rate at 3.51%. The fair value of the School's swap obligation amounted to \$228,047 and \$195,533 at June 30, 2010 and 2009, respectively. The swap agreement terminates in August 2017, has an original notional amount of \$3,950,000 and a current notional amount of \$2,678,000 at June 30, 2010.

### (9) Retirement and deferred compensation plans

The School sponsors a defined contribution retirement plan covering all full-time employees. The School makes matching contributions to the plan based on the employees' participation election, up to 5% of each participant's salary. The School's policy is to fund retirement costs accrued. Total expense recognized by the School under the plan amounted to \$414,478 and \$400,903 for the years ended June 30, 2010 and 2009, respectively.

Effective June 30, 2004, the School entered into a deferred compensation arrangement with its Director. The arrangement consists of an eligible plan under Section 457(b) of the Code, and an ineligible plan under Section 457(f) of the Code. Eligible plan contributions vest when made; ineligible plan contributions and related earnings vest only if the director's employment term continues through age 62.

The School has also entered into a similar arrangement with another key employee. This plan qualifies as an eligible plan under Section 457(b) of the Code. Contributions to this plan vest when made, provided the employee remains a full-time employee of the School.

The assets in these plans are held by the School, subject to the claims of its general creditors. As of June 30, 2010 and 2009, assets of \$241,917 and \$219,785, respectively, are included in other assets on the statement of financial position and are reported based on the current fair value of the underlying investments. Related liabilities, adjusted each year to the amount of the vested and unvested balance, of \$241,917 and \$169,773 are included in accrued salaries and related benefits with the corresponding expense recognized in general administration for the years ended June 30, 2010 and 2009, respectively.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

Total deferred compensation charged to expense amounted to \$81,048 and \$31,590 for the years ended June 30, 2010 and 2009, respectively.

**(10) USN Association**

The USN Association is a service organization whose accounts and operations are included in the financial statements of the School. The Association's sole mission is to enhance the educational experience of the School's students by supporting the School with needed resources. A summary of the activity of the USN Association follows for the years ended June 30, 2010 and 2009:

	<u>2010</u>	<u>2009</u>
USN Association revenue	\$ <u>384,244</u>	\$ <u>380,429</u>
USN Association expenses:		
Fundraising expenses	238,485	229,820
Association activities	<u>24,957</u>	<u>30,402</u>
Total USN Association expenses	<u>263,442</u>	<u>260,222</u>
Transfers to the school		
Purchase of fixed assets	-	(8,459)
Investment proceeds used for Payne renovation	-	(50,000)
Operating contribution	(20,000)	(20,000)
Proceeds from used book sale	(15,020)	(17,409)
Proceeds from Artclectic - to endowment	(28,641)	(23,866)
Proceeds from evening classes - to endowment	<u>(24,845)</u>	<u>(24,465)</u>
Total transfers to the school	(88,506)	(144,199)
Change in USN Association assets	32,296	(23,992)
Designated USN Association - beginning of year	<u>80,096</u>	<u>104,088</u>
Designated USN Association - end of year	\$ <u>112,392</u>	\$ <u>80,096</u>

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

**(11) Net assets**

The Board of Directors has designated that certain types of support received not be used for current operating purposes. Such designation may be terminated at the discretion of the Board and does not represent donor restrictions. A summary of unrestricted net assets at June 30, 2010 and 2009 is as follows:

	<u>2010</u>	<u>2009</u>
<b>Board-designated:</b>		
Quasi-endowment fund	\$ 857,034	\$ 476,604
Campaign resources	91,418	91,418
Deferred compensation	-	50,012
Debt retirement	28,908	96,561
Plant replacement	1,284,575	1,306,341
Plant improvement	450,000	-
Invested plant	16,972,627	17,496,594
Employee benefits	150,000	-
USN Association	<u>112,392</u>	<u>80,096</u>
Total board-designated	19,946,954	19,597,626
Undesignated	<u>1,240,970</u>	<u>1,123,907</u>
	<u>\$ 21,187,924</u>	<u>\$ 20,721,533</u>

Temporarily restricted net assets as of June 30, 2010 and 2009 are available for the following purposes:

	<u>2010</u>	<u>2009</u>
Endowment	\$ 267,833	\$ -
Other	<u>122,745</u>	<u>117,305</u>
	<u>\$ 390,578</u>	<u>\$ 117,305</u>

Permanently restricted net assets are held in perpetuity with the income from assets expendable to provide financial aid and scholarships.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

### (12) Net assets released from restrictions

Temporarily restricted net assets were released from donor restrictions as follows for the years ended June 30:

	<u>2010</u>	<u>2009</u>
Purpose restriction accomplished:		
Property, plant and equipment purchases	\$ 137,243	\$ 17,058
Purchased life insurance policy	18,537	37,073
Library books	27,046	-
Other	9,269	856
Scholarship award	16,665	14,685
Shmerling faculty chair award	-	5,000
Restore endowment deficiency	199,366	-
Endowment spending rate (portion from temporarily restricted)	<u>251,440</u>	<u>322,306</u>
	<u>\$ 659,566</u>	<u>\$ 396,978</u>

The School corrected the classification of cash value of life insurance policies restricted to the endowment by the donor from temporarily restricted to permanently restricted. Net assets reclassified as of June 30, 2010 amounted to \$37,165 and is included in contributions on the statement of activities.

### (13) Endowment funds

Permanently restricted net assets includes the School's endowment funds established for the purpose of financial aid and scholarships. As required by generally accepted accounting principles, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

During 2007, the state of Tennessee adopted the Uniform Prudent Management of Institutional Funds Act ("UPMIFA"). As prescribed by UPMIFA, the School intends to preserve the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the School classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment 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 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 the School in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the School considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

- (a) The duration and preservation of the fund
- (b) The purposes of the School and the donor-restricted endowment fund
- (c) General economic conditions
- (d) The possible effect of inflation and deflation
- (e) The expected total return from income and the appreciation of investments
- (f) Other resources of the School
- (g) The investment policies of the School

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 the School to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were approximately \$199,366 as of June 30, 2009. These deficiencies generally result from unfavorable market fluctuations that occur shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that were deemed prudent by the Board of Directors. There were no such deficiencies as of June 30, 2010.

### Spending policy

The School has a policy of appropriating for distribution each year 3.5% of the most recent September 30 balance of the endowment as of the time of the annual budget approval, except as otherwise stipulated by donors for specific restricted funds. This amount should not exceed 5% nor be less than 2% of the trailing three-year average of the fiscal year end market value for the three fiscal years immediately preceding the respective budget approval.

The Malone Foundation scholarship fund stipulates an annual spending of 5% of the fair market value of the fund.

### Investment return objective, risk parameters and strategies

The School's primary objectives for the investment of its endowments are to:

- Preserve the real purchasing power of the principal, and
- Provide a reasonably stable source of perpetual financial support.

To arrive at a specific asset allocation, the Board endorses the following principles:

- Diversification is critical at both the asset and security level;
- As a perpetual fund, cash reserves should be minimal;
- The timing of initial investments will be made over an appropriate period as determined by the finance committee;
- Liquidity is important to consider for investment in securities; and
- An allocation to real estate, private equity, and other non-marketable investments may be appropriate given the possibility of both added diversification and enhanced return.



# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

Endowments should have as their objective an asset allocation sufficient to meet the spending policy herein. This allocation should include:

- Total publicly traded equity exposure not to exceed 65%.
- Up to 40% investment in fixed income securities with a portion in cash equivalents as determined appropriate by the investment subcommittee and/or finance committee.
- Up to 35% investment in real estate, private equity and hedge funds.

A summary of endowment asset composition by type of fund as of June 30, 2010 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Board-designated	\$ 857,034	\$ 267,893	\$ -	\$ 1,124,927
Donor-restricted	<u>-</u>	<u>-</u>	<u>6,874,897</u>	<u>6,874,897</u>
Total	<u>\$ 857,034</u>	<u>\$ 267,893</u>	<u>\$ 6,874,897</u>	<u>\$ 7,999,824</u>

A summary of endowment asset composition by type of fund as of June 30, 2009 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Board-designated	\$ 675,970	\$ -	\$ -	\$ 675,970
Donor-restricted (1)	<u>(199,366)</u>	<u>-</u>	<u>6,697,819</u>	<u>6,498,453</u>
Total	<u>\$ 476,604</u>	<u>\$ -</u>	<u>\$ 6,697,819</u>	<u>\$ 7,174,423</u>

- (1) The fair value of the donor-restricted endowment funds as determined, in accordance with the requirements of ASC 958, at the date of the original donors' gifts, exceeded the fair value of those funds at June 30, 2009 by \$199,366. No such deficiency existed at June 30, 2010.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

Changes in endowment net assets for the fiscal years ended June 30, 2010 and 2009 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, June 30, 2008	\$ 829,963	\$ 1,180,106	\$ 6,612,445	\$ 8,622,514
Contributions	-	-	85,374	85,374
Realized and unrealized loss	(322,608)	(857,800)	-	(1,180,408)
Amounts appropriated for expenditures	<u>(30,751)</u>	<u>(322,306)</u>	<u>-</u>	<u>(353,057)</u>
Endowment net assets, June 30, 2009	476,604	-	6,697,819	7,174,423
Contributions	125,000	-	177,078	302,078
Realized and unrealized gain	79,624	718,699	-	798,323
Reimburse endowment deficiency	199,366	(199,366)	-	-
Amounts appropriated for expenditures	<u>(23,560)</u>	<u>(251,440)</u>	<u>-</u>	<u>(275,000)</u>
Endowment net assets, June 30, 2010	\$ <u>857,034</u>	\$ <u>267,893</u>	\$ <u>6,874,897</u>	\$ <u>7,999,824</u>

### (14) Lease commitments

The School leases various office equipment under operating leases. Rent expense under these leases amounted to approximately \$40,000 in 2010 and 2009.

A summary of approximate future minimum payments under these equipment leases as of June 30, 2010 is as follows:

<u>Year ending June 30</u>	<u>Amount</u>
2011	\$ 40,000
2012	35,000
2013	24,000
2014	<u>12,000</u>
	\$ <u>111,000</u>

It is expected that in the normal course of business, leases that expire will be renewed or replaced by other leases; thus, it is anticipated that future lease payments will not be less than the expense for 2010.

# UNIVERSITY SCHOOL OF NASHVILLE

## Notes to the Financial Statements

June 30, 2010 and 2009

(15) Related party transactions

The School may receive pledges and, on occasion, purchase goods or services from individuals, companies or organizations that are affiliated with or owned, directly or indirectly, by members of the Board of Trustees.

(16) Supplemental disclosures of cash flow statement information

	<u>2010</u>	<u>2009</u>
Interest paid	\$ <u>142,653</u>	\$ <u>158,838</u>