

National Association for Music Education

**Financial Statements and
Independent Auditor's Report**

June 30, 2014 and 2013

National Association for Music Education

Index

	<u>Page</u>
Independent Auditor's Report	2
Financial Statements	
Statement of Financial Position	4
Statement of Activities	5
Statement of Functional Expenses	6
Statement of Cash Flows	7
Notes to Financial Statements	8

Independent Auditor's Report

The Board of Directors
National Association for Music Education

We have audited the accompanying financial statements of National Association for Music Education (the "Association" or "NAfME"), which comprise the statement of financial position as of June 30, 2014, and the related statements of activities, functional expenses and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of NAfME as of June 30, 2014, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited National Association for Music Education's 2013 financial statements, and we expressed an unmodified audit opinion on those audited combined financial statements in our report dated October 22, 2013. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2013, is consistent, in all material respects, with the audited financial statements from which it has been derived.

CohnReznick LLP

Bethesda, Maryland
October 19, 2014

National Association for Music Education
Statement of Financial Position
June 30, 2014 (with comparative totals for 2013)

Assets	2014						2013
	Unrestricted			Temporary restricted	Permanently restricted	Total	
	Unrestricted	Board designated	Total unrestricted				
Current assets							
Cash and cash equivalents	\$ 177,070	\$ 54,393	\$ 231,463	\$ 2,321	\$ 135	\$ 233,919	\$ 449,653
Investments - short-term	-	4,227,823	4,227,823	9,000	75,000	4,311,823	4,129,482
Accounts receivable, net	177,740	4,505	182,245	-	-	182,245	334,888
Current portion of note receivable	1,682	-	1,682	-	-	1,682	19,992
Inventories, net	145,736	-	145,736	-	-	145,736	159,820
Prepaid expenses	105,900	-	105,900	-	-	105,900	110,618
Total current assets	608,128	4,286,721	4,894,849	11,321	75,135	4,981,305	5,204,453
Noncurrent assets							
Note receivable, net of current portion	-	-	-	-	-	-	1,682
Investments - long-term	-	339,178	339,178	-	-	339,178	339,178
Land, building and equipment, net	2,732,571	-	2,732,571	-	-	2,732,571	2,851,652
Total assets	\$ 3,340,699	\$ 4,625,899	\$ 7,966,598	\$ 11,321	\$ 75,135	\$ 8,053,054	\$ 8,396,965
Liabilities and Net Assets							
Current liabilities							
Accounts payable and accrued expenses	\$ 987,680	\$ -	\$ 987,680	\$ -	\$ -	\$ 987,680	\$ 755,098
Deferred income	2,006,762	-	2,006,762	-	-	2,006,762	1,886,507
Total current liabilities	2,994,442	-	2,994,442	-	-	2,994,442	2,641,605
Commitments and contingencies	-	-	-	-	-	-	-
Net assets	346,257	4,625,899	4,972,156	11,321	75,135	5,058,612	5,755,360
Total liabilities and net assets	\$ 3,340,699	\$ 4,625,899	\$ 7,966,598	\$ 11,321	\$ 75,135	\$ 8,053,054	\$ 8,396,965

See Notes to Financial Statements.

National Association for Music Education

Statement of Functional Expenses
Year Ended June 30, 2014 (with comparative totals for 2013)

	2014						2013
	Unrestricted			Temporarily restricted	Permanently restricted	Total	
	Unrestricted	Board designated	Total unrestricted				
Operating activities							
Revenue and support							
Membership dues and contributions	\$ 4,717,563	\$ -	\$ 4,717,563	\$ 159,547	\$ -	\$ 4,877,110	\$ 4,361,300
Contributions/donations	50,878	-	50,878	200	-	51,078	61,840
Sponsorships	40,736	-	40,736	-	-	40,736	60,215
Royalty income	149,303	-	149,303	-	-	149,303	223,659
Sale of inventories	539,976	-	539,976	-	-	539,976	520,641
Meetings and conventions	747,367	-	747,367	-	-	747,367	86,259
Advertising	511,917	-	511,917	-	-	511,917	520,229
Investment income	166	617,462	617,628	2,100	-	619,728	482,121
Publication revenue	183,559	-	183,559	-	-	183,559	146,054
Rent revenue	125,032	-	125,032	-	-	125,032	101,703
Miscellaneous income	161,290	-	161,290	5,606	-	166,896	289,884
Net assets released from restrictions	167,153	-	167,153	(167,153)	-	-	-
Net assets released from designation	607,831	(607,831)	-	-	-	-	-
Total revenue and support	8,002,771	9,631	8,012,402	300	-	8,012,702	6,853,905
Expenses							
Program services:							
Governance	794,512	-	794,512	-	-	794,512	812,072
Outside advocacy	300,983	-	300,983	-	-	300,983	174,488
Constituent advocacy	390,783	-	390,783	-	-	390,783	34,113
Constituency events	1,482,719	-	1,482,719	-	-	1,482,719	379,100
Business development	697,435	-	697,435	-	-	697,435	643,444
Fundraising	3,668	-	3,668	-	-	3,668	4,889
Professional development	46,181	-	46,181	-	-	46,181	132,566
Constituency services	212,952	-	212,952	-	-	212,952	244,305
Membership	890,429	-	890,429	-	-	890,429	773,772
Communications services	1,485,199	-	1,485,199	-	-	1,485,199	1,511,130
Scholarship programs	2,000	-	2,000	-	-	2,000	2,507
Total program services	6,306,861	-	6,306,861	-	-	6,306,861	4,712,386
Supporting services:							
Administration	2,080,933	38,082	2,119,015	-	-	2,119,015	1,817,496
Fundraising and development	280,609	-	280,609	-	-	280,609	551,070
Total supporting services	2,361,542	38,082	2,399,624	-	-	2,399,624	2,368,566
Total expenses	8,668,403	38,082	8,706,485	-	-	8,706,485	7,080,952
Changes in net assets before nonoperating activities	(665,632)	(28,451)	(694,083)	300	-	(693,783)	(227,047)
Provision for income tax	2,965	-	2,965	-	-	2,965	6,900
Changes in net assets	(668,597)	(28,451)	(697,048)	300	-	(696,748)	(233,947)
Net assets, beginning	1,014,854	4,654,350	5,669,204	11,021	75,135	5,755,360	5,989,307
Net assets, end of year	\$ 346,257	\$ 4,625,899	\$ 4,972,156	\$ 11,321	\$ 75,135	\$ 5,058,612	\$ 5,755,360

See Notes to Financial Statements.

National Association for Music Education

Statement of Functional Expenses
Year Ended June 30, 2014 (with comparative totals for 2013)

Expenses	Program services										Supporting services					Total - 2014	Total - 2013
	Governance	Outside Advocacy	Constituent Advocacy	Constituency Events	Business Development	Fundraising	Professional Development	Constituency Services	Membership	Communication Services	Scholarship Programs	Total program	Administration	Fundraising & Development	Total supporting services		
Salaries	\$ 250,509	\$ 153,856	\$ 149,711	\$ 174,007	\$ 197,205	\$ 1,862	\$ 21,538	\$ 91,503	\$ 295,824	\$ 278,249	\$ -	\$ 1,614,264	\$ 952,841	\$ 44,944	\$ 997,785	\$ 2,612,049	\$ 2,466,764
Fringe benefits	46,470	37,245	36,242	41,381	47,740	449	5,213	22,152	71,612	67,359	-	375,863	230,661	10,879	241,540	617,403	590,968
Travel	287,862	8,809	9,329	653,842	40,523	25	1,104	19,224.00	11,139	11,995	-	1,043,852	40,041	11,858	51,899	1,095,751	434,479
Annual professional dues	-	2,123	1,275	-	690	-	-	-	-	496	-	4,584	5,020	-	5,020	9,604	4,812
Membership dues expenses	-	-	-	-	-	-	-	-	8,741	-	-	8,741	45,000	-	45,000	53,741	-
Meetings, conventions and conferences	67,841	1,626	9,272	375,126	6,450	-	-	1,256	-	-	-	461,571	9,918	25,017	34,935	496,506	242,005
Cost of goods sold	285	6,410	61,594	13,687	82,141	249	-	381	5,297	(4,866)	-	165,178	709	2,117	2,826	168,004	128,107
Professional services/consultants	11,386	-	-	24,737	173,818	-	-	-	3,700	35,735	-	249,376	250,455	4,000	254,455	503,831	281,757
Outside support	945	-	-	90	7,458	-	973	1,500	25	9,071	-	20,062	150	25	175	20,237	64,277
Production and printing	8,888	20,435	50,156	45,452	15,405	203	45	10,449	60,494	749,732	-	961,259	8,874	13,164	22,038	983,297	865,455
Membership promotion and retention	-	-	-	-	-	-	-	-	116,415	-	-	116,415	-	-	-	116,415	89,219
Promotion, printing and publicity	4,610	8,680	6,400	31,991	19,904	200	9,310	2,590	8,160	16,280	-	108,125	301	3,270	3,571	111,696	162,214
Postage and mailings	1,555	577	11,120	6,168	27,419	15	309	6,169	84,657	124,293	-	262,282	19,159	674	19,833	282,115	341,627
Telephone	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	468
State sales tax	-	-	-	-	-	-	-	-	-	-	-	-	17	-	17	17	-
Bad debts	-	-	-	-	-	-	-	-	55,412	21,218	-	76,630	-	-	-	76,630	4,239
Management fees	18,000	6,225	1,553	47,435	3,851	-	-	25,060	62,573	17,368	-	182,065	113,667	9,307	122,974	305,039	251,551
Awards, scholarships, and grants	127	-	-	1,041	4,259	-	-	-	1,443	500	2,000	9,370	-	29	29	9,399	22,049
Overhead	68,533	54,931	54,131	62,126	70,407	665	7,689	32,668	104,937	99,343	-	555,430	313,709	16,048	329,757	885,187	740,250
Other	27,501	66	-	5,636	165	-	-	-	-	58,426	-	91,794	128,493	139,277	267,770	359,564	390,711
Total expenses	\$ 794,512	\$ 300,983	\$ 390,783	\$ 1,482,719	\$ 697,435	\$ 3,668	\$ 46,181	\$ 212,952	\$ 890,429	\$ 1,485,199	\$ 2,000	\$ 6,306,861	\$ 2,119,015	\$ 280,609	\$ 2,399,624	\$ 8,706,485	\$ 7,080,952

National Association for Music Education

Statement of Cash Flows
Year Ended June 30, 2014 (with comparative totals for 2013)

	2014	2013
Cash flows from operating activities		
Change in net assets	\$ (696,748)	\$ (233,947)
Adjustments to reconcile changes in net assets to net cash used in operating activities:		
Bad debt expense	76,630	4,239
Depreciation	245,072	212,377
Realized gain on investments	(233,146)	(74,504)
Unrealized gain on investments	(293,236)	(223,380)
Impairment on investments	75,000	-
Changes in assets (increase) decrease in:		
Accounts and notes receivable	76,013	(86,692)
Inventories	14,084	(23,236)
Prepaid expenses and other	4,718	(152,408)
Changes in liabilities increase (decrease) in:		
Accounts payable and accrued expenses	232,582	(140,709)
Deferred income	120,255	268,035
	<u>(378,776)</u>	<u>(450,225)</u>
Net cash used in operating activities		
Cash flows from investing activities		
Purchases of property and equipment	(125,991)	(281,416)
Proceeds from sales of investments	3,362,970	3,539,418
Purchase of investments	(3,093,929)	(2,804,330)
Loan advances	-	(20,000)
Proceeds from payment of loan advances	19,992	24,173
	<u>163,042</u>	<u>457,845</u>
Net cash provided by investing activities		
Net (decrease) increase in cash and cash equivalents	(215,734)	7,620
Cash and cash equivalents, beginning of year	<u>449,653</u>	<u>442,033</u>
Cash and cash equivalents, end of year	<u>\$ 233,919</u>	<u>\$ 449,653</u>
Supplemental disclosure of cash flow information		
Income taxes paid	<u>\$ 3,451</u>	<u>\$ 6,900</u>
Significant non-cash investing and financing activities		
Construction in progress transferred to property and equipment	<u>\$ -</u>	<u>\$ 319,423</u>

See Notes to Financial Statements.

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

Note 1 - Organization and purpose

Nature of operations

The National Association for Music Education (the "Association" or "NAfME"), a non-profit corporation located in Reston, Virginia, was organized April 12, 1907 under the laws of the state of Iowa for the specific purpose of the advancement of music education.

NAfME serves as leader and spokesperson for music education in the United States. Its members are engaged in music teaching or other music education work at institutional levels from preschool through college and university. The goals of NAfME include:

- Comprehensive music programs in all schools.
- Involvement of people of all ages in learning music.
- High-quality preparation of teachers.
- Use of the most effective techniques and resources in music instruction.

NAfME's significant programmatic areas include:

Governance

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

Advocacy and public affairs

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

Membership

The NAfME membership program is involved in producing and mailing membership promotion materials, mailing membership notices to the Association's more than 135,000 members (including active, retired, pre-service music teachers and honor students), collection and tracking of national, state and student chapter dues, and maintaining all

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

membership records and data. Other important functions include the distribution of membership information and management of services designed to be of benefit to members.

Music educators journal/teaching music - periodicals

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

Meetings and conventions

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

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

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

- Meetings of the NAfME National Assembly (officers from the Federated State Associations, the geographic divisions of the Association, and NAfME Societies and Councils).
- Meetings of the National Executive Board.
- Meetings and conventions held independently by the Federated State Associations, but to which NAfME sends Board Officers.
- Meetings and conventions held by the geographic divisions of the Association, hosted by a Federated State Association, and cosponsored by NAfME.

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

- Informational seminars on a variety of special topics (e.g., nonprofit tax requirements and budgeting, copyright issues) for specific subgroups of the Association or specific groups served by the Association.

Scholarship and grant programs

NAfME administers scholarship programs that support and advance the mission to encourage the study and making of music by all; these include the Shannon Kelly Kane Fund and the Harley Scholarship fund. The Shannon Kelly Kane Fund provides two \$1,000 scholarships annually and Harley Scholarship Fund provides one scholarship. Four grants are awarded annually as part of the NAfME Tri-M Music Honor Society Chapter of the Year program. Grants are to be used for musically enriching experience that benefits the school/chapter. Two \$1,000 grants are awarded to the Chapter of the Year in the Senior and Junior Division; Runner-Ups are awarded \$800 for Senior Division and \$400 for Junior Division. Criteria for selection are on the Tri-M website. NAfME also, from time to time, provides small grants for music education related research. These grants are distributed and monitored by the Society for Research in Music Education. In addition, NAfME entered into a partnership with Fox/Glee for the purpose of awarding a total of \$1,000,000 in grants to 73 schools across the USA. Grant awards ranged from \$10,000 to \$50,000. The funding for these grants was provided completely by Fox/Glee.

Miscellaneous programs

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

Tri-M

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

Note 2 - Summary of significant accounting policies and other matters

Basis of accounting

The financial statements have been prepared using the accrual basis of accounting. Revenue, other than contributions, is recognized when earned; expenses are recorded when the obligation is incurred. Contributions are recorded as unrestricted, temporarily restricted or permanently restricted support depending upon the existence and/or nature of any donor imposed restrictions. All donor-restricted contributions are reported initially as an increase in temporarily restricted net assets and then reclassified to unrestricted net assets when restrictions have been met.

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

Basis of presentation

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

- Unrestricted - Net assets that are not subject to donor-imposed stipulations. Revenues from sources other than contributions and investment income are reported as increases in unrestricted net assets. Designated net assets consist of unrestricted funds set aside for specific purposes by action of NAFME.
- Temporarily Restricted - Temporarily restricted net assets are subject to donor-imposed stipulations that may or will be met by the actions of the Association and/or passage of time.
- Permanently Restricted - Permanently restricted net assets are subject to donor-imposed stipulations that they be maintained permanently by the Association. Generally, the investment income is temporarily restricted until appropriated for expenditure.

The Association conforms to Statements of Financial Accounting Standards for the "Transfer of Assets to a Not-for-profit Organization or Charitable Trust That Raises or Holds Contributions for Others." This establishes standards for transactions in which an entity (the "donor") makes a contribution by transferring assets to a not-for-profit organization or charitable trust (the "recipient organization") who in accepting the assets from the donor agrees to use those assets on behalf, or transfer those assets to, another specified beneficiary. The standards require that the recipient organization recognize the fair value of the assets received from the donor. The Association accepts member dues from various members and agrees to transfer those assets to respective states.

Comparative financial information

The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Association's financial statements for the year ended June 30, 2013, from which the summarized information was derived. Certain items from the prior year financial statements have been reclassified to conform to the current year presentation.

Cash and cash equivalents

For the purposes of the statement of cash flows, the Association considers all highly liquid investments, purchased with a maturity of three months or less to be cash equivalents.

Concentration of credit risk

The Association maintains its cash, cash equivalents and investment balances in several accounts at multiple banks that are insured by the Federal Deposit Insurance Corporation ("FDIC") or the Security Investor Protection Corporation ("SIPC"). Certificates of deposit are

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

placed with a bank's Certificate of Deposit Registry Service ("CDARS") and are fully insured by the FDIC. At times, these balances may exceed the federal insurance limits; however, the Association has not experienced any losses with respect to its bank balances in excess of government provided insurance. As of June 30, 2014, management believes that no significant concentration of credit risk exists with respect to these cash, cash equivalents and investment balances.

Investments

Investments with readily determinable fair values are reflected at fair market value. Income is recognized from interest and dividends as earned. The Association maintains separate investment accounts for its endowment and similar funds. Realized and unrealized gains and losses from securities in the investment accounts are allocated to the individual endowment's fund based on the relationship of the fair value of each endowment fund to the total fair value of the investment accounts, as adjusted for additions to or deductions from these accounts. Investments in certificates of deposits and private equity with no readily determinable fair value are reported at cost.

Investment income classified as operating revenue consist of interest and dividend income on investments and any gains approved by the board of directors for use in operations (Note 4). All other realized and unrealized gains or losses are classified as Board designated activity.

The Association reports its investments in a commodity fund at fair value as determined by the investment managers. This valuation is reviewed and approved by management on a yearly basis.

Alternative Investments - Investment in Entities

The non-discretionary portion of NAFME's managed investment portfolio includes alternative investments partnerships. NAFME's objective as part of its alternative investments strategy is to mitigate risk and enhance diversification of the overall investment portfolio. Management believes that in an attempt to gain enhanced diversification, focusing on absolute return, that these alternative investments will reduce their overall portfolio investment risk and volatility and offer potential for returns that are not correlated to the traditional markets of stock and bonds. NAFME has established an investment policy and procedures statement with a maximum allowable alternative investment exposure of 15% of their overall investment portfolio. The managed futures component of the alternative investments is expected to include trading in commodities such as energy, metals, crops, livestock, currencies and financial markets. During the year ended June 30, 2014, alternative investments was comprised of investment in entities, which includes one limited liability company and one corporation.

NAFME is an investor member in Acceptd, LLC and a stockholder in Bandfind, Inc. NAFME's investment accounts for its 17% and 10% investment in Acceptd and Bandfind, Inc, respectively, under the cost method. As such the initial investment is recorded at cost and cash distribution is reported as income. Investment in entities is included in investments- long-term on the statements of financial position.

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

The Association's maximum exposure to loss is estimated to be the entire balance of its investment in entities, which includes its estimated future funding commitments. The Association has no obligation to fund liabilities of Bandfind, Inc. and Accepted beyond its investment, including loans and advances. The Association may be subject to additional losses to the extent it provides any voluntary subordinated financial support to Bandfind, Inc. and Accepted in the future.

The Association regularly assesses its investment in entities for impairment if it believes that it may not recover the carrying amount of the investment or if the investee is unable to sustain an earnings capacity that would justify the carrying amount of the investment. The Association is based on the amount that it expects to recover from the investment should it be sold or should the investee liquidate, taking into account the Association's claim on the investee's book value. A recordation of an impairment loss has no effect on the actual fair market value of the underlying property or performance of the overall investment. If the investment in entities is considered to be permanently impaired, the Association would reduce its investment balance in entities and include such reduction in investment income on the statement of activities. During the year ended June 30, 2014, impairment loss of \$75,000 was recorded to the Bandfind, Inc. investment, which reduced the investment balance to \$0.

Financial risk

The Association invests in a professionally managed portfolio that contains U.S. equity securities, mutual funds, fixed income securities, alternative investments and certificates of deposits. Such investments are exposed to various risks such as interest rate market volatility and credit risks. Due to the level of risk associated with such investments and the level of uncertainty related to the changes in the value of such investments, it is at least reasonably possible that changes in risks in the near term could materially affect investment balance and the amounts reported in the financial statements.

Inventories

Inventories consist of specialty items and publications, and are valued at the lower of cost or market. Cost is determined on a first-in, first-out basis net of obsolescence. Allowance for obsolete inventory at June 30, 2014 and 2013 was \$24,675 and \$20,283, respectively.

The Association contracts with a third party to publish, market, sell and distribute the Association's book publications. The Association receives an agreed upon royalty percentage of all revenues received on book and publication sales.

Accounts receivable

Accounts receivable are reported net of an allowance for doubtful accounts. Management's estimate of the allowance is based on historical collection experience and a review of the current status of accounts receivable. Receivables are charged to allowance when deemed uncollectible. It is reasonably possibly that management's estimate of the allowance will change. Allowance for doubtful accounts at June 30, 2014 and 2013 was \$83,337 and \$10,000, respectively.

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

Fair value of financial instruments

The Association has adopted the Fair Value Measurement topic of the Financial Accounting Standards Board ("FASB"), Accounting Standards Codification ("ASC" or "Codification").

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practical to estimate that value:

Cash and cash equivalents: Cash and cash equivalents, are carried at cost, which approximates fair value.

Investments: For securities held for investments purposes, fair values are based on quoted market prices. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Inventories: Fair value is based on lower of cost or market.

Property and equipment and depreciation

Property and equipment are recorded at cost. Expenditures for maintenance and repairs are charged to expenses as incurred while major renewals and betterments are capitalized. Upon disposal of depreciable property, the appropriate property accounts are reduced by the related cost and accumulated depreciation. The resulting gain and losses are reflected in the statement of operations. Depreciation is computed on a straight-line basis over the estimated useful lives of each asset. The Association capitalizes all property and equipment purchased with a cost of \$500 or more. Depreciation expense for the years ended June 30, 2014 and 2013 was \$245,072 and \$212,377, respectively, and is included in overhead expenses on the statement of functional expenses.

Impairment of long-lived assets

The Association reviews its long-lived assets for impairment whenever events and changes in circumstances indicate that the carrying value of an asset may not be recoverable. If the fair value is less than the carrying value of an asset, an impairment loss is recognized for the difference. No impairment loss was recognized for the years ended June 30, 2014 and 2013.

Revenue recognition

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

Membership revenue

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

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

Contributions

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

Non-cash and in-kind contributions are recorded as revenue at fair value of the items contributed.

There were no promises to give, non-cash contributions, and in-kind contributions received during the years ended June 30, 2014 and 2013.

Rental income

Rental income is recognized as rent becomes due from tenants related to property owned by NAFME. Rental payments received in advance are deferred until earned. All leases between the Association and the tenants of the property are operating leases.

Functional allocation of expenses

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

Income taxes

The Association is exempt from federal income taxes under the provision of Section 501(c)(3) of the Internal Revenue Code ("IRC"). The Association is subject to income taxes on unrelated business income, as defined by the Internal Revenue Service ("IRS"). The Association is required to file and does file tax returns with the IRS and other taxing authorities.

Federal and state income tax expense for the years ended June 30, 2014 and 2013 was \$2,965 and \$6,900, respectively, in connection with advertising income. Income tax returns filed by the Association are subject to examination by the Internal Revenue Service for a period of three years. While no other tax returns are currently being examined by the Internal Revenue Service, tax years since 2011 remain open.

The Association adopted the accounting standard on accounting for uncertainty in income taxes ("FASB ASC Topic 740-10"), which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under this guidance, the Association may recognize the tax benefit from an uncertain tax position only if it is more-likely-than-not that the tax position will be

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

sustained on examination by taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The guidance on accounting for uncertainty in income taxes also addresses de-recognition, classification, interest and penalties on income taxes, and accounting in interim periods.

Management evaluated the Association's tax positions and concluded that the Association has taken no uncertain tax positions that require adjustment to the financial statements to comply with the provisions of this guidance.

Advertising

Advertising costs are charged to activities when incurred. Advertising expense during the years ended June 30, 2014 and 2013 was \$111,696 and \$227,155, respectively.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include allowance for uncollectible receivables, and inventory obsolescence.

Reclassification

Certain reclassifications have been made to the 2013 balances to conform to the 2014 presentation.

National Association for Music Education

**Notes to Financial Statements
June 30, 2014 and 2013**

Note 3 - Cash and cash equivalents

Cash and cash equivalents consist of the following as of June 30, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Unrestricted:		
Operating		
Checking accounts and petty cash	\$ 181,343	\$ 417,699
Money Market accounts	2,691	15,132
Cash equivalents held in investment accounts	<u>47,429</u>	<u>14,666</u>
	<u>231,463</u>	<u>447,497</u>
Temporarily and Permanently restricted:		
Harley Scholarship Fund	2,321	2,021
Kane Scholarship Fund	<u>135</u>	<u>135</u>
	<u>2,456</u>	<u>2,156</u>
Total cash and cash equivalents	<u><u>\$ 233,919</u></u>	<u><u>\$ 449,653</u></u>

Note 4 - Investments

Investments consist of the following as of June 30, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Certificates of deposits (at cost)	\$ 84,000	\$ 84,000
Mutual funds	3,949,274	3,734,176
Corporate bonds	278,549	311,306
Alternative investments (at cost)	<u>339,178</u>	<u>339,178</u>
Total investments	<u><u>\$ 4,651,001</u></u>	<u><u>\$ 4,468,660</u></u>

The following summarizes the investment return and its classification in the statement of activities for the years ended June 30, 2014 and 2013:

	<u>2014</u>			<u>2013</u>
	<u>Operating</u>	<u>Board designated</u>	<u>Total</u>	
Investment income	\$ 2,266	\$ 166,080	\$ 168,346	\$ 184,237
Realized gains	-	233,146	233,146	74,504
Unrealized gains	-	293,236	293,236	223,380
Impairment loss on investment	<u>-</u>	<u>(75,000)</u>	<u>(75,000)</u>	<u>-</u>
Total	<u><u>\$ 2,266</u></u>	<u><u>\$ 617,462</u></u>	<u><u>\$ 619,728</u></u>	<u><u>\$ 482,121</u></u>

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

Alternative Investments - Investment in Entities

The Association entered into a senior secured convertible promissory note agreement with Acceptd LLC ("Acceptd") in the total amount of \$250,000. The note bore interest at 7.5% compounded annually and matured on June 8, 2017, at which time all unpaid interest and principal was due and payable. In March 2013, the Association elected to convert all outstanding principal of \$250,000 and accrued interest of \$14,178 into shares of Series A preferred stock. In addition to the note conversion, the Association purchased additional shares of Series A preferred stock for \$75,000 resulting in a total investment of \$339,178. As June 30, 2014 and 2013, investment balance in Acceptd is \$339,178.

On August 19, 2013, the Association acquired its interest in Bandfind, Inc. ("Bandfind"), through the purchase of 50 shares of outstanding capital stock, for an investment of \$75,000. As a result of management's assessment of the value of the investment in Bandfind under applicable accounting guidelines, the Association reduced its investment in Bandfind for the year ended June 30, 2014 by \$75,000. Such loss is included as a reduction of investment income in the accompanying statements of activities. At June 30, 2014, the investment balance in Bandfind is \$0.

Note 5 - Fair Value Measurement

The Association has adopted the Fair Value Measurements topic of the Codification. The guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. It also establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three levels. The following summarizes the three levels of inputs and hierarchy of fair value the Association uses when measuring fair value:

1. Level 1 inputs - quoted prices (unadjusted) in active markets for identical assets or liabilities that the Association has the ability to access;
2. Level 2 inputs - quoted prices for similar assets and liabilities in active markets, as well as interest rates and yield curves that are observable at commonly quoted intervals; and
3. Level 3 inputs - unobservable inputs for the asset or liability that are typically based on an entity's own assumptions as there is little, if any, related market activity.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the fair value measurement will fall within the lowest level input that is significant to the fair value measurement in its entirety. Management's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

The following table presents the assets measured at fair value of assets at June 30, 2014 and 2013 have been categorized in the tables below based upon the fair value hierarchy described below:

Description	Fair value measurements as of June 30, 2014 using			Balance at June 30, 2014
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
Mutual Funds:				
Closed end mutual funds	\$ 3,949,274	\$ -	\$ -	\$ 3,949,274
Fixed Income securities:				
Corporate bonds	278,549	-	-	278,549
Total fixed income securities	\$ 4,227,823	\$ -	\$ -	\$ 4,227,823

Note 6 - Board designated and restricted net assets

Board designated

The Association policies set as a goal that NAFME maintain a reserve account equaling or exceeding 100% of the annual operating budget, and is to be used as designated by the board. In 1999, the National Executive Board approved an annual \$45,000 transfer of funds from the reserve account to the NAFME operating account to alleviate current life member expenses. The transfer of these funds no longer takes place after 2013.

Activity in board designated net assets during the years ended June 30, 2014 and 2013, respectively, consist of the following:

	2014	2013
Board designated net assets		
beginning of the year	\$ 4,654,350	\$ 4,262,783
Investment income	617,462	472,844
Release from designation		
Management fees	(38,082)	(36,277)
Life member dues	-	(45,000)
Total technology expenses	(607,831)	-
Total released from designation	(645,913)	(81,277)
Board designated net assets end of year	\$ 4,625,899	\$ 4,654,350

National Association for Music Education

**Notes to Financial Statements
June 30, 2014 and 2013**

Temporarily restricted

Net assets were released from restriction by satisfying the program restrictions. During the current year, the Association set temporarily restricted funds from members in order to fund technology expenses and purchases related to their operations. Temporary restricted net assets consist of the following at June 30, 2014:

	2013	Additions	Investment gains (losses)	Released from restrictions	2014
Harly scholarship fund	\$ 8,792	\$ -	\$ 450	\$ -	\$ 9,242
Kane scholarship fund	2,229	200	1,650	(2,000)	2,079
Technology Fund	-	165,153	-	(165,153)	-
Total	\$ 11,021	\$ 165,353	\$ 2,100	\$ (167,153)	\$ 11,321

Permanently restricted

Permanently restricted net assets consist of the principal portion of the Association's donor restricted endowment funds in which the donor has stipulated that the principal be maintained intact. Unless otherwise stated by the donor, the investment income portion of

National Association for Music Education

**Notes to Financial Statements
June 30, 2014 and 2013**

the donor restricted endowment funds is classified as temporarily restricted net assets to be used for specific purposes. Permanently restricted net assets as of June 30, 2014 and 2013 consisted of the following:

	<u>2014</u>	<u>2013</u>
Endowments:		
Kane scholarship fund	\$ 65,395	\$ 65,395
Harley scholarship fund	<u>9,740</u>	<u>9,740</u>
Total	<u>\$ 75,135</u>	<u>\$ 75,135</u>

Permanently restricted net assets consist of funds to support various music related scholarships and grants.

Note 7 - Endowments

The Association's endowment consists of three individual funds established for a variety of purposes. These endowments include donor-restricted endowment funds and a fund designated by the Association to function as an endowment. As required by GAAP, net assets associated with endowment funds, including funds designated by the Association to function as an endowment, are classified based on the existence of donor imposed restrictions.

Interpretation of relevant law

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

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

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

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

The changes in endowment net assets for the years ended June 30, 2014 and 2013, and the endowment net assets at June 30, 2014 and 2013 were as follows:

	Temporarily restricted	Permanently restricted	Total
Endowment net assets at June 30, 2013	\$ 11,021	\$ 75,135	\$ 86,156
Investment net income	2,100	-	2,100
Contributions	200	-	200
Releases from restrictions	<u>(2,000)</u>	<u>-</u>	<u>(2,000)</u>
Endowment net assets at June 30, 2014	<u>\$ 11,321</u>	<u>\$ 75,135</u>	<u>\$ 86,456</u>

As of June 30, 2014 and 2013, amounts classified as permanently restricted net assets are permanently restricted either by explicit donor stipulations or by UPMIFA, and amounts classified as temporarily restricted net assets are subject to purpose restrictions and net earnings from permanently restricted funds.

Funds with deficiencies

From time to time, the fair value of assets associated with donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Association to retain as a fund of perpetual duration. In accordance with accounting principles generally accepted in the United States of America, deficiencies of this nature are reported in unrestricted net assets. There were no such deficiencies as of June 30, 2014 and 2013.

Return objectives and risk parameters

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

Strategies employed for achieving objectives

To satisfy its long-term rate of return objectives, the Association relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized/unrealized) and current yield (interest/dividends). The Association targets a

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

diversified asset allocation in order to satisfy its cash withdrawal and long-term rate-of-return objectives.

Spending policies

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

Note 8 - Land, building and equipment

The following is a summary of land, building and equipment as of June 30, 2014 and 2013:

<u>Asset Category</u>	<u>Estimated life</u>	<u>2014</u>	<u>2013</u>
Land		\$ 1,069,089	\$ 1,069,089
Building and improvements	10 - 40 years	2,323,736	2,323,736
Furniture and equipment	3 - 7 years	2,117,417	1,991,426
		<u>5,510,242</u>	<u>5,384,251</u>
Accumulated depreciation		<u>(2,777,671)</u>	<u>(2,532,599)</u>
Property and equipment, net		<u>\$ 2,732,571</u>	<u>\$ 2,851,652</u>

Note 9 - Pension plans and retirement benefits

The Association has a defined contribution retirement plan covering all employees who work over 1,000 hours in the plan year following one month of service. On an annual basis, the Association contributes 7% of participants' eligible compensation to the defined contribution retirement. For the years ended June 30, 2014 and 2013, net amounts contributed after forfeitures were \$168,733 and \$149,133, respectively.

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

Accrued vacation and sick leave

Depending on length of service and other factors, the Association's employees are entitled to paid vacation time. At June 30, 2014 and 2013, the accrued vacation leave was

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

\$299,713 and \$260,906, respectively, and is included in accounts payable and accrued expenses in the statement of financial position at June 30, 2014 and 2013.

Effective July 1, 2009, employees in good standing are entitled to be paid sick leave upon employment termination, depending on meeting certain age and years of service requirements. At June 30, 2014 and 2013, accrued sick leave was \$134,903 and \$106,736, respectively, and is included in accounts payable and accrued expenses in the statement of financial position at June 30, 2014 and 2013.

Note 10 - Operating leases

The Association has various leases for automobiles and equipment which are classified as operating leases with lease terms expiring through August 31, 2015. The leases require monthly payments ranging from \$376 to \$3,314 over the term of the lease. Total rent expense for all operating leases for the years ended June 30, 2014 and 2013 was \$118,157 and \$101,177, respectively and is included in overhead expenses on the statement of functional expenses.

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

June 30, 2015	\$	95,217
2016		<u>10,009</u>
Total	\$	<u>105,226</u>

Note 11 - Lease commitments

NAfME leases office and storage space to National Art Education Association and Metronome Software LLC under operating agreements with lease terms expiring through July 31, 2015. The leases require monthly payments ranging from \$350 to \$5,649 over the lease term. No security deposits were received for these leases. Additionally, NAfME rents parking spaces to Access Bank on a month-to-month basis and can be terminated by either party at any time. For the years ended June 30, 2014 and 2013, total rent revenue was \$125,032 and \$101,703, respectively.

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

June 30, 2015	\$	89,531
2016		14,099
2017		8,100
2018		8,100
2019		<u>8,100</u>
Total	\$	<u>127,930</u>

National Association for Music Education

Notes to Financial Statements June 30, 2014 and 2013

Note 12 - Note receivable

Effective June 25, 2010, the Association made available an interest-free line of credit to a member of the Federated State Association of Music Educators National Conference up to a total amount of \$75,000. The term of the agreement is for two years expiring July 30, 2015 and may be extended upon the written agreement of both parties. As of June 30, 2014 and 2013, the balance drawn and receivable was \$1,682 and \$21,674, respectively. Future minimum principal payments under the terms of the agreement for the year ended June 30, 2015 are \$1,682.

Note 13 - Related party

Give a note foundation

The Give a Note Foundation (the "Foundation") is a related party of NAFME. The Foundation was formed by the leadership of the Association as a separate corporation and filed their 1023 with the IRS. The Foundation's primary purpose is to support the work of NAFME by providing a source of funding to encourage the study of music education; encourage public and private financial support for the advancement of music education; support research activities aimed at educating people about the benefits of music; and providing grant support for activities that strengthen music education. Although economic interest exists between NAFME and the Foundation, the Foundation maintains a board that is independent from that of NAFME. As of and for the year ended June 30, 2014, the statement of financial position and the statement of activities for the Foundation consist of the following:

Give a Note Foundation

Statements of Financial Position June 30, 2014

	<u>2014</u>
<u>Assets</u>	
Current assets	
Cash	\$ 121,437
Contribution receivable, net	1,811
Investments	39,613
Prepaid expenses	2,295
	<hr/>
Total assets	<u>\$ 165,156</u>
<u>Liabilities and Net Assets</u>	
Net assets - unrestricted	<u>\$ 165,156</u>
	<hr/>
Total liabilities and net assets	<u>\$ 165,156</u>

National Association for Music Education

**Notes to Financial Statements
June 30, 2014 and 2013**

**Statements of Activities
Year ended June 30, 2014**

	<u>2014</u>
Revenue	
Contributions and donations	\$ 92,585
In-kind goods and services	141,218
Sales	15,930
Interest Income	82
	<hr/>
Total revenue	249,815
	<hr/>
Expenses	
Program expenses	109,910
Management and general	117,695
Fundraising	20,229
	<hr/>
Total operating expenses	247,834
	<hr/>
Change in net assets before other changes	1,981
	<hr/>
Other changes	
Unrealized gain on investments	4,582
	<hr/>
Total other changes	4,582
	<hr/>
Change in net assets	6,563
	<hr/>
Net assets, beginning of year	158,593
	<hr/>
Net assets, end of year	<u>\$ 165,156</u>

Cost sharing agreement

On April 23, 2012, NAFME entered into a cost sharing agreement with the Foundation, whereby the Foundation may share use of certain office equipment, facilities and staff service. According to the terms of the agreement, the Foundation shall reimburse NAFME, for such costs, on a monthly basis, except for the first two years, whereby NAFME has agreed to forgive all related costs incurred by the Foundation. For the years ended June 30, 2014 and 2013, total donated costs were \$141,218 and \$185,898, respectively.

Note 14 - Subsequent events

Events that occur after the balance sheet date but before the financial statements were available to be issued must be evaluated for recognition or disclosure. The effects of subsequent events that provide evidence about conditions that existed at the balance sheet

National Association for Music Education

**Notes to Financial Statements
June 30, 2014 and 2013**

date are recognized in the accompanying financial statements. Subsequent events which provide evidence about conditions that existed after the balance sheet date require disclosure in the accompanying notes. Management evaluated the activity of the Association through October 19, 2014 and concluded that no subsequent events have occurred that would require disclosure in the financial statements.