

*Financial Statements and  
Independent Auditors' Report*

**THE NICHOLAS ENDOWMENT**



*As of and for the Years Ended December 31, 2014 and 2013*

# THE NICHOLAS ENDOWMENT

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## INDEPENDENT AUDITORS' REPORT

To the Board of Trustees  
The Nicholas Endowment

We have audited the accompanying financial statements of The Nicholas Endowment (the "Endowment"), which comprise the statement of financial position as of December 31, 2014, and the related statements of activities and changes in net assets 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.

### Auditors' 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider 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.

## INDEPENDENT AUDITORS' REPORT (CONTINUED)

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Nicholas Endowment as of December 31, 2014, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### Other Matter – Prior Year Reviewed Financial Statements

The Endowment's 2013 financial statements were reviewed by us and our report thereon, dated December 19, 2014, stated we were not aware of any material modifications that should be made to those statements for them to be in accordance with accounting principles generally accepted in the United States of America. However, a review is substantially less in scope than an audit and does not provide a basis for the expression of an opinion on the financial statements.

*Haskell & White LLP*  
HASKELL & WHITE LLP

January 15, 2016  
Irvine, California

## THE NICHOLAS ENDOWMENT

### Statements of Financial Position As of December 31, 2014 and 2013

<b>ASSETS</b>	<u>2014</u>	<u>2013</u>
Assets:		
Cash and cash equivalents	\$ 736,891	\$ 388,082
Investments, at fair value (Notes 1 and 2)	<u>38,000,352</u>	<u>38,630,125</u>
Total assets	<u>\$ 38,737,243</u>	<u>\$ 39,018,207</u>
<b>LIABILITIES AND NET ASSETS</b>		
Liabilities:		
Federal excise tax liabilities	\$ -	\$ 12,806
Deferred federal excise tax liabilities	<u>141,761</u>	<u>156,039</u>
Total liabilities	<u>141,761</u>	<u>168,845</u>
Net Assets:		
Unrestricted	<u>38,595,482</u>	<u>38,849,362</u>
Total net assets	<u>38,595,482</u>	<u>38,849,362</u>
Total liabilities and net assets	<u>\$ 38,737,243</u>	<u>\$ 39,018,207</u>

See accompanying notes to financial statements and independent auditors' report.

## THE NICHOLAS ENDOWMENT

### Statements of Activities and Changes in Net Assets For the Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Investment income (Notes 1 and 2), net of investment management and custodian fees	\$ 1,374,210	\$ 5,937,715
Total net investment income	<u>1,374,210</u>	<u>5,937,715</u>
Expenses:		
Grants awarded (Note 1)	1,585,250	1,721,000
General and administrative	69,924	90,805
Federal excise tax (benefit) provision	<u>(27,084)</u>	<u>132,830</u>
Total expenses	<u>1,628,090</u>	<u>1,944,635</u>
Change in net assets	(253,880)	3,993,080
Net assets at beginning of the year	<u>38,849,362</u>	<u>34,856,282</u>
Net assets at end of the year	<u>\$ 38,595,482</u>	<u>\$ 38,849,362</u>

See accompanying notes to financial statements and independent auditors' report.

**THE NICHOLAS ENDOWMENT**

**Statements of Cash Flows  
For the Years Ended December 31, 2014 and 2013**

	<u>2014</u>	<u>2013</u>
<b>Cash flows from operating activities</b>		
Change in net assets	\$ (253,880)	\$ 3,993,080
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Net realized and unrealized losses (gains) on investments	123,153	(5,484,377)
Change in liabilities:		
Federal excise tax liabilities	<u>(27,084)</u>	<u>102,111</u>
Net cash used in operating activities	<u>(157,811)</u>	<u>(1,389,186)</u>
<b>Cash flows from investing activities</b>		
Proceeds from sale of investments	4,227,756	8,515,836
Purchase of investments	<u>(3,721,136)</u>	<u>(7,583,011)</u>
Net cash provided by investing activities	<u>506,620</u>	<u>932,825</u>
<b>Net change in cash and cash equivalents</b>	348,809	(456,361)
<b>Cash and cash equivalents, beginning of year</b>	<u>388,082</u>	<u>844,443</u>
<b>Cash and cash equivalents, end of year</b>	<u><u>\$ 736,891</u></u>	<u><u>\$ 388,082</u></u>
<i>Supplemental disclosure of cash flow information:</i>		
Cash paid during the year for federal excise taxes	<u><u>\$ -</u></u>	<u><u>\$ 30,719</u></u>

See accompanying notes to financial statements and independent auditors' report.

## THE NICHOLAS ENDOWMENT

### Notes to Financial Statements December 31, 2014 and 2013

#### 1. Nature of Operations and Summary of Significant Accounting Policies

##### *Nature of Operations*

The Nicholas Endowment (the “Endowment”) was established in 2002 to provide a perpetual base of funding to supporting organizations and charities. The Endowment awards grants in the areas of science and education, performing and visual arts, and other selected causes.

Effective January 1, 2011, the Endowment was converted from a public charity to a private foundation. With this conversion, the minimum distribution of assets is based upon an assessment of the endowment value at the end of each year. The year ended December 31, 2011 was considered a grace year and the minimum distribution of assets assessment started with the year ended December 31, 2012. The Endowment was in compliance with the minimum distribution requirement for each of the years ended December 31, 2014 and 2013.

##### *Basis of Presentation*

The financial statements of the Endowment have been prepared on the accrual basis of accounting and on the basis of unrestricted, temporarily restricted and permanently restricted net assets. As of December 31, 2014 and 2013, all of the Endowment’s net assets are unrestricted. The statements of financial position are prepared using specialized accounting principles of Accounting Standards Codification (“ASC”) 958, *Not-for-Profit Entities*.

##### *Use of Estimates*

The process of preparing financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues and gains, and expenses and losses. Such estimates primarily relate to fair value of investments that do not have readily determinable market values and unsettled transactions and events as of the date of the financial statements. Accordingly, actual results may differ from estimated amounts.

##### *Reclassifications*

Certain prior year amounts have been reclassified to conform to the current year financial statement presentation.



## THE NICHOLAS ENDOWMENT

### Notes to Financial Statements (continued) December 31, 2014 and 2013

#### 1. Nature of Operations and Summary of Significant Accounting Policies (continued)

##### *Cash and Cash Equivalents*

For purposes of reporting cash flows, cash and cash equivalents may include, bank checking accounts, money market funds and highly-liquid debt instruments with maturities of three months or less when purchased.

##### *Investments*

Investments are presented at estimated fair value. Where available and appropriate, alternative investments, which generally do not have a readily determinable fair value, are valued using fund-provided net asset values per share or ownership interest (NAVs) as allowed under Financial Accounting Standards Board Accounting Standards Update No. 2009-12, *Fair Value Measurements and Disclosures (Topic 820): Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*. Fair value is discussed further in Note 2.

The ultimate liquidation of alternative investments is restricted to certain time periods and is generally limited to sell to the fund manager or distributions from the fund. Due to the inherent uncertainty of valuation of nonmarketable and restricted investments, those estimated values may differ significantly from the values that would have been used had a ready market for the securities existed and the differences could be material.

Investments are exposed to various risks such as significant world events, interest rates, credit, and overall market volatility risks. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the fair value of investments will occur in the near-term and that such changes could materially affect the amounts reported in the statements of financial position.

##### *Grants*

Grant expense is recognized in the period the grant is approved, provided the grant is not subject to significant future conditions. Conditional grants are recognized as grant expense and as a grant payable in the period in which the grantee meets the terms of the conditions. Grants payable that are expected to be paid in future years are recorded at the present value of expected future payments. At December 31, 2014 and 2013, the Endowment had no grants payable. For the years ended December 31, 2014 and 2013, grants expense totaled \$1,585,250 and \$1,721,000, respectively.

# THE NICHOLAS ENDOWMENT

## Notes to Financial Statements (continued) December 31, 2014 and 2013

### 1. Nature of Operations and Summary of Significant Accounting Policies (continued)

#### *Taxes*

The Endowment is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code (“IRC”) and corresponding state codes. However, the Endowment is subject to a federal excise tax because it is a private foundation in accordance with Internal Revenue Service regulations. The IRC imposes an excise tax on private foundations equal to 2% of net investment income, as defined by the IRC. The tax is reduced to 1% for foundations that meet certain distribution requirements under Section 4940(e) of the IRC.

The Endowment’s current provision for federal excise tax is based on a 1% rate for the years ended December 31, 2014 and 2013 while the deferred provision for federal excise tax on cumulative net unrealized gains is based on a 2% rate for the years ended December 31, 2014 and 2013. As of December 31, 2014, the Endowment had no current federal excise tax liability and an estimated deferred tax liability of \$141,761. As of December 31, 2013, federal excise tax liabilities were comprised of a current payable of \$12,806 and an estimated deferred tax liability of \$156,039.

The Endowment determines whether tax positions of the Endowment are “more likely than not” to be sustained upon examination by the applicable taxing authority based on the technical merits of the positions. As of December 31, 2014 and 2013, the Endowment has analyzed the inventory of tax positions taken with respect to all applicable income tax issues for all open tax years (in each respective jurisdiction) and has concluded that no reserve for uncertain tax positions is required.

### 2. Investments

#### *Investment Composition*

The Endowment’s investments measured at fair value as of December 31, 2014 and 2013 are comprised of the following:

**THE NICHOLAS ENDOWMENT**

**Notes to Financial Statements (continued)  
December 31, 2014 and 2013**

**2. Investments (continued)**

*Investment Composition (continued)*

	2014	2013
United States equities	\$ 12,635,718	\$ 8,739,270
Non-United States equities	8,530,336	13,856,323
Fixed income investments	7,609,972	7,319,018
Real assets mutual funds	1,109,888	-
Hedge funds	6,328,396	6,718,683
Partnerships	1,786,042	1,996,831
	\$ 38,000,352	\$ 38,630,125

At December 31, 2014 and 2013, the Endowment had commitments to contribute additional capital to its investment partnerships of approximately \$1,751,000 and \$930,000, respectively.

*Net Investment Income*

Net investment income for the years ended December 31, 2014 and 2013 is comprised of the following:

	2014	2013
Interest, dividend and mutual fund distributions	\$ 1,639,428	\$ 528,165
Operating (loss) income from partnerships	(14,506)	24,214
Net realized gains on investments sold	590,752	405,966
Net change in unrealized (losses) gains on investment	(713,905)	5,078,411
Investment management and custodian fees	(127,559)	(99,041)
	\$ 1,374,210	\$ 5,937,715

## THE NICHOLAS ENDOWMENT

### Notes to Financial Statements (continued) December 31, 2014 and 2013

#### 2. Investments (continued)

##### *Fair Value Measurements*

Fair value is defined as the price that the Endowment would receive to sell an asset, or pay to transfer a liability, in an orderly transaction between market participants at the measurement date. The Endowment utilizes a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation of an asset or liability. Inputs may be observable or unobservable and refer broadly to the assumptions that market participants would use in pricing the asset or liability. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. Unobservable inputs reflect the Endowment's own assumptions about the assumptions that market participants would use in pricing the asset or liability developed based on the best information available under the circumstances. The three-tier hierarchy of inputs is summarized below.

Level 1 - inputs are quoted prices in active markets.

Level 2 - inputs are observable, directly or indirectly.

Level 3 - inputs are unobservable and reflect assumptions on the part of management.

The following table summarizes the valuation of the Endowment's investments by their assigned three-level fair value hierarchy as of December 31, 2014 and 2013:

	2014			
	Level 1	Level 2	Level 3	Total
Equities	\$ 21,166,054	\$ -	\$ -	\$ 21,166,054
Fixed income	7,609,972	-	-	7,609,972
Real assets	1,109,888	-	-	1,109,888
Hedge funds	-	-	6,328,396	6,328,396
Partnerships	-	-	1,786,042	1,786,042
	\$ 29,885,914	\$ -	\$ 8,114,438	\$ 38,000,352

	2013			
	Level 1	Level 2	Level 3	Total
Equities	\$ 22,595,593	\$ -	\$ -	\$ 22,595,593
Fixed income	7,319,018	-	-	7,319,018
Hedge funds	-	-	6,718,683	6,718,683
Partnerships	-	-	1,996,831	1,996,831
	\$ 29,914,611	\$ -	\$ 8,715,514	\$ 38,630,125

## THE NICHOLAS ENDOWMENT

### Notes to Financial Statements (continued) December 31, 2014 and 2013

#### 2. Investments (continued)

##### *Fair Value Measurements (continued)*

The fair value of equities and corporate bonds is based on quoted prices in active markets.

The Endowment has investments in hedge funds and partnerships that are classified as Level III investments, which are collectively referred to as “alternative investments”, whose values have been estimated by the Endowment in the absence of readily ascertainable market values. The Endowment’s estimate of fair value is generally based on the NAV provided by each alternative investment fund, supported by independently audited financial statements of the alternative investment fund, when available.

Changes in Level 3 assets measured at fair value for the years ended December 31, 2014 and 2013 are as follows:

	2014						
	Balance January 1, 2014	Realized Gains (Losses)	Unrealized Gains (Losses)	Purchases	Sales	Return of Capital	Balance December 31, 2014
Hedge funds	\$ 6,718,683	\$ -	\$ 228,896	\$ -	\$ (619,183)	\$ -	\$ 6,328,396
Partnerships	1,996,831	394,114	(58,148)	234,737	(106,729)	(674,763)	1,786,042
	<u>\$ 8,715,514</u>	<u>\$ 394,114</u>	<u>\$ 170,748</u>	<u>\$ 234,737</u>	<u>\$ (725,912)</u>	<u>\$ (674,763)</u>	<u>\$ 8,114,438</u>
	2013						
	Balance January 1, 2013	Realized Gains (Losses)	Unrealized Gains (Losses)	Purchases	Sales	Return of Capital	Balance December 31, 2013
Hedge funds	\$ 6,591,373	\$ 42,426	\$ 890,905	\$ 2,000,000	\$(2,806,021)	\$ -	\$ 6,718,683
Partnerships	2,127,858	6,913	106,607	134,690	-	(379,237)	1,996,831
	<u>\$ 8,719,231</u>	<u>\$ 49,339</u>	<u>\$ 997,512</u>	<u>\$ 2,134,690</u>	<u>\$(2,806,021)</u>	<u>\$ (379,237)</u>	<u>\$ 8,715,514</u>

## THE NICHOLAS ENDOWMENT

### Notes to Financial Statements (continued) December 31, 2014 and 2013

#### 2. Investments (continued)

##### *Risks and Uncertainties*

The Endowment maintains its cash, cash equivalents, and a significant portion of its investments with high-credit quality financial institutions. At times, balances in these accounts exceed the Federal Deposit Insurance Corporation insurance limit of \$250,000 or the Securities Investor Protection Corporation insurance limit of \$500,000. The Endowment has not experienced any losses in such accounts and management does not believe there is significant risk of non-performance by these financial institutions.

To address market risk of investments, the Endowment maintains a formal investment policy that sets out performance criteria, investment guidelines and requires review of the investment managers' performances. Investments are managed by multiple investment managers, who have responsibility for investing the funds in various investment alternatives. In addition, an investment consultant is also utilized. The Endowment also has custody agreements with selected banks, which process disbursements at the direction of authorized staff and the board.

#### 3. Consulting Services

The Endowment has an agreement with a management group to receive consulting services. Under the terms of the agreement, the Endowment pays a monthly fee of approximately \$3,300 to the management group for the management of day-to-day activities and operations, as well as the provision of administrative support to the Endowment's Trustees. Consulting service fees totaled approximately \$40,000 during each of the years ended December 31, 2014 and 2013, and are included within general and administrative expenses in the accompanying statements of activities and changes in net assets.

#### 4. Related Party Transactions

The Endowment has a conflict of interest policy which covers relationships with trustees. The policy requires annual disclosures and discussion of potential conflicts at meetings, so that trustees may continue to serve the Endowment through their professional knowledge and expertise. Additionally, the policy requires a trustee to recuse him/herself from voting on matters when a potential conflict of interest may exist.

## **THE NICHOLAS ENDOWMENT**

### **Notes to Financial Statements (continued) December 31, 2014 and 2013**

#### **4. Related Party Transactions (continued)**

The Endowment has, and may continue to have, trustees who are employed by organizations that are supported by the Endowment. Total grants given to these organizations totaled \$300,000 for each of the years ended December 31, 2014 and 2013, respectively. In addition, the Endowment also maintains an investment in a partnership that is managed by an organization that employs a trustee and the fair value of this partnership investment as of December 31, 2014 is \$1,492,000 and as of December 31, 2013 is \$1,470,000.

#### **5. Subsequent Events**

Events occurring subsequent to year end have been evaluated for possible adjustment to the financial statements or disclosure through January 15, 2016.